COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

Application of Kentucky-American Water Company, a/k/a Kentucky American Water For Certificate of Convenience and Public Necessity Authorizing Construction of Kentucky River Station II ("KRS II"), Associated Facilities, and Transmission Line	))))))	Case No. 2007-00134

CITIZENS FOR ALTERNATIVE WATER SOLUTIONS
POST-HEARING BRIEF IN OPPOSITION TO ISSUANCE
OF A CERTIFICATE OF PUBLIC CONVENIENCE AND
NECESSITY TO KENTUCKY-AMERICAN WATER CO.

Comes the Intervenor Citizens for Alternative Water Solutions (CAWS), and pursuant to the January 16, 2008 Order of the Commission setting a schedule for submission of written briefs, herewith tenders this brief. For the reasons outlined below, and on the basis of the evidence and testimony in the record of this case, CAWS believes that applicant Kentucky-American Water Company (KAWC) has failed to satisfy the burden of demonstrating *entitlement* to a Certificate of Public Convenience and Necessity ("CPCN") authorizing construction of a new water treatment plant with a capacity of twenty (20) million gallons per day in Owen County on the Kentucky River at Pool 3, and approximately 160,000 linear feet of associated transmission main to transport the treated water from that plant to KAWC's facilities in Fayette County, Kentucky.

STATEMENT OF APPLICABLE LAW

On March 30, 2007, KAWC filed an application with the Public Service Commission seeking a CPCN authorizing the construction of a new water treatment plant, identified as "Kentucky River Station II" or "KRS II" as well as associated transmission lines and facilities.

As a public utility regulated by the Public Service Commission, KAWC is obligated to supply water that is "[f]rom a source reasonably adequate to provide a continuous supply of water[;] 807 KAR 5:066 Section 3(2)(c); and sufficient in quantity to "supply adequately, dependably and safely the total reasonable requirements of its customers under maximum consumption." 807 KAR 5:066 Section 10(4). Additionally, the utility is to make reasonable efforts to "prevent interruptions of service[.]" 807 KAR 5:066 Section 4(1). The utility's facilities are to be designed, constructed and operated to "provide adequate and safe service to its customers" 807 KAR 5:066 Section 7. Finally, a copy of any water shortage response plan filed with the [Environmental and Public Protection Cabinet] is required to be filed with the Commission. 807 KAR 5:066 Section 17.

Issuance of a Certificate of Public Convenience and Necessity is governed by K.R.S. 278.020(1), which states in relevant part that:

> No person, partnership, public or private corporation, or combination thereof shall commence providing utility service to or for the public or begin the construction of any plant, equipment, property, or facility for the furnishing to the public any of the services enumerated in KRS 278.010 . . . until that person has obtained from the Public Service Commission a filing of an application for a certificate that public convenience and necessity require the service or construction.

K.R.S. 278.020(1).

That a CPCN is required in this instance is clear, since among those "services enumerated in KRS 278.010" is "the purity, pressure, and quantity of water[.]" K.R.S. 278.010(13).

The determination of *when* public convenience and necessity *requires* the proposed service or construction, has been left to the Commission, in the first instance, and the courts, in the last, to *amplify*.

The Courts and the Commission have both spoken to the test to be employed in determining whether the applicant has demonstrated entitlement to a certificate. The Court in *Kentucky Utilities Co. v. Public Service Commission, Ky., 252 S.W.2d 885 (1952)* described the factors that are utilized to determine whether the applicant has met the burden of establishing that public convenience and necessity demand the proposed service or facility:

> We think it is obvious that the establishment of convenience and necessity for a new service system or a new service facility requires first a showing of a *substantial inadequacy of existing service*, involving a consumer market sufficiently large to make it economically feasible for the new system or facility to be constructed and operated.
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> Second, the inadequacy must be due either to a substantial deficiency of service facilities, beyond what could be supplied by normal improvements in the ordinary course of business; or to indifference, poor management or disregard of the rights of consumers, persisting over such a period of time as to establish an inability or unwillingness to render adequate service."
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> The above two factors have relation to the need of particular consumers for service. However, our concept of the meaning of '*public convenience and necessity,' as expressed in our decisions in previous cases, embodies the element of absence of wasteful duplication, as well as a need for service*. (Citations omitted). Therefore, a determination of public convenience and necessity requires both a finding of the need for a new service system or facility from the standpoint of service requirements, and an absence of wasteful duplication resulting from the construction of the new system or facility.

Id., at 890. (Italics added).

The dual standards of "need" and "absence of waste duplication" have been utilized consistently by the Courts and the Commission in adjudicating applications for certificates. "Duplication of facilities" means, as this Commission noted in *In the Matter of The Application of East Kentucky Power Cooperative, Inc. For A Certificate Of Public Convenience and Necessity To Construct A 138 KV Transmission Line In Rowan County, Kentucky,* (hereafter "Rowan County") Case No. 2005-00089 (August 19, 2005), that "the Commission must examine proposed facilities 'from

the standpoints of excessive investment in relation to efficiency, and an unnecessary multiplicity of physical properties.'" *Id.* at p. 5, quoting *Kentucky Utilities,* at 891.

As the Commission noted in the December 21, 2007 Order in this case:

> To obtain a CPCN, Kentucky-American must demonstrate 'the need for a new service system or facility from the standpoint of service requirements and an absence of wasteful duplication resulting from the construction of the new system or facility." *Kentucky Utilities Company v. Public Service Commission,* 252 S.W.2d 885, 890 (Ky. 1952). Wasteful duplication, Kentucky courts have held, 'embraces the meaning of an excessive investment in relation to productivity.' Id. Simply put, Kentucky-American must demonstrate that it has considered all reasonable alternatives to resolve its water supply needs and that its proposed facilities represent the most reasonable solution to those needs.

December 21, 2007 Order, Case No. 2007-00134, at pp. 1-2.

In the *Rowan County*, this Commission denied East Kentucky Power Cooperative's initial application for construction of a 138 kV transmission line, underscoring that the term "wasteful duplication of facilities" incorporates a balancing of factors, including consideration of and demonstration of *infeasibility* of other alternatives, cost, and any unique characteristics that could be affected by the proposed alternative. Finding that a new transmission corridor through the Daniel Boone National Forest would result in a wasteful duplication of facilities due to the existence of an alternative that would have been slightly *more* costly but would have utilized or paralleled an existing corridor, the certificate was denied. *Rowan County, supra,* at p.8.

The *Kentucky Utilities* Court further clarified that a consideration of whether a request for CPCN would result in a wasteful duplication of facilities requires examination of the proposed facilities from the standpoints of excessive investment in relation to efficiency, "and from the standpoint of inconvenience to the public generally, and economic loss through interference with normal uses of the land, that may result from multiple sets of right of ways [sic] and a cluttering of the land with poles and wires." *Kentucky Utilities,* 252 S.W.2d at 892.

Applying the standards enunciated in *Kentucky Utilities* and reaffirmed by this Commission in numerous decisions reviewing requests for CPCNs and in prior Orders in this proceeding, it is apparent that the applicant KAWC has failed to demonstrate entitlement to the requested certificate.

BACKGROUND

The issue of how best to meet the needs of the ratepayers of KAWC for safe and dependable water supply has been the subject of several cases before this Commission. It is, as the Chairman aptly stated at the conclusion of the supplemental hearing, an issue that must be placed in context in light of the daily unavailability of safe and dependable water for many citizens of the Commonwealth who would gladly trade the unavailability of such a supply for the enviable circumstance of two utilities vying for the right to provide such a resource under worst-case conditions.

In Case No. 93-434, which was opened on November 19, 1993 as an "[I]nvestigation into the sources of supply and future demand, including demand side management, of Kentucky-American Water Company[,]" the Commission framed the issue well in stating that:

> [t]he issue here is not sufficiency of water for health and sanitation uses. An adequate supply exists for such purposes. The real issue is whether Kentucky-American's customers should pay $50 million for a supplemental source of supply to ensure their unrestricted ability to use water during a drought of record.

March 14, 1995 Order, Case No. 93-434.

In response to a Commission Order, KAWC filed on March 21, 2001 a Report To The Public Service Commission captioned "Source of Supply and Treatment Status" which provided "a summary of the activities of Kentucky-American Water Company (KAWC) and other relevant agencies subsequent to the Kentucky Public Service Commission (PSC) Order of August 21, 1997 which directed KAWC to "take the necessary and appropriate measures to obtain sources

of supply so that the quantity and quality of water delivered to its distribution system shall be sufficient to adequately, dependably, and safely supply the total reasonable requirements of its customers under maximum consumption through the year 2020."

Among the salient points raised in that report are that:

* KAWC identified a source of supply deficit of 21 mgd during a severe drought, and a reliable production capacity deficit of 11 mgd. Report, p. 1.

* KAWC explained that subsequent to the December 9, 1999 LFUCG resolution calling for a Kentucky River solution to the region's water supply shortage, KAWC abandoned the LWC pipeline option and "pledged its support for the LFUCG's proposed program for resolution of the deficit." Report, p. 2.

* The Kentucky Water Resources Research Institute (KWRRI) 1996 analysis of the Kentucky River demonstrated that the basin deficit in the Kentucky River could be reduced from 9.727 billion gallons to 5.467 billion gallons with the installation of six valves in upstream dams that would allow the transfer of water to downstream pools. The installation of the valves and proposed valve operating plan could reduce KAWC's deficit by approximately half, to 3.038 billion gallons over the duration of the drought of record. Report pp. 3-4.[1]

* That the now-abandoned Ohio River supply project had been selected by KAWC in 1992 from over 50 alternatives as the most feasible, cost effective solution for the water supply deficits. Report p. 5.

The Report bears close scrutiny, since it outlines a series of short-term and long-term actions that KAWC committed to undertake in order to address the needs of its customers – actions which do not appear from the record to have been fully implemented. The record in this case

[1] The Commission accepted 3.489 billion gallons to be a "reasonable estimate of the magnitude of Kentucky-American's total annual water supply deficit for the planning horizon through the year 2020." Case No. 93-434, August 21, 1997 Order, p. 4.

contains little information on a number of questions identified by KAWC in that Report as needing answers, including:

* Whether the hydraulic improvements at the RRS which KAWC projected could produce an additional 5 mgd were implemented;

* The outcome of discussions with the Frankfort Electric and Plant Board to purchase finished water;[2]

* The outcome of KAWC's pursuit of modifications of the DOW permit restrictions on withdrawals from the Kentucky River under low flow conditions.

Missing also from the record is an explanation of why KAWC departed from the process outlined in the Report for addressing long-term needs. KAWC has not demonstrated that the combination of enhancements, including the mining of pools through the valve operating plan, additional capital improvements to enhance treatment capability, temporary relaxation of withdrawal permit restrictions under low-flow drought conditions, installation of temporary or permanent additions to increase storage of water at Pools 10 or 9, are inadequate to meet reasonable needs for its customers under maximum demand conditions. In the absence of a demonstration that one or more combinations of these alternatives that KAWC had itself identified as reasonable in its proposed plan of action, the construction of a new 20 mgd plant on Pool 3 cannot be shown to be needed, nor to avoid wasteful duplication of facilities.

[2] While witnesses for KAWC were dismissive of the proposal by LWC to interconnect with Frankfort in order to purchase finished water from the eastern side of the Frankfort system once LWC completes the planned interconnection to the western side of the Frankfort system, the 2001 Report identified purchase of such finished water, to the extent available, as providing "short-term treatment capacity reliability, additional system reinforcement for a growing area of KAWC's distribution system and greater system reliability for KAWC and Frankfort." Report at 27.

SUMMARY OF ARGUMENT

KAWC has failed to demonstrate entitlement to the requested certificate both because the need for additional water supply and water treatment appears to have been overestimated, and because the applicant has failed to adequately evaluate a range of both supply and demand-side measures that could address the water supply needs of its ratepayers and wholesale customers at a more modest cost and in a more flexible, step-wise manner. The evidence reflects graphically that KAWC has refused to evaluate a range of measures that, in combination, could augment available treated and raw water supply.

As will be discussed in greater detail, the record reflects KAWC's inexplicable refusal to seriously evaluate proposals that could provide additional treated water supply during peak demand conditions, and which could augment available raw water. Despite knowing for over a decade that it would face limitations in treatment capacity, and that the available supply was not adequate to meet drought-of-record demand, KAWC has (a) failed to evaluate the cost and feasibility of providing capital and in-kind engineering and other services to the Kentucky River Authority in order to expedite the completion of renovations on Dams 10 and 9 and installation of crest gates on 9; (b) failed to meaningfully engage Louisville Water Company in discussions concerning the feasibility of a joint plan to serve the water supply needs of Kentucky-American's and [Bluegrass Water Supply Commission's] customers from the Ohio River, despite LWC's repeated attempts to engage the utility that had previously signed (and never formally rescinded) a water supply contract to serve those needs;[3] [4] (c) failed to fully explore and evaluate the

[3] The Commission was on target in suggesting that discussions between Kentucky-American and Louisville Water Company regarding the feasibility of such a joint plan "would indicate the level and completeness of utility management's review of available options before embarking upon the present course of action." December 21, 2007 Order at p. 3. CAWS submits that the refusal of KAWC to engage LWC in such discussions, speaks volumes concerning the incompleteness of the "utility management's review of available options[.]"

feasibility of purchasing treated water from Versailles through an existing system interconnection; and (d) failed to explore the possibility of interconnection with Frankfort in order to purchase treated water from the Frankfort system once it is interconnected on the western side of that system with LWC. Additionally, the record reflects that KAWC has devoted scant attention to conservation or to management of unaccounted for system losses, despite admonitions from the Commission in previous cases to do so.

As this Commission noted in the December 21, 2007 Order, the "decision in this case will affect hundreds of thousands of ratepayers for decades to come[.]" Id. at 3. The approval of the requested treatment plant and associated facilities would significantly affect a generation of ratepayers, and this Commission has acted with appropriate circumspection in assuring that "no stone has been left unturned, and that all reasonable proposals have been examined[.]"

Would that KAWC had been as thorough in its exploration of reasonable alternatives. It is clear from the record that KAWC has focused exclusively on finding one supply-side option to meet all of its needs over the planning horizon, and has selected an option that will impose significant present costs on ratepayers, and has rejected a range of options that in combination could augment and expand available supply and treatment capacity sufficient to satisfy the reasonable needs of KAWC customers in a more step-wise, flexible manner and at lower cost to ratepayers.

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[4] The excuse given for the failure to have engaged LWC in discussions is mystifying, since the apparent concern for offending the KAWC's partners by engaging in discussions with LWC apparently didn't extend to concern for the effect on the BWSC of KAWC moving forward without BWSC to construct the Pool 3 project. It is clear that the so-called partnership is illusory, since what had been a proposed regional project of the BWSC has become an unaffordable option for many of the participants in BWSC, for which an infusion of $60 million in federal and state subsidies would be needed in order to buy down the BWSC involvement to a reasonable level. As is evident from intervening actions, the cities of Frankfort and others are moving forward to meet the region's needs independently of KAWC.

Having failed to demonstrate the need for the new treatment plant and associated facilities, and having failed to fully evaluate the range of alternative water demand moderation and supply augmentation measures, the CPCN should be denied.

ARGUMENT

I. KAWC HAS FAILED TO DEMONSTRATE THE NEED FOR A NEW 20 MGD TREATMENT PLANT AND ASSOCIATED FACILITIES

1. KAWC'S PROJECTED NEEDS ARE IN EXCESS OF REASONABLE ESTIMATES BASED ON HISTORIC USAGE BY KAWC CUSTOMERS

Fundamental to the question of whether the applicant for a CPCN has met the burden of demonstrating the *need* for the proposed service or supply, is the reasonableness of the demand projections.

In a CPCN proceeding, there is no penalty for overestimation of demand; in fact, there is a reward in terms of return on investment. Unfortunately, for the ratepayer, there is the penalty of rate increases to fund capacity development that might be better served through more realistic assumptions and more reasonably scaled improvements in system management and supply augmentation.

While the Commission has, in a March 14, 1995 Order, indicated that KAWC's demand projections are "within the realm of reasonableness," the Commission did not ratify *carte blanche* all projections that KAWC might generate from use of its model. In fact, the Commission also found that the assumptions of intervenors in that case that projected a lower demand were also "within the realm of reasonableness." March 14, 1995 Order, p. 5.

The Commission concluded that because all of the "demand projections in this case indicate a supply deficit under a drought of record scenario, further analysis of demand projections would be little more than an academic exercise." March 14, 1995 Order, p. 5. While in the context of

Case No. 93-434, it might have been an academic exercise, in the context of a concrete proposal to build a new 20 mgd treatment plant and associated facilities, further analysis of the reasonableness of demand projections is an essential first step compelled by the requirement that the applicant demonstrate and the Commission find that the reasonable "need" has been properly identified and that the least cost alternative has been selected from among reasonable options.

The prefiled direct testimony of Dr. Martin Solomon raised serious questions about the KAWC projections of future demand, noting that

> From 2000 to 2006, Kentucky American's maximum daily demand in normal weather increased by 140,000 gallons per day, or 0.14 mgd each year. Yet for 2006 to 2030, their projected normal daily demand increases much more dramatically, with a projected increase over the 24-year period of .58 mgd per year. This dramatic increase in projected demand is hard to fathom. The projections for drought daily maximum demand increases are likewise seemingly high with a projected annual increase of .56 mgd. Using demand increase numbers that are more in line with historic trends, the necessity for a major new capital project is even more questionable.

Solomon Direct Testimony, pp. 3-4.

In fact, as evidenced in Dr. Solomon's chart (attached to his Prefiled Direct Testimony), even *doubling* the historical annual increase in maximum daily demand from .14 mgd/year to .28 mgd/year, the value is still substantially lower (in fact slightly less that *half*) than the estimated maximum daily demand increase projected by KAWC. Utilizing reasonable demand projections more consistent with historic use trends, KAWC has not demonstrated the need for an additional 20 mgd of treated water in order to serve customers maximum reasonable demands in year 2020.

solutions to such deficit will be examined in the new docket (i.e. in this case). Case No. 2001-00117, April 19, 2007 Order, p. 1.

2. PLANNING FOR UNRESTRICTED USE DURING THE DROUGHT OF RECORD IS UNREASONABLE AND IN EXCESS OF REGULATORY OBLIGATIONS

While no party to the proceeding would dispute that it is appropriate to plan for addressing the ***reasonable*** needs of customers in the worst-case scenario, couched in terms of the "drought of record," the question of what amount of supply is "reasonable" under those circumstances is one that the Commission must weigh, and which in turn weighs heavily on this CPCN process.

CAWS believe that the Commission was correct in its Order closing case 93-434 when it stated:

> [T]he issue here is not the sufficiency of water for health and sanitation Uses. An adequate supply exists for such purposes. The real issue is whether Kentucky-American's customers should pay $50 million for a supplemental source of supply to ensure their unrestricted ability to use water during a drought of record.

March 14, 1995 Order, Case No. 93-434.

Planning for unrestricted demand in a drought of record is unreasonable, and results in the inflation of drought demand numbers that will cause wasteful expenditure of ratepayer monies to address an unrealistic goal. As Dr. Solomon commented in his testimony, (and as the Attorney General's witness argued in his opposition to the earlier Louisville pipeline project), a more realistic assumption concerning drought demand would include conservation measures.

The 2001 KAWC report on Source of Supply and Treatment Status describes the array of measures that were employed during the 1999 drought (which the report indicated was one of the worst of the century). Report p. 21. The measures employed included voluntary, and then

mandatory odd/even watering, and finally, no outdoor water use during the last two months of the drought. A drought tariff was discussed and drafted but not implemented.

Any reasonable projection for demand based on the drought of record would necessarily include such restrictions rather than planning, building (and charging ratepayers) for capacity to provide unrestricted supplies in a drought of record.

II. THE POOL 3 PROJECT WOULD CONSTITUTE A WASTEFUL DUPLICATION OF FACILITIES SINCE BOTH REASONABLE SUPPLY AND DEMAND-SIDE ALTERNATIVES HAVE NOT BEEN EXPLORED AND IMPLEMENTED

1. REASONABLE SUPPLY ALTERNATIVES HAVE NOT BEEN EXPLORED

As LFUCG argued and this Commission concurred in Case No. 2001-00117, "'[a]ny solution to the water supply deficit issue that ignores a potentially lower cost solution for KAW[C]'s ratepayers is not in the public interest.' ...Any proceeding that considers KAWC's construction of a water treatment plant on Pool 3 of the Kentucky River must consider and evaluate all other alternatives that may provide a lower cost solution." Case No. 2001-00117, October 2, 2006 Order, p. 2.

The Commission has attentively listened to the testimony and has reviewed the evidence in this case. It is apparent that virtually all studies that have been done have concluded that the KAWC plan is not the most cost-effective, and will impose costs on ratepayers that are higher than would be the case were KAWC to link to the LWC line through Frankfort, or by constructing a transmission main along the I-64 corridor. To the extent that after implementation of aggressive conservation and leak detection, and after installation of crest gates on Dam 9, there remains a deficit in treatment and supply, the Louisville Water Company option is demonstrably superior to the Pool 3 project. The LWC option is scaled, in the sense that water customers would pay only for the incremental increases in water use that would be required over

time rather than paying immediately for capacity that won't be needed for some 20-30 years. The LWC plan offers another advantage by providing another source of supply from the Ohio River, providing additional security of supply availability, and avoiding costs of expanding treatment capacity.

As noted below, with the implementation of cost-effective measures, the short-term needs of the KAWC system can be met. Given the significant movement towards extension of the LWC supply to Frankfort, it is prudent to defer approval of any new KAWC treatment capacity at Pool 3 until the Louisville-Frankfort connection is completed or until it is determined that the connection will not occur.

In June, 1998, KAWC published Volume 1, Number 1 of "Bluegrass Water Project Update" identifying a pipeline connection to LWC as the "best alternative & environmental solution." Among the salient points raised by KAWC were:

- that the "option to purchase treated water from Louisville Water Company will eliminate the need for additional investments in plant capacity to overcome the treatment plant deficit [which] would run $38 million.

- that "[t]he Ohio River is a limitless source of water; providing communities existing along the banks of the Ohio with a continual source of supply. The Ohio River Basin Sanitation Commission is a watchdog organization that carefully monitors the Ohio River. The Kentucky River is not monitored to the level of the Ohio and does not presently have such a sophisticated protection system.

As the Commission noted in the Order granting full intervention status to LWC, the participation of LWC was important to this proceeding because the company possessed "significant information regarding the cost of purchasing and transporting water from LWC to central Kentucky[,]" and because in order to determine the reasonableness of the proposed KAWC Pool 3 Project, the Commission "must review all options that Kentucky-American Water

Company ("Kentucky- American") considered to resolve its supply deficit." August 13, 2007 Order, p. 1.

The Commission properly noted that the "public expects the Commission to determine the need for and reasonableness of investment in the proposed facilities in light of all known and viable options." It is clear from the Commission's Orders and from the flexibility it has shown in adjusting the briefing schedule to assure full development of the issues that the Commission has taken very seriously its statutory charge.

It has become equally clear that KAWC has not meaningfully engaged LWC in discussion concerning meeting the water supply needs of the central Kentucky region. Rather, having failed to communicate directly with LWC since the decision to abandon the pipeline project, KAWC has devoted significant resources and time to demonstrating why the LWC plan is not the best among alternatives, rather than attempting to explore the various options to make the project a positive one for the region and for KAWC ratepayers.[5]

It is apparent from the record that KAWC has not pursued other solutions to short and long-term needs as well. Missing from KAWC's filing was any meaningful exploration of the feasibility of purchasing treated water from Versailles through an existing system interconnection. The availability of 2-3 mgd, which KAWC indicated had not been explored with the Division of Water, in conjunction with savings from reductions in unaccounted for water, would net sufficient additional treated water supply to meet short-term needs as the LWC – Frankfort project proceeds.

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[5] While the Commission is probably aware of this point, it is important to note that the LWC plan is not the same as the earlier pipeline proposal, for several reasons. Initially, the first corridor selected by KAWC in the earlier case left the I-64 corridor and followed a gas pipeline easement. Additionally, as KAWC noted in the 2001 Report, it was unable to secure approval for use of the Interstate right of way – an issue that has been revisited and which the evidence indicates may be an option available for those instances along the corridor where it might be necessary. Additionally, with the commitment by LWC to construct a line to Frankfort, the cost to KAWC would be only that additional incremental cost of constructing the remaining interconnection and the cost of water used.

The feasibility of interconnection with Frankfort in order to purchase treated water from the Frankfort system once it is interconnected on the western side of that system with LWC, in order to meet longer-term needs, has not been adequately considered by KAWC. Prudence dictates that the combination of short-term measures, including purchase of treated water from Versailles, improved leak detection, upgrading of treatment capacity at the existing facility, be employed and that a reasonable period be given to allow the LWC-Frankfort transmission main to be constructed and the crest gates incorporated into the reconstructed Dam 9.

Finally, KAWC has failed to adequately evaluate the impact of installation of the crest gates on Dam 9. The record reflects that the Kentucky River Authority is moving forward with plans to install crest gates on Dam 9, and that the crest gates will have the capacity to store an additional .9 billion gallons of water, reducing the deficit in that pool by almost a third. Despite the acknowledgment that the parent company of KAWC owns and manages water supply impoundments, and the testimony of Ms. Bridwell that the crest gates present challenges, KAWC has not offered any assistance, financial or in-kind, to help KRA address the "challenges." There is no indication that KAWC has evaluated the alternative of assisting in the funding of reconstruction of Dam 10 or installation of crest gates for Dam 9, despite the reliance by KAWC on the continued maintenance and rehabilitation of both. Given the acknowledgment in the KAWC Post-Hearing Data Request 1 that for roughly half of the projected cost of the Pool 3 project, treatment capacity could be expanded by KAWC at the existing facilities to 80 mgd, KAWC should be required to serious explore partnership with KRA to expedite the deployment of crest gates on Dam 9 and the reconstruction of Dam 10.

2. DEMAND MANAGEMENT ALTERNATIVES HAVE NOT BEEN ADEQUATELY EVALUATED

In addition to the supply-side alternatives not thoroughly evaluated by the applicant, the record is clear that KAWC has not adequately addressed demand management measures that could flatten the peak demand and augment available treated water supply.

The record reflects that Kentucky-American's unaccounted for water loss is at or near 17%, while the national average is substantially lower at 12%. Without *any* augmentation of supply, a more aggressive program of leak detection and system maintenance could significantly reduce the need to supply augmentation. Assuming the ability to treat 65 mgd, a 17% loss is 11 mgd, and a 12& loss is 7.8 mgd – a difference of 3.2 mgd that could be captured for customer use simply by bringing line losses down to the national average, and fully half (and slightly more) of what KAWC indicated they would routinely treat and pump from the Pool 3 project in year one. Prior to saddling the ratepayers with a 50% increase in rates,[6] it might be prudent to require KAWC to fix its leaky pipes.

A recent Joint Stipulation and Agreement for Settlement in a rate case before the Public Service Commission of West Virginia captioned *West Virginia-American Water Company*, Case No. 07-0998-W-42T, reflects the agreement by a sister company of KAWC to commission an independent study and plan for reduction of unaccounted for water:

> Company shall engage an independent consultant to study and submit a written report with recommendations for a comprehensive plan to reduce unaccounted for water, and the report shall include estimates of capital expenditures necessary to achieve quantifiable improvement ("Water Study and report.")

Case No. 07-0998-W-42T, Attachment A, p. 6. (A copy of the Joint Stipulation and Agreement is attached to this brief as Appendix A.)

[6] The roughly 50% increase in average monthly rates was provided by KAWC.

Such an independent study and plan is an essential predicate to granting a CPCN, since as the Court in *Kentucky Utilities Co. v. Public Service Commission, Ky., 252 S.W.2d 885 (1952)* noted,

> [w]e think it is obvious that the establishment of convenience and necessity or a new service system or a new service facility requires first a showing of a *substantial inadequacy of existing service*. . . due either to a substantial deficiency of service facilities, beyond what could be supplied by normal improvements in the ordinary course of business; or to indifference, poor management or disregard of the rights of consumers[.]

Id., at 890. (Italics added).

KAWC ratepayers have every right to expect that before they are requested to shoulder a 50% increase in average monthly bills, that the management of the unaccounted for water losses has been optimized and that the losses of treated water have been reduced to a reasonable level on a consistent basis. KAWC has failed to meet the burden of demonstrating that the projected treated water deficit necessitates the construction of a new 20 mgd plant, since "normal improvements in the ordinary course of business" such as those agreed to by KAWC's sister company are highly likely to yield reductions in the loss of water that has already been withdrawn and treated, and to augment by as much as 3.2 mgd the availability of water to KAWC customers. Failing to have done so, new treatment facility capital construction at Pool 3 is presumptively wasteful and duplicative of existing capacity that has been withdrawn, treated, and lost.

Additionally, despite the admonition of the Commission that conservation measures should be employed, Ms. Bridwell's testimony reflects that minimal efforts have been made in the area of conservation. The prefiled direct testimony of Liz Felgendreher notes that other than community education, KAWC has done little in the area of conservation since 1991, and as reflected in KAWC's Response to CAWS Second Supplemental Data Requests 17 – 19, has not exhausted reasonable approaches to addressing demand management.

As is the case with a number of alternatives that could assist in meeting the short and/or long-term needs of the KAWC customer base, KAWC argues that conservation alone will not "solve" the source of supply deficit or treatment capacity deficit. A review of the table provided in KAWC Post-Hearing Data Request 1, reflects that KAWC has similarly rejected a number of incremental alternatives that could in combination address any reasonable water treatment and water supply deficits, on that basis that the alternatives standing alone would not "solve" the deficits. Until KAWC properly and thoroughly evaluates the combination of supply-side and demand-management alternatives, the requested CPCN should not be issued.'

III. RESPONSE TO QUESTIONS POSED IN APPENDIX E OF DECEMBER 21, 2007 ORDER

In the December 21, 2007 Order, the Commission directed that parties address four questions contained in Appendix E of that Order, to wit:

> 1. Does the Louisville Water Company have the legal authority to make wholesale water sales in the counties other than Jefferson County and those counties that are contiguous to Jefferson County?
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> 2. Does the Louisville Water Company have the statutory authority to construct, own, and operate a water transmission main in counties other than Jefferson County and those counties that are contiguous to Jefferson County for the purpose of making wholesale water sales in counties other than Jefferson County and those counties that are contiguous to Jefferson County?
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> 3. Does the LFUCG have the statutory authority to construct, own and opeate (sic) a joint public-private venture to supply water to Kentucky-American and any other regional water suppliers?
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> 4. May the Commission, as a condition for granting a CPCN for the proposed facilities, limit the amount that Kentucky-American may include in its rate base for ratemaking purposes to the estimated cost of the proposed facilities at the time a CPCN is issued?

CAWS responds to these questions *seriatum*.

1. LOUISVILLE WATER COMPANY HAS THE LEGAL AUTHORITY TO MAKE WHOLESALE WATER SALES TO COUNTIES OTHER THAN

THOSE CONTIGUOUS TO JEFFERSON COUNTY

Louisville Water Company (LWC) was first established as a private corporation in 1854 by the General Assembly under Chapter 507. *Phelps v. Louisville Water Co.*, 103 S.W.3d 46, 49 (Ky. 2003). Subsequently, the City of Louisville purchased all of LWC's shares of stock and that stock is held in a sinking fund. *Id.* In addition, the legislature created a Board of Waterworks to govern the company and control and manage its properties in 1906. *Id.*; KRS 96.230-.310. In 1908, LWC transferred legal title to all of its property to the City of Louisville, which currently holds legal title to all physical property of the LWC. *Phelps,* 103 S.W.3d at 49. LWC is a for-profit corporate entity wholly separate from the City of Louisville, however, the city owns all the stock of the corporation. *Id.*

According to the LWC website,[7] the company currently provides water to customers in Oldham and Bullitt counties, in addition to Jefferson County. LWC also sells water at wholesale to the West Shelby Water District, the North Shelby Water Company, the North Nelson Water District, Taylorsville, Mount Washington, and Lebanon Junction, none of which are located in Jefferson County.

Concerning whether a municipality may sell water to customers outside a city limit, "[i]t is well-established that a city may extend its water system and furnish and sell water to customers beyond the city's corporate limits." OAG 02-1, 2002 Ky. AG Lexis 4 (February 7, 2002). Under the common law, a city can sell surplus water to any territory outside the city limits, but cannot extend its facilities absent statutory authority. Id., citing *Henderson v. Young*, 83 S.W. 583 (Ky. 1904); *Rogers v. City of Wickliffe*, 94 S.W. 24 (Ky. 2002). Therefore, it appears that

[7] www lwcky.com/about_us/default.asp

there is no legal impediment to LWC selling any surplus water to non-resident customers at wholesale.

2. THE LOUISVILLE WATER COMPANY HAS AUTHORITY TO CONSTRUCT, OWN, AND OPERATE A WATER TRANSMISSION MAIN IN COUNTIES OTHER THAN JEFFERSON COUNTY AND THOSE COUNTIES THAT ARE CONTIGUOUS TO JEFFERSON COUNTY FOR THE PURPOSE OF MAKING WHOLESALE WATER SALES IN COUNTIES OTHER THAN JEFFERSON COUNTY AND COUNTIES CONTIGUOUS TO JEFFERSON COUNTY

Statutory authority also seems to give LWC the right to extend its facilities outside the county to provide water to non-residents. Kentucky Revised Statute 96.150 provides:

> Any city that owns or operates a water supply or sanitary sewer system may extend the system into, and furnish and sell water and provide sanitary sewers to any person within, any territory contiguous to the city, and may install within that territory necessary apparatus; provided, however, that the extension of a water supply or sanitary sewer system shall not enter into any territory served by an existing water supply or sanitary sewer district unless such district requests the extension of water or sewer services from a city.

There is no statutory definition of "territory" in Chapter 96, but the statute clearly contemplates that LWC would be able to both extend its system into contiguous water districts outside of the city, and to sell water to contiguous water districts in those territories, provided that the existing water supply districts requested the extension of water services. In this instance, the record reflects that LWC is working in conjunction with the water districts along the route from Louisville to Frankfort and that those systems are desirous of the possibility of purchasing treated water from the LWC system.

Kentucky's highest court, in the context of adverse possession, has defined "contiguous" to mean having a common border. *Parson v. Dils*, 189 S.W. 1158, 1159 (Ky. 1916). However, a with respect to the use of "contiguous" in KRS 96.150, Attorney General Opinion OAG 77-559, 1977 Ky AG Lexis 246 (September 1, 1977), rejected the interpretation that a city and the county

proposed to be served needed to be connected by a common border to be considered contiguous under the statute. Id. at 2. Relying on KRS 96.130 and a South Carolina opinion addressing a similar issue, the Attorney General found that the legislature likely used contiguous in the statute to mean that the extension of water mains to a territory outside the city, made that territory contiguous to the city by virtue of the extension. Id. Under that interpretation, LWC could incrementally extend its transmission and delivery system and sell waters to even non-bordering counties since the extension of service would make the newly-serviced territory contiguous.

Additionally, KRS 96.130 authorizes any city that owns and operates its own water supply system to contract with another city to furnish water to that city. The statute would likely apply to LWC because the city is the sole shareholder of the company and the company is controlled by a Board of Waterworks, who are appointed by the city. Unlike KRS 96.150, there is no requirement in K.R.S. 96.130 that the territory served outside the city limits be contiguous to the city, so that LWC could contract with any other city in the state and furnish water to it through a water supply system constructed by another city or a consortium of water districts and cities.

3. JOINT OWNERSHIP BY LFUCG AND KAWC OF A PUBLIC-PRIVATE VENTURE TO SUPPLY WATER WOULD NOT BE PERMISSIBLE; LFUCG COULD FINANCE, CONSTRUCT AND OWN SUCH A PROJECT AND LEASE PROJECT OPERATION TO KENTUCKY-AMERICAN

Undertaking any "partnership" between LFUCG and Kentucky-American in a joint public-private ownership and operation of a water supply plant and distribution system would appear to be impermissible under Kentucky law, and the ownership of such an operation needs to be either private or public (although it may be more accurate to characterize municipal corporations as quasi-public)

To find otherwise would allow Kentucky-American to operate under the auspices of LFUCG's discretionary governmental authority. On the other hand, LFUCG and Kentucky-American are not prohibited from cooperating in developing and completing the project. LFUCG may be able to finance the construction of the venture and then lease the facilities and appurtenances to Kentucky-American if Kentucky-American is willing to forego ownership of these capital improvements.

Kentucky Revised Statutes Chapter 67A contains the provisions allowing for the creation of the urban county form of government, and outlines the urban county government's powers and responsibilities. Urban County government merges all units of city and county government into one governing body. K.R.S. 67A.010. "All debts, property, franchises and rights of the existing county government and of any municipality within the county ... [are] assumed by the urban-county government." K.R.S. 67A.030. The urban county government is then deemed to have the powers of a county and also the city of the highest class that existed on the day prior to the merger. K.R.S. 67A.060. While Chapter 67A includes special provisions extending the permissive authority of urban county governments for assessment financing of public improvement projects[8] and extending the permissive authority of urban county governments to *directly* plan, develop, initiate, finance and carry out wastewater collection projects,[9] there is no provision in Chapter 67A that addresses the authority (or lack thereof) of the urban county government to enter into a joint public-private water supply venture.

Pursuant to K.R.S. 67A.060, the Lexington-Fayette Urban County Government (LFUCG) is effectively both a county and a city of the second class, and possesses all of the rights, powers,

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[8] *See*, K.R.S. 67A.710-67A.825

[9] *See*, K.R.S. 67A.871-67A.894.

privileges, immunities and responsibilities incumbent in both entities. *See* Lexington-Fayette Urban County Government Charter Article 3 Sec. 3.01. Therefore, in order to determine whether the LFUCG has statutory authority to construct, own and operate a joint public-private water-supply venture, the statutory authorizations of counties and cities if the second class must be examined.

Concerning the ability of Kentucky-American to "partner" with LFUCG in order to utilize LFUCG's financing options, the authority conveyed by Chapter 58 clearly allows a government agency by itself or in partnership with **another government agency** to acquire, construct, maintain, add to, and improve any public project and to borrow money and issue negotiable revenue bonds to defray the cost of such project, but nothing in this chapter allows a government agency to act jointly with a private, for-profit company to the same end. K.R.S. 58.020.[10] Furthermore, public project is defined for the purposes of Chapter 58 as "any lands, buildings, or structures, works or facilities" that are "suitable for and intended for use as public property for public purposes or suitable for and intended for use in the promotion of the public health, public welfare or the conservation of natural resources". K.R.S. 58.010.

A proposed water supply project is arguably suitable for and intended for use in the promotion of public health and welfare even though the facilities and appurtenances may not constitute public property. K.R.S. 58.180. The problem with the application of the financing options available under this chapter to a joint venture between the LFUCG and Kentucky-American lies in the fact that it only contains an explicit extension of financing power for individual and interlocal government projects. Nothing in this chapter allows for the issuance of

[10] *See also*, Decker v. City of Somerset, Ky. App., 838 S.W.2d 417, 419 (1992) ("Keep in mind that KRS 58.020 approves of joint ventures between and among government agencies. The statute is explicit. It says, 'A government agency acting separately or jointly with any one or more of any such agencies, may acquire, construct, maintain, add to and improve any public project as defined in KRS 58.010...").

revenue bonds by the LFUCG to finance a for-profit public works project owned and operated in part or whole by a private corporation.

There are several statutes that provide LFUCG with authority to construct, own, operate and maintain a water supply system for the benefit of its citizens. According to K.R.S. 96.350, a second class city can purchase, establish, maintain and operate a waterworks and any appurtenances necessary thereto within or without the city limits in order **to supply water to the city and its residents**. *See also*, K.R.S. 96.160. Any waterworks purchased can be operated as a department of the city, or through an appointed commission whose members must reside in the area served by the waterworks and be registered voters in that area. K.R.S. 96.320. However, any net revenue from the waterworks must be applied to the improvement or reconstruction of the city's public ways, extension of the waterworks system, or to repayment of any waterworks bonds. K.R.S. 96.330. No provision of K.R.S. Chapter 96 (which addresses utilities in cities) provides authority for the city to operate a waterworks in conjunction with a private for-profit company or payment of dividends to shareholders. An operation established pursuant to Chapter 96 would arguably prohibit the distribution of net profit to the benefit of Kentucky-American's investors – requiring proceeds to instead be reinvested in the waterworks system and/or the improvement of LFUCG public ways.

K.R.S. Chapter 106 provides an alternate authority by which cities and water districts can acquire and operate waterworks. K.R.S. 106.010; K.R.S. 106.030. Nothing in this chapter explicitly allows a city to enter into a joint public-private waterworks venture, but it does provide that a city has the express power to:

> Make any contracts necessary or convenient for the full exercise of the powers herein granted, including, but not limited to, contracts for either the purchase or sale or both the purchase and sale of water and contracts for the acquisition **or improvement of**

> **all or any part of a water plant and appurtenances thereto**; and in connection with any such contract with a governmental agency, the board may stipulate and agree to such covenants, terms, and conditions as the governing body deems appropriate including, but without limitation, covenants, terms and conditions with respect to the resale rates, financial and accounting methods and the manner of disposing of the revenue of the water plant and appurtenances thereto conducted and operated by the board.

K.R.S. 106.210(10).

Pursuant to the foregoing, LFUCG has clear statutory authority to independently construct, own and operate a water supply operation that could supply water to Kentucky-American and possibly other regional water utilities, but this power is limited by the duties and obligations attendant to a governmental body. As a general rule, a city may acquire and use property outside of its borders for legitimate municipal purposes, but cannot engage in any business activity that does not pertain to the government of its inhabitants. *City of Corbin v. Kentucky Utilities Company*, 447 S.W. 2d 356, 358 (1969). A city cannot engage in a project in order to further a private industrial enterprise, irrespective of whether the business engaged-in by the private enterprise is the provision of utility services. 447 S.W.2d at 358. If the enterprise extends beyond the physical boundaries of the city, it must be directly and predominantly tied to the public welfare of the city's inhabitants in order to be a valid exercise of municipal power. Id. at 359. The project must be closely integrated into the city's operations and closely related to the city's development. Id. In other words, if the proposed project is intended to provide a greater capacity than is necessary to meet the needs of LFUCG residents, financing the project may not be a permissible LFUCG governmental function.

The primary impediment to applying any provision of K.R.S. Chapter 67A, K.R.S. 96.320-96.510, or K.R.S. Chapter 106 as statutory authority for a joint public-private water supply venture lies in the fact that all three sections of the K.R.S. clearly apply only to circumstances

wherein the property, facilities, or operation at issue is owned by the county or city, not a private company. Improvement and expansion of Kentucky-American's operations would not a "public improvement" because under the current proposal these improvements would not be to property owned by LFUCG or some other government agency. Therefore, K.R.S. Chapter 67A does not apply. Nor is this a situation where Kentucky-American has offered to share the proprietary claim on the facility and appurtenances with LFUCG such that the project could be considered one in which the LFUCG sought to acquire or operate in accordance with K.R.S. 96.320-96.510 or Chapter 106. Therefore, authority for a joint public-private venture must extend from some other source.

There is no clear statutory authority for a joint public-private venture. But authority to enter into contractual relationships for provision of services is authorized. Sec. 3.02(8) of Article 3 of the LFUCG Charter specifically provides that LFUCG shall have power and authority to construct, maintain, purchase, and operate waterworks. Sec. 3.02(25) of the Charter allows for LFUCG to "enter into contracts and agreements with other governmental entities **and also private persons, firms, and corporations** with respect to furnishing services." Attendant with its incorporation of the powers and obligations of a second-class city, LFUCG has the power to "provide the city with water." K.R.S. 96.160. Furthermore, LFUCG "may exercise any power and perform any function within its boundaries [. . .] that is in furtherance of a public purpose of [LFUCG] and not in conflict with a constitutional provision or statute. K.R.S. 82.082.

It appears from case law that there is a fine line between the proper execution of a city or county's proprietary and corporate powers and statutory authorization to provide public services and an unconstitutional delegation of public function and discretionary authority. In *Booth v. City of Owensboro,* 118 S.W.2d 684 (1938), a plan to finance a new hospital for Owensboro and

Daviess County was challenged in part because it was to be managed by representatives of the county, the city and a private corporation. Both the city and county were authorized by statute to purchase, establish, construct, operate and maintain hospitals. 118 S.W.2d at 686. Counties were also authorized to contract with private hospitals to provide infirmaries for the sick and power and allowed hospital authorities (rather than public officers) to expend county funds appropriated for this purpose. Id. But counties were to "control" any such hospital and rates were to be regulated. Id.

The statutory authorization in the *City of Owensboro* case is similar to that addressing LFUCG's authority in relation to a waterworks except that the power given to counties with regard to hospitals was broader since there was explicit statutory authority for the county to give public funds to a private hospital. No such authority is given in the statutes addressing LFUCG's authority to engage in or finance a waterworks. Despite the broader authority, the court determined in *City of Owensboro* that the management plan was impermissible.

> We are of the opinion these statutes authorize a city and a county to join in the operation and maintenance of a hospital, but the court finds no authority in them or in any other statute for either the city or the county to take a private corporation or individuals into partnership in conducting public enterprise. To do so is to surrender official responsibility and to delegate the public function to persons who are not responsible to the people. The officers of a municipal corporation cannot so delegate the governmental discretionary authority confided to it by the legislature.

Id. at 686.

Similarly in *City of Middlesboro v. Kentucky Utilities Co.*, 146 S.W.2d 48 (1940), the validity of issuing revenue bonds for the construction of a municipal electric distribution system and a related contract between the city and the Tennessee Valley Authority (TVA)[11] were brought into question. The question was whether the TVA contract attendant to the construction of the

[11] The court treated the federal agency as no different than an individual or private corporation in its analysis. 146 S.W.2d at 53.

distribution system had the effect of partially, or wholly, "surrendering the management and operation of the system and of delegating municipal power specifically lodged in local officers by the law." Id. at 50. The TVA contract established a schedule of rates, required the operation and management of the system to meet TVA standards and subjected it to TVA inspections, and limited the city utility commission's ability to change its methods of operation without notice to the TVA. Id. at 51-52. The court found that this contract was a surrender of the city's discretionary authority and therefore impermissible. Id. at 52.

> Public office is a public trust and it is fundamental that the performance of the trust cannot be farmed out or delegated to one not chosen directly or indirectly by the citizens, and then only under permission of the legislative body which established the trust. A city cannot go beyond its charter, nor its officers step aside that their functions may be performed by or their administration shared with others.

Id.

The court found that municipal corporations may be quasi-private, but they are still entrusted with responsibilities and duties that cannot be delegated without express legislative authority. Id.

While the statutes addressing a city's authority to own and operate an electric generating and distribution system are slightly more restrictive than those addressing a city or county's authority to own or operate a waterworks, the *City of Middlesboro* case is still instructive. The relevance of the *City of Middlesboro* case becomes even more apparent when considering the restrictions placed on the disposition of net revenue from a waterworks operated by a second-class city – restrictions that would apply to LFUCG. As stated above, pursuant to K.R.S. 96.330, any net revenue from the waterworks owned or operated by a second-class city must be applied to the improvement or reconstruction of the city's public ways, extension of the waterworks system, or to repayment of any waterworks bonds. Accordingly, the statutes delineating LFUCG's power to own and operate a waterworks arguably establish a clear irreconcilable conflict between the

permissible disposition of net revenue by LFUCG and the legal duties and interests of any private for-profit company.

In contrast to both of the foregoing cases is *Abernathy v. City of Irvine*, 355 S.W.2d 159 (1961). In *Abernathy*, bonds and a federal grant were used to construct a city-county hospital building. 355 S.W.2d at 160. Following the building's construction, the city and county determined that they did not have the funds needed to operate a hospital there. Id. After a prolonged search, they found a private organization willing to lease the building for the operation of a charitable hospital. Id. An action was brought to declare the lease invalid and to require the city and county to take over the operation of the hospital. Id. The court found that the lease was valid and that there was no improper delegation of municipal authority because the hospital was not being operated as a governmental institution. Id. at 161.

Consideration of these three cases together, as well as the absence of any statutory authority for a joint public-private water supply venture, suggests that undertaking any "partnership" between LFUCG and Kentucky-American in the ownership and operation of a plant and distribution system would be viewed as an impermissible delegation of public function. The operation needs to be either private, or conducted under the explicit statutory authority given to LFUCG.

This is not to say that LFUCG and Kentucky-American are prohibited from any cooperation in developing and completing the project. LFUCG may be able to finance the construction of a water supply project and then lease these facilities and appurtenances to Kentucky-American if Kentucky-American is willing to forego ownership of these capital improvements. LFUCG clearly could finance the construction of a water-supply project that would primarily benefit its residents and then, through its proprietary powers, lease the facilities and appurtenances to

Kentucky-American to operate. *Wilson v. City of Henderson*, 461 S.W.2d 90 (1970) (it is permissible for a city to use revenue bonds to finance expansion of city's electricity generating facilities and contract with private company for use and operation of facilities and sale of surplus energy). However, any such operation would have to be mindful of extra-jurisdictional issues as well as constitutional limitations on the accrual of debt. *See e.g.*, *Smith v. City of Raceland*, 80 S.W.2d 827 (1935) (city has no right to engage in the waterworks business beyond its corporate limits and therefore cannot build a plant to supply neighboring city with water); Kentucky Constitution § 158. If the scope of the project and the customer base it is intended to serve extends beyond LFUCG boundaries, an analysis would have to be completed to determine whether the primary purpose of the project was to benefit LFUCG residents.

4. AN ATTEMPT TO IMPOSE A COST CAP BY LIMITING THE RECOVERY OF COSTS THROUGH THE RATE BASE TO ONLY THOSE COSTS INCLUDED IN THE $160 MILLION ESTIMATE WOULD MOST LIKELY BE CONSIDERED AN UNLAWFUL EXTENSION OF THE COMMISSION'S AUTHORITY

The final question asks whether, as a condition for granting a CPCN for the proposed water supply project, the Commission has authority to impose the "cost-cap" suggested by the witness for the Attorney General, by limiting the amount that Kentucky-American may include in its rate base for ratemaking purposes to the estimated cost of $160 million.

The question could alternately be characterized as asking whether it is an abuse of discretion for it to determine at the outset of this extensive expansion project that any expenses over the estimated cost of the proposed facilities are ipso facto unreasonable.

Essentially, what the Attorney General's witness has proposed is similar to the action taken by the Pennsylvania Public Utilities Commission to cap the costs of construction of a nuclear power plant through a cost-containment plan in *Barasch v. Pennsylvania Public Utility Commission*, 521 A.2d 482, 488 (1987). In *Barasch*, the Pennsylvania PUC ordered suspension of the construction in

response to rising costs and then conditioned the continuation of the construction on the utility's agreement to adopt a cost-containment plan (or cost cap). Id. at 486. The PUC found that there was a need for additional capacity but that the construction costs were escalating to a level so as to make the proposed nuclear power plant no longer in the public interest – it then determined that a nuclear power plant that was constructed under the cost-containment plan would be in the public interest. Id. at 489. The court upheld this action as a reasonable exercise of PUC discretion. Id.

The problem with applying this approach in Kentucky is that Pennsylvania grants broader authority to its utility commission with respect to construction projects and rate setting – allowing the Pennsylvania Public Utility Commission to suspend or cancel construction projects if it becomes apparent that costs will exceed projections and thereby the make completion of the project no longer in the public interest. The *Barasch* court based its decision in part on the fact that the PUC had so much control over active construction project so as to be able to suspend or cancel the project entirely. It felt that the lesser power of altering a project through a cost cap was subsumed in the authority to cancel the project completely. The powers conveyed to the Commission in Kentucky statutes are not so expansive.

Pursuant to K.R.S. 278.020(1), no entity is permitted to begin construction of a utility service without first obtaining from the Commission a certificate (CPCN) finding that public convenience and necessity require the service or construction. The Commission is vested with discretion to issue or refuse to issue a CPCN. K.R.S. 278.020(1). The Commission may also issue the CPCN in part, or refuse to issue it in part. Id. This statute gives the Commission fairly broad authority in addressing proposed construction projects at their outset and in altering or influencing the scope and direction of proposed projects to ensure that they actually serve public convenience and necessity. It may be

possible to argue that imposing cost-containment is a valid exercise of the Commission's ability partially issue or refuse to issue a CPCN. But Kentucky case law suggests this is unlikely.

There is no Kentucky case that directly addresses whether the Commission has the power to cap the allowable recovery of costs of a construction project in the CPCN proceeding. It is indisputable that the Commission has the authority to determine in a general rate case whether the inclusion of costs incurred and the pass-through of costs to consumers is just and reasonable. *See e.g.*, *National-Southwire Aluminum Co. v. Big Rives Electric Corp.*, Ky. App., 785 S.W.2d 503, 510 (1990) (it is a function of the PSC to determine in a rate case whether a facility is used and useful as it is public policy "to insure that utility consumers do not pay unreasonable rates and that utilities do not make unreasonable expansions."). K.R.S. 278.030 grants utilities the privilege of demanding, collecting and receiving fair, just and reasonable rates for the services they provide in accordance with the standards set by the General Assembly and Commission. But this authority to set rates and approve or disallow recovery of costs is a distinct statutory authority from the authority to determine whether a CPCN is appropriate.

In *South Central Bell Telephone Co. v. Utility Regulatory Commission,* Ky., 637 S.W.2d 649, 652 (1982), the Kentucky Supreme Court held that the utility commission's responsibility and authority in the area of rates was separate and distinct from its authority with regard to services and, therefore, an inadequacy of service could not be penalized through a reduction in reasonable rates. The Court held that "it is clear that the legislative grant of power to regulate rates will be strictly construed and will neither be interpreted by implication nor influence." 637 S.W.2d at 653. The Court held that allowing the utility commission to authority in a rate to penalize a utility for poor service would improperly extend statutory procedure. Id.

> In fixing rates, the Commission *must* give effect to all of the factors which are prescribed by the legislative body, but may not act on matter which the legislature has not established.

Id.

The *South Central Bell* case is distinguishable from the present circumstances in that the reasonableness of construction costs is a valid factor to be considered in rate setting. But *South Central Bell* is still instructive because the Commission is potentially seeking to impose a rate limitation not in a general rate case, but in a CPCN proceeding. Nothing in the statutes delineating the Commission's authority in a CPCN proceeding allows the commission to make determinations on the recoverability of funds expended on a project as a condition of issuance of a CPCN.

In *Blue Grass State Telephone Co. v. PSC*, 382 S.W.2d 81, 83 (1964), the court determined that it was inappropriate for the Commission to deny a CPCN for the operation of a telephone service on the grounds that it found the cost of purchasing the telephone service to be too high. The Commission was concerned that the inflated cost would be a determining factor in establishing too high of a rate base at a later date. 382 S.W.2d at 82. The court determined that the Commission's concerns about the potential effect on the rate base were not properly the subject of the CPCN proceeding and that the Commission would have discretion to determine in a general rate case whether the price paid for the telephone operation was too high and to adjust the rate base accordingly. Id.

That said, the Commission should not rely on its ability to exclude costs from the construction project over the $160 million estimate in a general rate case if it believes that the project would not serve public convenience and necessity if its cost exceeded that amount. The Commission is required to consider the reasonableness of costs of the construction project as well as the value of any new property in establishing rates. K.R.S. 278.290. Excluding in advance costs that might be

later shown were necessary or reasonable based on developing circumstances and/or unforeseen or unavoidable complications in the completion of a project may be determined unreasonable or arbitrary. *See*, *PSC v. Dewitt Water District*, Ky., 720 S.W.2d 725, 731 (1986) (PSC must consider all operating expenses in order to properly assess revenue requirements).

Considering the foregoing, attempting to impose a cost cap by limiting the recovery of costs through the rate base to only those costs included in the $160 million estimate would most likely be considered an unlawful expansion of the Commission's authority in a CPCN process. The Commission should take into account in this proceeding the very real possibility that a water supply project of the magnitude and geographic span as that proposed by Kentucky-American would encounter unanticipated complications or expenses in determining whether the project as proposed really will serve public convenience and necessity. Given the availability of options that would incrementally increase available water supply and treatment capacity as and when needed, the uncertainty concerning the actual capital costs for the Pool 3 Project suggests that the CPCN should be denied.

CONCLUSION

For the reasons outlined above, CAWS respectfully requests that the Commission deny the application of KAWC for a certificate of public convenience and necessity.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that the original and 10 copies of this brief have been filed with the Commission and that a true and correct copy has been served by first-class mail (and electronically) upon the following individuals this 20th day of March, 2008:

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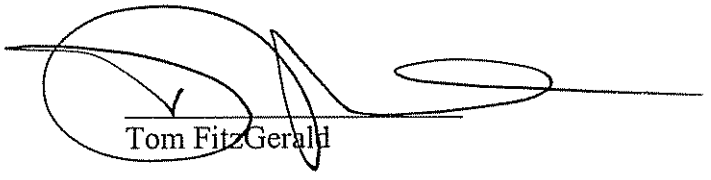

Tom FitzGerald

APPENDIX A

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA
CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA in the City of Charleston on the 18th day of March 2008.

CASE NO. 07-0998-W-42T

WEST VIRGINIA-AMERICAN WATER COMPANY
Tariff Rule 42 application to increase water rates and charges.

COMMISSION ORDER

By this Order, the Commission adopts a Joint Stipulation and Agreement for Settlement in resolution of this rate proceeding. The approved rates and charges are approved for use by West Virginia-American Water Company for service rendered on and after March 28, 2008.

Background

West Virginia-American Water Company (WVAWC or Company) filed this general rate case on June 1, 2007, and by Commission Order issued June 27, 2007, the Commission suspended the requested rates and charges until 12:01 a.m., Friday, March 28, 2008, unless otherwise ordered. As originally filed, WVAWC requested increased revenues of $24,065,516, or approximately 24.9% annually, for furnishing water utility service to approximately 166,000 customers in 19 West Virginia counties.

During the course of this proceeding, the Commission's Consumer Advocate Division (CAD), Putnam County and Lavalette Public Service Districts (collectively, the Public Systems), the Kanawha County Commission and the Regional Development Authority of Charleston, Kanawha County, West Virginia Metropolitan Region (together County), Kanawha Valley Chemical Manufacturers, Inc. and Steel of West Virginia, Inc. (Industrials), and the City of Charleston (the City) petitioned for, and were granted, intervenor status. *See* Commission Orders issued July 27, 2007 and September 21, 2007.

On October 22, 2007, WVAWC filed a revised rate application and supporting Rule 42 Financial Exhibit that reduced its rate increase request to $22,508,991, a 6.47% decrease from the original increase request.

On July 23, 2007, WVAWC filed its direct testimony and on November 14, 2007, Commission Staff (Staff), CAD, County, City and Industrials filed their direct testimonies.

The Commission's Division of Administrative Law Judges (ALJ Division) scheduled five public comment hearings in locations throughout WVAWC's service territory, the last of which occurred on December 12, 2007. *See*, Hearing Transcripts of public comment hearings held, each at 6:30 p.m.: on December 3, 2007 in Charleston; on December 5, 2007 in Huntington; on December 6, 2007 in Princeton; on December 10, 2007 in Oak Hill; and on December 12, 2007 in Madison. The Commission conducted the evidentiary hearing on December 17, 2007. *See* Hearing Transcript of December 17, 2007 evidentiary hearing.

The record and case file of this proceeding reflect that WVAWC satisfied all public notice, mailing, posting and publication requirements with respect to the filing of its rate case, and the several public hearings. *See* affidavits of publication filed December 17, 2007 and as supplemented on December 26, 2007.

At the December 17, 2007 evidentiary hearing, the witnesses who testified supported a Joint Stipulation and Agreement for Settlement filed by WVAWC, Staff and CAD on December 3, 2007 (Initial Joint Stipulation) recommending that the Commission approve an overall revenue increase of $14.75 million. The Public Systems and County signed the Initial Joint Stipulation for the purpose of indicating no objection. The City did not sign, but did not object to, the Initial Joint Stipulation. The Industrials did not sign, and objected to, the Initial Joint Stipulation. Five witnesses, WVAWC witnesses Paul Herbert and Michael A. Miller, CAD witness Randall R. Short, and Staff witnesses Dixie L. Kellmeyer and Robert McDonald, testified in support of the Initial Joint Stipulation and stood cross-examination on their positions.

At the close of hearing, the Commission stated that it would communicate in the near future with the parties regarding the briefing schedule.

By Order issued December 21, 2007, the Commission returned the Initial Joint Stipulation to the parties and requested that the parties meet to discuss the matter further and to discuss the settlement further. The Commission directed that any new or revised stipulation include some description of the parties' positions on substantive issues that allowed the parties to reach an agreed overall revenue requirement, rate design, and class cost of service calculation. Furthermore, the Commission provided that in the event the parties failed to reach an uncontested settlement, any further or revised stipulation describe all resolved and unresolved issues in this case and indicate the reasonableness of the parties' treatment of unresolved issues within the context of the overall settlement. The Commission also established a schedule for the filing of a revised stipulation and briefs.

On January 7, 2008, WVAWC, Staff, CAD, the City and the Industrials filed an amended Joint Stipulation and Agreement for Settlement that amended and revised the Initial Joint Stipulation (such Initial Joint Stipulation, as so amended, being hereinafter referred to

as the "Joint Stipulation"). On January 11, 2008, the County also signed the Joint Stipulation. The City of Charleston and the County endorsed the Joint Stipulation solely to acknowledge their lack of opposition to the Joint Stipulation, and not to evidence their support for the Joint Stipulation. The Public Systems declined to sign the Joint Stipulation.

On January 7, 2008, the Public Systems filed a letter stating two reasons for their refusal to sign the Joint Stipulation. First, the Public Systems believed that if they signed the Joint Stipulation, they might be foreclosed from raising an argument in the next Company rate case that updated customer usage and demand data should be filed with the rate case instead of at a later date and that such filing should consist of twelve months of data. Second, the Public Systems objected to the agreed $250,000 reduction in rate recovery from the industrial class because the Public Systems do not believe the record supports treating the industrial class different from the resale class.

WVAWC, CAD, Industrials, Public Systems, and Staff filed Initial Briefs. WVAWC and the Industrials filed Reply Briefs.

DISCUSSION

The Joint Stipulation seeks Commission approval of an increase in WVAWC's annual revenues of $14.75 million effective March 28, 2008, through an across-the-board rate increase to WVAWC's volumetric rates and charges except for 1) public fire protection rates that shall remain frozen at historical levels pursuant to prior Commission Order, and 2) certain high-usage rate blocks applicable to the Industrials. *See* Joint Stipulation, pp. 4-5. The Joint Stipulation contains an agreed-upon method of calculating the WVAWC revenue requirement and states that the pre-filed testimony and exhibits are adequate to support the Joint Stipulation. *Id.* p. 5.

Although the parties noted that the positions taken in the Joint Stipulation were only for purposes of developing a reasonable settlement of this proceeding and may be contested in future Company proceedings, they agreed that the Commission should approve the Joint Stipulation on findings that the individual agreements are reasonable in the context of the overall settlement in this case. *Id.* pp. 8-19. The Joint Stipulation describes the parties' compromises and agreements with respect to the agreed-upon calculations and is attached in full text to this Order. As a consequence, the Commission will not repeat those descriptions in this Order, and the Joint Stipulation is incorporated in this Order by this reference. *Id.*

The parties agreed that the Commission should approve the Joint Stipulation and find that the Company's annual revenue deficiency under presently authorized rates is $14,750,000, despite the fact that the parties' resolutions would support a finding that the Company's annual revenue deficiency is actually $14,754,625, which is $4,625 more than the agreed-upon amount. *Id.* p. 19.

To secure the Industrials' support of the Joint Stipulation, the Joint Stipulation provides that WVAWC will forego recovery of $250,000 from high-usage customers. This will be accomplished by adjusting the rate blocks in excess of 900,000 gallons on the Company's tariffs, which will limit the Company's rate recovery to $14.5 million under the billing units used in this case. *Id.* pp. 19-20. Because rate design is likely to be contested in future rate cases and the outcome of a litigated decision on rate design is uncertain, the parties request the Commission to adopt the following resolution of certain issues addressed in the Joint Stipulation:

1) The tariff attached to the Joint Stipulation that reduces the Company's revenue requirement to be collected from the industrial class of customers by $250,000 is fair and reasonable. *Id.* pp. 20-21.

2) The Company has agreed to collect usage and demand data (U&D data) incident to filing its next general rate case and file customer U&D data as soon as possible after its availability, but at least 45 days prior to the time by which other parties are required to file direct testimony in the Company's next rate case. If 45 days do not remain in the procedural schedule between the date the Company files the updated U&D data and the date when other parties' direct testimony is due in the Company's next rate case, the Company has agreed in the Joint Stipulation that it will request that the Commission toll the statutory suspension period as necessary to allow at least 45 days for other parties to file direct testimony after the date the Company files the updated U&D data. *Id.* p. 21.

3) The Company will file with its next general rate case a class cost of service study that includes the updated U&D data. If the Company files its next rate case prior to the end of summer 2008 peaking period, and thus prior to the Company's compilation of the updated U&D data, the Company will provide parties to the rate case copies of updated U&D data on a weekly basis as it becomes available between the date of filing of the rate case and the date the Company files an update to the cost of service study. Furthermore, after filing the updated cost of service containing the updated U&D data, the Company agrees to the expedited discovery process regarding the U&D data and cost of service study set forth in the Joint Stipulation. *Id.* pp. 21-22.

Under the Joint Stipulation, the parties have explicitly reserved the right to take different positions or espouse different ratemaking principles and treatments in future regulatory proceedings involving the Company. *Id.* pp. 23-24.

As noted in the Commission's December 21, 2007 Order and in Commission practice generally, the Commission values stipulations and appreciates the efforts of parties to reach reasonable and just settlements in rate and other proceedings. Stipulations are a significant assistance to the Commission in carrying out its statutory duties and frequently resolve many cases in a prompt, fair, reasonable and expedited fashion based on the arms-length negotiations of the parties. This can reduce litigation costs for the benefit of all parties and the ratepayers.

The settling parties to this case have put forth a substantial, diligent and good faith effort to reach agreement, and the Joint Stipulation demonstrates that the cost of service and rate design resolutions in this case are fair and reasonable. The Joint Stipulation reflects substantial compromises by the settling parties evidenced by modification of each party's respective position in this case.

The procedures and agreements set forth in subparagraphs 11(b)(2) and (3) of the Joint Stipulation that govern WVAWC's future collection and filing of updated U&D data in its next general rate application are fair and reasonable and should be approved.

The Commission understands that the parties to stipulations present their agreements on rate design and cost of service issues as reasonable resolutions in the context of the settlement of that particular rate case and that, unless specifically provided in the stipulation, do not intend their agreements to bind them in future proceedings.

The Public Systems' decision not to sign the Joint Stipulation in this case does not affect the reasonableness of the resolutions reached in the settlement. The Public Systems did not present any evidence on the Company's revenue requirement or its allocated cost of service. *See* Hearing Transcript. The evidence filed in this case supports an across-the-board allocation of the agreed-upon revenue requirement. Notwithstanding evidence in support of that allocation, because of (i) the age of the empirical U&D data on which the cost of service studies were based and (ii) the Company's desire to obtain the Industrials' support for a rate settlement, the Joint Stipulation reflects a Company concession to recover less in revenue than the amount to which it might have otherwise been entitled. The Industrials presented evidence in the form of cross-examination that led to the Company's agreement to a revenue concession in favor of the industrial class of customers. That revenue concession was not imposed on other customers. *See* Tr. pp. 22-31. The Public Systems did not submit any evidence to show that the Company's revenue deficiency or rate design were not supported by the record. *See* Tr. generally.

Further, we note that the Public Systems signed the Initial Joint Stipulation that proposed rates applicable to the Public Systems that are identical to those now presented in the Joint Stipulation. *See* Initial Joint Stipulation, Exh. 1, and Joint Stipulation, Exh. 1. The Commission concludes, therefore, that the record supports the Joint Stipulation and that the Joint Stipulation does not discriminate against the Public Systems.

Turning to the Public Systems' objection to the Joint Stipulation's agreements regarding the timing of WVAWC's updated U&D data, the Commission notes that the Public Systems will be free, in the Company's next rate case, to take issue with the adequacy, timing, and scope of the updated U&D data and class cost of service study.

Accordingly, the Commission concludes that the Joint Stipulation should be adopted in resolution of the issues presented in this case, and that the rates and charges set forth in

Exhibit 1 thereto should be in effect for service rendered by the Company on and after March 28, 2008.

FINDINGS OF FACT

1. WVAWC originally requested increased revenues of $24,065,516, or approximately 24.9% annually. *See* Company's filing of June 1, 2007. By filing on October 22, 2007, WVAWC reduced its rate increase request by 6.47% to $22,508,991. *See* amended filing of October 22, 2007.

2. Prior to the Commission's evidentiary hearing on December 17, 2007, the ALJ Division conducted five public comment hearings in locations throughout WVAWC's service territory. *See*, Hearing Transcripts of public comment hearings held, each at 6:30 p.m.: on December 3, 2007 in Charleston; on December 5, 2007 in Huntington; on December 6, 2007 in Princeton; on December 10, 2007 in Oak Hill; and on December 12, 2007 in Madison.

3. WVAWC satisfied all public notice, mailing, posting and publication requirements with respect to the filing of its rate case, and the several public hearings. *See* affidavits of publication filed December 17, 2007 and as supplemented on December 26, 2007.

4. At the December 17, 2007 evidentiary hearing, witnesses testified in support of the Initial Joint Stipulation filed on December 3, 2007, and signed by WVAWC, Staff and CAD. *See* December 17, 2007 Hearing transcript; Joint Exh. 1. The Public Systems and County signed the Initial Joint Stipulation for the purpose of indicating no objection. *See* Joint Exh. 1. The City did not sign, but did not object to, the Initial Joint Stipulation. The Industrials did not sign, and objected to, the Initial Joint Stipulation.

5. The Public Systems did not present evidence on the Company's revenue requirement or its allocated cost of service. *See* December 17, 2007 Hearing transcript.

6. By Order issued December 21, 2007, the Commission returned the Initial Joint Stipulation to the parties and, among other things, requested that the parties meet to discuss the matter further and to discuss the settlement further. *See* December 21, 2007 Commission Order.

7. On January 7, 2008, WVAWC, Staff, CAD, the City and the Industrials filed a Joint Stipulation. On January 11, 2008, the County also signed the Joint Stipulation. The City and the County endorsed the Joint Stipulation solely to acknowledge their lack of opposition, but not to support it. The Public Systems declined to sign the Joint Stipulation. *See* January 7 and January 11, 2008 case filings.

8. On January 7, 2008, the Public Systems filed a letter stating two reasons for their refusal to sign the Joint Stipulation.

9. The Joint Stipulation seeks Commission approval of an increase in WVAWC's annual revenues of $14.75 million effective March 28, 2008, through an across-the-board rate increase to WVAWC's volumetric rates and charges except for 1) public fire protection rates that shall remain frozen at historical levels pursuant to prior Commission Order, and 2) certain high-usage rate blocks applicable to the Industrials. *See* Joint Stipulation, pp. 4-5.

10. The Joint Stipulation contains an agreed-upon method of calculating the WVAWC revenue requirement. *Id.* p. 5.

11. Although the parties noted that the parties are likely to contest the agreed-upon calculations in future Company rate cases, they agreed that the Commission should approve the Joint Stipulation on findings that the individual agreements are reasonable in the context of the overall settlement. *Id.* pp. 8-19.

12. The parties agreed that the Commission should approve the Joint Stipulation on a finding that the Company's annual revenue deficiency under presently authorized rates is $14,750,000, despite the fact that the parties' resolutions would support a finding that the Company's annual revenue deficiency is actually $14,754,625, which is $4,625 more than the agreed-upon amount. *Id.* p. 19.

13. To secure the Industrials' support of the Joint Stipulation, the settlement provides that WVAWC will forego recovery of $250,000 from high-usage customers. This will be accomplished by adjusting the rate blocks in excess of 900,000 gallons on the Company's tariffs, which will limit the Company's rate recovery to $14.5 million. *Id.* pp. 19-20.

CONCLUSIONS OF LAW

1. The Commission values stipulations in rate and other proceedings because they resolve many cases in a prompt, fair, reasonable and expedited fashion based on the arms-length negotiations of the parties and can reduce litigation costs.

2. The Joint Stipulation demonstrates the reasonableness of the cost of service and rate design resolutions contained therein. The Joint Stipulation reflects substantial compromises by the settling parties evidenced by modification of each party's respective position in this case.

3. Although the evidence filed in this case supports an across-the-board allocation of the agreed-upon revenue requirement, the settling parties' agreement that WVAWC will forego $250,000 of its revenue requirement for the purpose of settling this case is reasonable and should be approved.

4. The procedures and agreements set forth in subparagraphs 11(b)(2) and (3) of the Joint Stipulation that govern WVAWC's future filing of updated U&D data in its next general rate application are fair and reasonable and should be approved.

5. The settling parties' agreements on rate design and cost of service issues are reasonable in the context of the settlement of this rate case, and will not bind the settling parties in future WVAWC rate cases.

6. The Public Systems' decision not to sign the Joint Stipulation does not affect the reasonableness of the resolutions of the settlement.

7. The Industrials presented evidence in the form of cross-examination that led to the Company's agreement to a revenue concession in favor of the industrial class of customers. *See* Tr. p. 22-31.

8. Because the Public Systems did not present evidence on either the Company's revenue requirement or allocated cost of service, and because the Public Systems did not object to rates set forth in the Initial Joint Stipulation and identical to those now presented in the Joint Stipulation, it is reasonable to conclude that the record supports the Joint Stipulation and that the Joint Stipulation does not discriminate against the Public Systems.

9. The Public Systems will be free, in the Company's next rate case, to take issue with the adequacy, timing, and scope of the Company's updated U&D data and class cost of service study.

10. The Commission should adopt the Joint Stipulation in resolution of the issues presented in this rate case, and the rates and charges set forth on Exhibit 1 thereto should be in effect for service rendered by the Company on and after March 28, 2008.

ORDER

IT IS THEREFORE ORDERED that the Amended Joint Stipulation and Agreement for Settlement attached to this Order as Attachment A is adopted in resolution of the issues presented in this case.

IT IS FURTHER ORDERED that the proposed rates set forth on Exhibit 1 to the Joint Stipulation are hereby approved for all service rendered by WVAWC on and after March 28, 2008.

IT IS FURTHER ORDERED that within thirty days of the date of this Order, the Company shall file an original and six copies of its revised tariff setting forth the rates approved herein.

IT IS FURTHER ORDERED that upon entry hereof this case is closed and shall be removed from the Commission's open docket.

IT IS FURTHER ORDERED that the Commission's Executive Secretary serve a copy of this Order upon all parties of record by United States First Class Mail and upon Commission Staff by hand delivery.

A True Copy, Tester

Sandra Squire
Executive Secretary

JML/klm
070998cg.wpd

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA
CHARLESTON

CASE NO. 07-0998-W-42T

WEST VIRGINIA-AMERICAN WATER COMPANY
Rule 42T tariff filing to increase
water rates and charges.

AMENDED JOINT STIPULATION AND AGREEMENT FOR SETTLEMENT

Pursuant to W. Va. Code § 24-1-9(f) and Rule 13(d) of the Public Service Commission's Rules of Practice and Procedure, and certain Commission Orders and proceedings described below, West Virginia-American Water Company ("Company"); the Staff of the Public Service Commission of West Virginia ("Staff" and "Commission," respectively); the Consumer Advocate Division of the Commission ("CAD"); and the Kanawha Valley Chemical Manufacturers and SWVA, Inc. ("Industrials"), collectively the "Parties," join in this Amended Joint Stipulation and Agreement for Settlement ("Amended Joint Stipulation").

In this Amended Joint Stipulation, the Parties propose and recommend to the Commission a settlement ("Settlement") of Company's pending general rate case, PSC Case No. 07-0998-W-42T. In this Amended Joint Stipulation, the Parties have agreed and recommend to the Commission that the Commission approve and establish a fair and

reasonable set of rates to meet Company's current cost of service and the revenue requirement set forth herein. In support of this Amended Joint Stipulation, the Parties state that:

1. On June 1, 2007, Company filed revised tariff sheets reflecting increased operating revenues of $24,065,516, or approximately 24.9% annually, for furnishing water service to approximately 166,000 customers in Boone, Braxton, Cabell, Clay, Fayette, Harrison, Jackson, Kanawha, Lewis, Lincoln, Logan, Mason, Mercer, Putnam, Raleigh, Roane, Summers, Wayne and Webster Counties, such rates originally to become effective July 1, 2007.

2. On June 27, 2007, in accordance with W. Va. Code § 24-2-4a, the Commission entered an Order that, among other things, suspended the rates and charges, deferred their use until 12:01 a.m., on March 28, 2008, and instituted a formal investigation into the reasonableness of the rates and charges contained in the revised tariff sheets and the supporting data filed by Company.

3. During the course of this proceeding, CAD, Putnam Public Service District and Lavalette Public Service District ("Public Systems"); the County Commission of Kanawha County and the Regional Development Authority of Charleston, Kanawha County, West Virginia, Metropolitan Region (together, the "County"), City of Charleston ("City"); and the Industrials filed petitions to intervene.

4. Through Commission Orders dated July 27, 2007, September 21, 2007, and December 7, 2007, the Commission granted all petitions to intervene.

5. On July 23, 2007, Company filed its direct testimony and exhibits. Staff, CAD, County, City, and SWVA filed their direct testimony and exhibits on November 14, 2007.

6. The Parties undertook extensive discovery, both of a formal and informal nature, including an examination of the books and records of Company and a review of extensive data responses and other documents provided by Company.

7. On October 22, 2007, Company filed a Revised Rule 42 Exhibit, thereby reducing its rate increase request to $22,508,691, a 6.47% decrease from the initial filing.

8. Company represents that it has satisfied all posting and publication requirements and provided evidence thereof to the Commission.

9. The Parties have attempted to negotiate a resolution of this case during pre-hearing conferences held on November 2 and 19, 2007, in other correspondence, and telephone discussions, some of which involved the Intervenors. The Parties have attempted to address or eliminate certain of the issues in this case and to reach an overall resolution of those issues. Based on those discussions and negotiations, the Parties other than the Industrials reached the Settlement in principle on November 19, 2007, the detailed terms of which were embodied in the Parties' Joint Stipulation ("Initial Joint Stipulation") filed December 3, 2007. The Parties have since participated in a

Commission hearing held December 17, 2007, and, in response to the Commission Order entered December 21, 2007, resumed their negotiations with all parties to this proceeding.

10. This Amended Joint Stipulation will have no effect whatsoever until and unless approved by the Commission in all of its material terms. Pending such approval of this Amended Joint Stipulation and the Settlement, the Parties reserve their rights to fully advocate their positions on the basis of all the evidence, unlimited by the terms of the Settlement. However, in the interest of certainty before the Commission, the Parties agree that, as a result of the Settlement, the proposed rates and charges in the tariff attached as Exhibit 1 to this Amended Joint Stipulation are fair and reasonable and agree and recommend that the Commission should approve those rates and charges to be effective on March 28, 2008. The particulars of the Settlement, all of which the Parties believe to be elements of a fair and reasonable resolution of this case, are:

(a) The Parties agree that a fair and reasonable resolution of this proceeding is an increase in annual revenues of $14.750 million effective March 28, 2008, as reflected in the Parties' negotiated resolution of certain issues in this proceeding as more fully described below;

(b) As shown on Exhibit 1, Company's volumetric rates and charges will be increased across-the-board, except for (i) public fire protection rates, which shall continue to remain frozen at historical levels pursuant to previous Commission Order,

and (ii) certain high-usage rate blocks applicable to the Industrials. The increase shall be effective on March 28, 2008;

(c) The Parties continue to support the Settlement after further negotiations subsequent to entry of the December 21, 2007, Commission Order, and now agree for purposes of effecting the Settlement and in consideration of the December 21, 2007, Commission Order, to the method of calculating the revenue requirement reflected in this Amended Joint Stipulation, but reiterating their agreement that the prefiled testimony and exhibits are adequate to support the Settlement. The Parties support and recommend this Amended Joint Stipulation, and the particular resolution of issues recited below, as a fair and reasonable determination of Company's revenue requirement based on the positions they have taken in the case, in discussions leading to the Settlement, to the Initial Joint Stipulation, and to this Amended Joint Stipulation;

(d) Company's request to implement the low-income discount tariff requested in its filing is withdrawn and will not be addressed in the Settlement;

(e) Company shall not be required pursuant to § 4.8.a.7 of the Water Rules to accept payments for water and/or sewer service at the customer's premises in lieu of disconnecting service for non-payment, and in lieu of payments being tendered at a customer's premises, a customer shall be afforded no less than one hour in which to remit payment using an authorized electronic payment service or at authorized collection agencies of Company;

(f) This Joint Stipulation and Settlement shall have no effect on the line extension multiplier pursuant to § 5.5.e.4.D of the Water Rules as previously agreed to by Company and Staff in Case No. 04-1731-W-PC; and

(g) Company shall engage an independent consultant to study and submit a written report with recommendations for a comprehensive plan to reduce unaccounted for water, and the report shall include estimates of capital expenditures necessary to achieve quantifiable improvement ("Water Study and Report"). The engagement by the Company of the consultant is subject to the following conditions:

(1) By December 14, 2007, Company shall submit to Staff and CAD a draft request for proposal for the Water Study and Report ("RFP") and shall include a list of potential consultants, including background and qualifications of providers to the extent practicably available ("Potential Consultant List");

(2) By January 11, 2008, Staff and CAD shall respond with any recommended refinements to the RFP and may remove consultants from the Potential Consultant List;

(3) Following responses from the CAD and Staff, Company shall send the RFP to consultants on the Potential Consultants List, with responses due on or about February 1, 2008;

(4) Following receipt of responses to the RFP, Staff and the CAD shall each have five business days to indicate in writing that they find either the proposed cost or the

proposed scope of the Water Study and Report to be unacceptable for purposes of this Joint Stipulation (the "Withdrawal of Support"). In the absence of a Withdrawal of Support, then Company shall award a contract for the Water Study and Report as soon as practicable. In the event of a Withdrawal of Support, then the Company, Staff and CAD shall work together to promptly resolve the issues leading to the Withdrawal of Support. Should a reasonable joint resolution not be achieved within five business days, then the Company may proceed with, modify, or abandon the Water Study and Report, in its discretion, and in the event of an abandonment by the Company, the Company shall have no further obligations in respect of the Water Study and Report;

(5) In the absence of a Withdrawal of Support, (i) the Water Study and Report shall be due by May 2, 2008, and (ii) should the completion of the Water Study and Report be delayed beyond that date for any reason, the filing of the Water Study and Report shall be deemed for purposes of the suspension period under W. Va. Code § 24-2-4a to have been filed on the 30th day preceding the filing of the Water Study and Report, in which case the Company agrees to (A) file a timely motion with the Commission for an extension of the statutory suspension period by the same number of days by which the filing of the Water Study and Report was delayed beyond May 2, 2008, and (B) to take all other steps reasonably necessary to ensure that the Other Parties will have the benefit of a procedural schedule (including the filing of the Other Parties' direct testimony) that is consistent with the extended suspension period;

(6) Irrespective of any Withdrawal of Support, all communications that relate to the Water Study and Report between the Company and the consultant engaged to conduct and prepare the Water Study and Report, including, but not limited to, letters of engagement and contracts, are to be made available to Staff, the CAD, or any party to this proceeding within five business days of any request and without the need to file a formal data request; and

(7) In the absence of a Withdrawal of Support, the cost of the Water Study and Report shall be deemed by the other Parties to be recoverable by the Company in future rate proceedings, except to the extent that the consultant fails in a material way to fulfill the terms and conditions of its contract.

11. Pursuant to the Commission Order entered December 21, 2007, the Parties have negotiated further and resolved each issue relevant to Company's overall revenue requirement, rate design, and class cost of service calculation.

(a) The Parties have resolved the issues relevant to Company's overall revenue requirement for purposes of this proceeding as summarized on Exhibit 2, and as particularly described below. The issues are listed in the context of their impact upon Company's revenue requirement, with appropriate annotations to the evidentiary record reflecting the Parties' positions prior to the Settlement. Exhibit 2 resolves each such issue in the context of an overall settlement relative to Company's position in its original

filing, in which it sought approval of rates adequate to generate an additional $24,065,516 in annual revenues.

(1) Company's amended Rule 42 exhibit reduced Company's request for additional annual revenue to $22,508,991, based primarily upon Company's concessions with respect to reclassification of maintenance expenses and going-level revenues.[a] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 1, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(2) Company's filing was predicated on terminal rate base at the end of the historical test-year (12-31-06) for all the 2006 Utility Plant additions and other rate base elements that Company believes to be non-revenue producing and non-expense reducing. Both the Staff and the CAD filed testimony recommending rate base be determined strictly on a thirteen-month average basis, both indicating that Company had not substantiated the non-revenue producing and non-expense reducing nature of the 2006 rate base items. While this issue is likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that the Staff's position on rate base is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's proposed rate base by approximately

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[a] See Co. Ex. 2, including cover letter, and Mr. Miller's testimony at page 45 of the December 17, 2007, hearing transcript.

$9,205,000, and Company's revenue requirement by $1,047,028.[b] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 2, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(3) Company's filing included historical test-year management fee expense reduced by a number of one-time, nonrecurring expenses totaling $1,015,835. In addition Company requested an adjustment to reflect a three percent increase related to salary increases that would occur in 2007 and 2008, the time which rates from this case would be in effect. Both the Staff and the CAD indicated in their testimony that the three percent post-test year increase should be eliminated based on that increase not meeting the known and measurable test. The CAD made further adjustments to Company's adjusted historical test-year management fee expense to limit the management fees to a three percent per year increase over the management fees included in Company's 2004 rate case, which would have further reduced Company's recovery of management fees as compared with the test year amount. While this issue is likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of finding that Staff's and CAD's recommended disallowance of Company's proposed 3% increase in test year management fees (but not the CAD's additional reduction of management fees below test

[b] See Co. Ex. 1, Statement B, Co. Ex. 2, Statement B, Co. Ex. JLW-A, pages 5-6, CAD Ex. 1, pages 6-16, Staff Ex. 5, pages 8-11, Staff Ex. 6, Statement B, and the testimony of Mr. Miller and Mr. Short at pages 56, 57, 61, 94 and 95 of the December 17, 2007, hearing transcript.

year levels) is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $280,495.[c] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 3, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(4) The Staff made a number of relatively minor adjustments to employee benefit costs based upon updated employee contribution rates, workers compensation premiums and capitalization ratios. The CAD made no adjustments to benefit costs from Company's filing. While these issues are likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that Staff's proposed adjustments to employee benefits, workers' compensation expense, and capital ratio are reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $36,246.[d] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 4, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(5) Company proposed a two-year amortization of the rate case expense for this proceeding. Both the Staff and the CAD proposed a three-year amortization of

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[c] Staff Ex. 5, pages 5-6; Co. Ex. MAM-A, pages 35-40; Co. Ex. PLB-A, PLB-1; CAD Ex. 1, pages 25-33.

[d] Staff Ex. 4, pages 3-4; Co. Ex. JLW-A, pages 11-12.

the rate case expense, citing their positions from past rate cases. The Staff also indicated the disallowance of the amortization requested for the prior depreciation study which will be nonrecurring in the rate year. While this issue is likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that Staff's proposed adjustments to rate case expense are reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $195,200.[e] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 5, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(6) Company proposed a "low income tariff" that, if approved, would have provided a twenty-five percent discount for any customer who demonstrated income at or below federal poverty guidelines. The Staff indicated in their testimony that such a tariff was discriminatory and should be addressed through legislation. While this issue is likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that Company's withdrawal of a low-income tariff is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding

[e] Staff Ex. 3, page 2; Co. Ex. JLW-A, page 13; CAD Ex. 1, pages 33-34.

reduces Company's revenue requirement by $106,328.[f] The effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 6, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(7) Company in its filing proposed adding $600,000 to its historical test-year maintenance expense to provide for additional tank site and road repairs, and additional valve maintenance. Company indicated the additional tank site and road maintenance was needed to bolster system security. The valve maintenance program was needed to improve service, improve liability claims and address unaccounted for water levels. Both the Staff and the CAD eliminated these additional expenses in their testimony, citing the absence of these expenses in the historical test-year. While these issues are likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that one-quarter of Company's proposed adjustment to tank site access maintenance and valve operations is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation based on the service benefits to be gained, which finding reduces Company's revenue requirement by $478,476.[g] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 7, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

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[f] Co. Ex. MAM-A, pages 55-57; Staff Ex. 4, page 10.

[g] Staff Ex. 3, page 3; Co. Ex. JLW-A, page 13; CAD Ex. 1, pages 34-37.

(8) Based on the adjustments to rate base described in paragraph (2) above, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that depreciation expense should be synchronized to reflect Staff's rate base and is thus reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $237,568.[h] The effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 8, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(9) Company's filing included an estimate of the property taxes to be paid in 2007. During the audit and discovery process of the case the actual 2007 property tax bills were provided. Both the Staff and the CAD included the lower 2007 actual property taxes in their recommendations and also included lower payroll taxes for changes in payroll as described in subparagraph (16) below. The Parties agree that the Commission can and should approve the Settlement on the basis of a finding that general taxes should be adjusted to reflect other adjustments to Company's filing and, thus, is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $102,123.[i] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 9, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

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h Co. Ex. JRW-A, pages 13-14; CAD Ex. 1, pages 37-38.

i Staff Ex. 3, page 4; CAD Ex. 1, page 38.

(10) The Company capital structures used by Company, the Staff and the CAD were all very similar in the percentage make-up of Debt, Preferred Stock, and Common Equity. The Staff and the CAD witnesses both recommended minor adjustments to the cost of short-term debt. Notwithstanding the conclusions of Dr. Vilbert, who determined ROEs ranging from 12.25% to 13.5%, Company requested ROE to be established at 11.25%, the Staff recommended an ROE of 9.52%, and the CAD recommended an ROE of 9.375%. While these issues are likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that Staff's proposed capital structure is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, and that Company's cost of equity capital is agreed to be 10.0%, which findings reduce Company's revenue requirement by $3,119,171.[j] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 10, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(11) Due to the capital structure used by the Parties as described in paragraph (10) above, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that the Staff's capital structure and cost of debt correctly calculated Company's weighted cost of debt and interest synchronization and

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[j] Co. Ex. MAM-A, pages 9-12, 28-35; Co. Ex. MAM-1, pages 1-2; Co. Ex. MJV-A,; CAD Ex. 1, pages 5-6; CAD Ex. 2; Staff Ex. 2.

thus is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $41,972.[k] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 11, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(12) Company used a "parent company loss adjustment" methodology in its filing that produced an effective federal income tax ("FIT") rate of 26.54%. Company made numerous adjustments to the taxable income of the various American Water Works Company, Inc. ("AWW") subsidiaries, including eliminating tax losses of regulated subsidiaries, eliminating tax losses of non-regulated AWW subsidiaries, and eliminating tax losses associated with the Change of Control costs and the capital cost related to the premium paid by RWE AG for the AWW common stock. The CAD calculated an effective FIT rate of 21.02% using the Company adjustments related to the Change of Control tax losses, but including the losses of non-regulated AWW subsidiaries. The Staff calculated an effective FIT rate of 12.71% by including the taxable losses of the regulated AWW subsidiaries, the non-regulated AWW subsidiaries, and the Change of Control tax losses. Recognizing that this issue is likely to be contested in future rate cases involving Company and other utilities and that the outcome of a litigated decision on this issue would be uncertain, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that the CAD's composite federal income

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[k] See footnote j.

tax rate of 21.02% is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation based on the evidence presented by all the parties, which finding reduces Company's revenue requirement by $1,626,148.[l] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 12, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(13) Company used a three-year average ratio of uncollectible expenses to revenue to determine the uncollectible expense in its filing. The Staff adjusted Company's revenue in this calculation to include B&O taxes. The Parties agree that the Commission can and should approve the Settlement on the basis of a finding that Staff's calculation of uncollectible expense is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $43,911.[m] The effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 13, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(14) In its filing, Company did not adjust forfeited discounts for the impact of adjusting historical test-year revenues to reflect 365 days of billed revenue. During the course of the Staff's audit, the Staff discovered this omission. The Parties agree that the Commission can and should approve the Settlement on the basis of a

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[l] CAD Ex. 1, pages 38-42; Co. Ex. MAM-A, pages 41-50; Co. Ex. MAM-6, pages 1-2; Staff Ex. 2, pages 13-14; Staff Ex. 5, pages 6-8; Staff Ex. 6, Schedule 5, pages 1-2.

[m] Co. Ex. JLW-A, page 11; Staff Ex. 5, page 5.

finding that the Staff's adjustment to increase going-level revenues for forfeited discounts is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $26,360.[n] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 14, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(15) Company used actual historical test-year B&O surcharge revenue and local B&O expense in its filing. The Staff recommended that both the local B&O revenue and expense should offset. While this issue is likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that the Staff's adjustment to increase going-level revenues for the local B&O tax is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which finding reduces Company's revenue requirement by $145,080.[o] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 15, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(16) In its filing, the Company requested that non-union wage increases for 2008 be recognized in this case based on the salary administration policy of Company. In addition, Company requested recognition of two additional management

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[n] Co. Ex. JLW-A, pages 4-5; Staff Ex. 5, page 4.

[o] Staff Ex. 5, page 4; Co Ex. JRW-A, pages 4-5.

employee positions, one of which is currently filled and the other to be filled in January 2008. Both the Staff and the CAD recommended that neither the 2008 salary increase for non-union employees nor the two additional employees be recognized. While these issues are likely to be contested in future rate case proceedings of Company and other utilities, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that the Staff's and the CAD's adjustment to reduce labor expense is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, which reduces Company's revenue requirement by $268,261.[P] The aggregate effect of the Parties' resolution of this issue for purposes of the Settlement is shown on line 16, page 1 of 1 of Exhibit 2 to this Amended Joint Stipulation.

(17) As shown on Exhibit 2 to this Amended Joint Stipulation, the foregoing resolutions of the issues would support a finding that Company's annual revenue deficiency under presently authorized rates is $14,754,625, which is $4,625 more than the agreed settlement amount reflected in this Amended Joint Stipulation. Nevertheless, the Parties agree that the Commission can and should approve the Settlement on the basis of a finding that Company's annual revenue deficiency under presently authorized rates is $14,750,000.

(b) In order to add the Industrials to the Parties to the Settlement, and in recognition of the position of the Industrials described in subparagraph (1) below,

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[P] Staff Ex. 5, pages 4-5; CAD Ex. 1, pages 17-18; JRW A, pages 7-8.

Company has agreed to forego recovery of $250,000 from high-usage customers by adjusting the rate blocks in excess of 900,000 gallons as shown on the tariffs attached as Exhibit 1. This adjustment will limit the Company's rate recovery to $14.500 million. Recognizing that the rate design issue is likely to be contested in future rate cases involving the Company and other utilities and that the outcome of a litigated decision on this issue would be uncertain, the Parties have further resolved the issues relevant to Company's rate design and class cost of service allocation in the context of the overall Settlement as follows:

(1) Company proposed an across-the-board increase based on the cost of service provided in Company Exhibits PRH-A and PRH-1. Staff Exhibit 4 also recommends an across-the-board increase, citing the principles of gradualism and the fact that the Company's demand factors had not been updated since 2000. No other party to this case provided testimony regarding the cost of service allocation. At the Evidentiary hearing, the Industrials questioned whether the class cost of service studies submitted by Company and Staff would support an across-the-board increase. The Parties agree that the class cost of service study filed in this case, and the empirical data supporting it, could be interpreted to generally support a finding that a substantially across-the-board allocation of Company's overall revenue requirement, is reasonable and appropriate[9]. However, the parties further agree that in order to resolve their differing positions the

[9] Staff Ex. 4, pages 6-12; Co. Ex. PRH-A, pages 4-12.

Commission should approve the tariff attached as Exhibit 1 which effectively reduces the amount of the revenue requirement to be collected from the industrial class of customers by $250,000.

(2) In light of the fact that it has historically been a "summer-peaking" water utility, and recognizing the fact that Company may file its next rate case prior to the end of summer 2008 peaking period and thus without the benefit of updated customer usage and demand data in its class cost of service study, Company agrees that it will file the updated customer usage and demand data as soon as possible after its availability but at least 45 days prior to the time by which the other parties are required to file their direct testimony. If there are not 45 days left in the procedural schedule between the date Company files the updated information and the date when the other parties' direct testimony is due, then Company agrees it will request a tolling of the statutory suspension period as may be necessary to allow the other parties at least 45 days to file their direct testimony after the date on which the updated customer usage and demand data are filed.

(3) Company shall file in its next general rate case a class cost of service study at the time the general rate case is filed, and include with or supplement that study with the customer usage and demand data described in (2), above. If the filing of Company's next rate case occurs prior to end of the summer 2008 peaking period and thus before the accumulation and compilation of the updated usage and demand data, Company agrees to provide the parties to that general rate case copies of the updated

usage and demand data collected or generated for use in preparing the update to the class cost of service study on a weekly basis as that data becomes available between the filing of the general rate case and the filing of the update to the cost of service study.. After filing the updated cost of service containing the updated usage and demand data, Company agrees to an expedited discovery process regarding the updated usage and demand data and cost of service study as follows; (i) Company shall file objections to such discovery requests within five (5) days, and (ii) to provide responses to such discovery requests within ten (10) days of receipt of the discovery request.

(c) The Parties acknowledge and represent to the Commission that each and every provision of this paragraph 11 is a reasonable resolution of each such issue, to which each of the Parties has agreed within the overall context of the Settlement.

12. The Amended Joint Stipulation and Settlement are based upon the Parties' analyses of the existing and foreseeable financial condition of Company and the existing statutory and regulatory framework that imposes certain obligations upon Company.

13. The Parties support this Settlement and this Amended Joint Stipulation and state that it resolves all issues raised in Company's rate case. Based on the record, the Parties agree and recommend that the Commission accept this Amended Joint Stipulation in complete resolution of this case.

14. Nothing in this Amended Joint Stipulation shall prevent Company from filing with the Commission and entering into Special Contracts for specific customers

which provide rates that are different from those set forth in Company's filed tariffs and from seeking Commission approval of rate experiments of limited application. Nothing in this Amended Joint Stipulation shall prevent the other Parties from taking whatever position they deem appropriate in relation to any such proposed Special Contracts or rate experiments.

15. This Amended Joint Stipulation is entered into subject to the acceptance and approval of the Commission. It results from a review of all filings in this case, the Commission Orders entered December 7 and 21, 2007, the evidence presented at the December 17, 2007, hearing, and extensive negotiation both before and after the issuance of the December 21 Commission Order. This Amended Joint Stipulation reflects substantial compromises and modifications by the Parties of their respective positions asserted in this case and is being proposed to expedite and simplify the resolution of these proceedings and other matters in the context of an overall Settlement. It is made without any admission or prejudice to any positions that any of the Parties might adopt during subsequent litigation in this or any future proceeding.

16. The Parties adopt this Amended Joint Stipulation as being in the public interest, without adopting any of the compromise positions set forth herein as ratemaking principles applicable to future regulatory proceedings, except as may otherwise be provided herein. The Parties note that in the December 21, 2007 Order, the Commission indicated its appreciation of the reluctance of parties to stipulated settlements to be bound

in future cases by virtue of their agreements on substantive issues in a settled case, and that a disclaimer of the type appearing in the preceding sentence, which is part of virtually every settlement agreement filed with the Commission, should be respected as it fosters the development of settlements in contested cases without prejudice to the parties entering into the settlement. *December 21 Order at 2-3.* The Parties' willingness to execute this Amended Joint Stipulation is predicated upon the disclaimer in the first sentence of this paragraph 16 and the Commission's endorsement of such disclaimers as provided in the December 21, 2007 order. Moreover, the Parties affirmatively state that in recommending to the Commission that it can and should approve the Settlement on the basis of a finding that a particular adjustment is reasonable in the context of the overall Settlement reflected in this Amended Joint Stipulation, no inference can or should be made as to the willingness of any Party to recommend or support the same or a similar resolution of the same issue in a future case, either in the context of the Party's evidentiary presentation in such future case or its position during settlement negotiations in such future case. The Parties further acknowledge that it is the Commission's prerogative to accept, reject, or modify any stipulation. However, each component of the Settlement, and in particular the resolution of each disputed issue and the provisions of this paragraph 16, is integral to the others. None of the Parties advocates the Commission's resolution of any issue as proposed in this Amended Joint Stipulation other than in the context of their support for the Settlement as a whole. Accordingly, in

the event that the Amended Joint Stipulation is modified or rejected by the Commission, it is expressly understood that the Parties are not bound to accept the Amended Joint Stipulation as modified or rejected, and may avail themselves of whatever rights are available to them under law and the Commission's Rules of Practice and Procedure.

17. The other parties to this case that have endorsed this Amended Joint Stipulation (i.e., those other than the Company, the Staff, the CAD, and the Industrials) are not parties to and have not approved the terms of the Settlement. These parties, however, have agreed not to oppose the Settlement or the approval of the Amended Joint Stipulation by the Commission.

WHEREFORE, the Parties on the basis of all of the foregoing respectfully recommend and request that the Commission make appropriate findings of fact and conclusions of law adopting and approving the Amended Joint Stipulation in its entirety, including the attached Exhibits 1 and 2.

Respectfully submitted,

John Philip Melick (State Bar #2522)
Christopher L. Callas (State Bar #5991)
Counsel for West Virginia-American Water Company

Meyishi Blair (State Bar #360)
Counsel for the Staff of the Public Service Commission of West Virginia

David A. Sade (State Bar #3229)
Counsel for the Consumer Advocate

Lee F. Feinberg (State Bar #1173)
Counsel for Kanawha Valley Chemical Manufacturers, and SWVA, Inc.

Thomas N. Hanna (State Bar #1581)
Counsel for the County Commission of Kanawha County and the Regional Development Authority of Charleston, Kanawha County, W. Va. Metropolitan Region (solely to acknowledge their lack of opposition to the Joint Stipulation, not their support for it)

Lee F. Feinberg (State Bar #1173)
Counsel for City of Charleston (solely to acknowledge the City's lack of opposition to the Joint Stipulation, not its support of it)

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EXHIBIT 1

General Service Territory

	Rates Effective July 1, 2005	Current Rates	Proposed Rates	
GENERAL DOMESTIC, COMMERCIAL AND INDUSTRIAL WATER SERVICE.				
5/8 -inch meter	17.28	17.28	19.86	1.1493
3/4-Inch meter	17.28	17.28	19.86	1.1493
1 -inch meter	42.33	42.33	48.66	1.1495
1 1/2 -inch meter	84.08	84.08	96.66	1.1496
2 -inch meter	134.22	134.22	154.30	1.1496
3 -inch meter	251.18	251.18	288.75	1.1496
4 -inch meter	418.24	418.24	480.80	1.1496
6 -inch meter	835.94	835.94	960.97	1.1496
8 -inch meter	1,337.19	1,337.19	1,537.19	1.1496
First 1,500 gallons				
Next 28,500 gallons	7.6617	7.6617	8.8077	1.1496
Next 870,000 gallons	5.0000	5.0000	5.8000	1.1600
Next 8,100,000 gallons	3.8400	3.8400	4.2200	1.0990
All over 9,000,000 gallons	2.8000	2.8000	2.7450	0.9804
WHOLESALE WATER SERVICE.				
5/8 -Inch meter	17.28	17.28	19.86	1.1493
3/4-Inch meter	17.28	17.28	19.86	1.1493
1 -Inch meter	42.33	42.33	48.66	1.1495
1 1/2 -inch meter	84.08	84.08	96.66	1.1496
2 -inch meter	134.22	134.22	154.30	1.1496
3 -inch meter	251.18	251.18	288.75	1.1496
4 -inch meter	418.24	418.24	480.80	1.1496
6 -inch meter	835.94	835.94	960.97	1.1496
8 -Inch meter	1,337.19	1,337.19	1,537.19	1.1496
First 1,500 gallons				
Next 28,500 gallons	7.6617	7.6617	8.8077	1.1496
Next 870,000 gallons	5.0000	5.0000	5.7478	1.1496
Next 8,100,000 gallons	3.8400	3.8400	4.4143	1.1496
All over 9,000,000 gallons	2.7064	2.7064	3.1112	1.1496
PRIVATE FIRE SERVICE				
2 - INCH SERVICE		69.59	80.00	1.1496
3 - INCH SERVICE		158.23	181.90	1.1496
4 - INCH SERVICE		277.81	319.36	1.1496
6 - INCH SERVICE		704.18	809.50	1.1496
8 - INCH SERVICE		1,154.78	1,327.50	1.1496
10 - INCH SERVICE		2,048.71	2,355.13	1.1496
12 - INCH SERVICE		2,870.79	3,300.17	1.1496

West Virginia American Water
Case No. 07-0998-W-42T
Revenue Deficiency Calculation for Settlement

Overall Weighted Cost of Capital	7.95%
Return on Equity	10.00%
Rate Base	401,308,541
Return on Rate Base	31,904,029
Federal Taxes	4,639,182
State Taxes	1,735,603
Operation & Maintenance Expenses	51,577,485
Depreciation Expense	14,064,490
Taxes Other Than Income Taxes	13,296,899
Subtotal	117,217,688
Going Level Revenues	103,341,198
Subtotal	13,876,490
Additional Uncollectibles	239,468
Additional B & O	638,667
Revenue Increase	14,754,625

	Revenue Requirement	Revenue Requirement Difference
Original Filing	24,065,516	
Adjustments to Company's Original Filing:		
1. Revision to Filing to primarily reflect maintenance reclass & going-level revenues	22,508,991	(1,556,525)
2. Reduction to Rate Base	21,461,963	(1,047,028)
3. Remove 3% Inflation in Man. Fees	21,181,468	(280,495)
4. Used Staff's adjustments to Benefit, Work. Comp. costs and Capital ratio	21,145,222	(36,246)
5. Used Staff's 3-Year Amtz. Of Rate Case Expense	20,950,022	(195,200)
6. Withdrew Low Income Tariff Request	20,843,694	(106,328)
7. Recognize 1/2 Tank Maintenance & Valve Operation	20,365,218	(478,476)
8. Synchronize Depreciation to revised rate base	20,127,650	(237,568)
9. Staff Changes to Property & Payroll Taxes	20,025,527	(102,123)
10. Used Staff's Capital Structure & Reduced ROE to 10.00 %	16,906,356	(3,119,171)
11. Used Staff's Weighted Costs of Debt	16,864,384	(41,972)
12. Used CAD's Composite Rate for FIT of 21.02 %	15,238,237	(1,626,148)
13. Staff's adjustment to Uncollectible	15,194,326	(43,911)
14. Staff's adjustment to Forfeited Discounts	15,167,966	(26,360)
15. Staff's adjustment to B & O Taxes	15,022,886	(145,080)
16. Staff's Adj. to eliminate pay raise 3% and 2 new salaried positions	14,754,625	(268,261)

West Virginia American Water
Case No. 07-0998-W-42T
Company Calculated Capitalization for the Settlement

	Capital Structure	% of total	Effective Cost To Co	Weighted Cost
Short Term Debt	2,207,284	0 53%	4 62%	0 02%
Long Term Debt	243,273,156	58 68%	6 55%	3 85%
Preferred Stock	2,199,304	0 53%	8 62%	0 05%
Common Equity	166,887,622	40.26%	10 00%	4.03%
Total Capitalization	414,567,366	100.00%		7.95%