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BEFORE THE PUBLIC SERVICE COMMISSION

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PUBLIC SERVICE  
COMMISSION

IN THE MATTER OF:

THE APPLICATION OF KENTUCKY-AMERICAN )  
WATER COMPANY FOR A CERTIFICATE OF ) CASE NO. 2007-00134  
CONVENIENCE AND NECESSITY AUTHORIZING )  
THE CONSTRUCTION OF KENTUCKY RIVER )  
STATION II, ASSOCIATED FACILITIES AND )  
TRANSMISSION MAIN )

KENTUCKY-AMERICAN WATER  
COMPANY'S POST-HEARING BRIEF

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## **I. INTRODUCTION**

This case involves Kentucky-American Water Company's ("KAW") Application under KRS 278.020(1) for a certificate of convenience and necessity authorizing the construction of Kentucky River Station II adjacent to Pool 3 of the Kentucky River ("KRS II"), associated facilities and transmission main (collectively "Facilities" or "Pool 3 option" or "KAW proposal"). KAW and its regional partner, the Bluegrass Water Supply Commission ("BWSC"), have a need for the Facilities as established in previous Public Service Commission ("Commission") proceedings and the filings in this case. KAW has also established that the construction of the Facilities is both reasonable and cost-effective and will not result in a wasteful investment or duplication of facilities. Indeed, KAW has established that the construction of the Facilities is the most reasonable and least cost solution for the Central Kentucky water supply problem. The construction of the Facilities will allow KAW to continue to provide to its customers a reliable supply of potable water through the year 2030. Accordingly, and for all the reasons set forth below, the Commission should grant a certificate that will allow construction of the Facilities at 20 MGD and that further allows construction of the Facilities at 25 MGD in the event BWSC elects to participate.

## **II. PROCEDURAL HISTORY**

On March 14, 2006,<sup>1</sup> KAW announced publicly its intention to construct facilities on the Kentucky River to solve the Central Kentucky water supply problem. A little over a year later, on March 30, 2007, KAW filed its Application in this case. By that time, KAW had designed the Facilities, applied for and obtained numerous permits necessary for the construction and

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<sup>1</sup> On that date, KAW and many others attended an informal conference at the Commission for the purpose of discussing plans to solve the regional water supply problem as part of Case No. 2001-00117.

operation of the Facilities, completed detailed cost studies for the Facilities, obtained rights to real estate that would be necessary for the Facilities, and conducted numerous meetings and informational sessions with citizens and affected landowners who are concerned about the project. In short, KAW had performed an enormous amount of work, as it should have, before it filed its Application in this case, all in accordance with the rigorous requirements of 807 KAR 5:001, Section 9. The Commission entered a procedural schedule for the case on April 20, 2007. As expected, numerous entities<sup>2</sup> intervened in time to allow them to participate fully in the case.

On July 30, 2007, after extensive discovery had occurred and after the Commission had served an open records request on the Louisville Water Company (“LWC”), LWC moved to intervene in the case so that it could “help the Commission understand the Louisville Water Company documents it is receiving pursuant to the Open Records Act.”<sup>3</sup> LWC filed the testimony of its President, Mr. Greg Heitzman, along with its Motion to Intervene. In that testimony, Mr. Heitzman set forth what he termed a “proposal” by which LWC alleged it could solve the Central Kentucky water supply problem more cheaply than KAW and BWSC.<sup>4</sup>

After the Commission granted LWC’s Motion to Intervene, LWC sought and was granted additional time to respond to discovery requests. In the September 5, 2007 Order granting additional time, the Commission stated that Mr. Heitzman had provided “few specifics” to support LWC’s claim that LWC could solve the Central Kentucky water supply problem more

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<sup>2</sup> Those intervenors are: the Attorney General (“AG”); the Lexington-Fayette Urban County Government (“LFUCG”); Citizens for Alternative Water Solution (“CAWS”); the Kentucky River Authority (“KRA”); the Kentucky Industrial Utility Customers (“KIUC”); and the BWSC.

<sup>3</sup> LWC’s July 30, 2007 Motion for Full Intervention, p. 3, ¶ 10.

<sup>4</sup> Heitzman July 30, 2007 Direct Testimony, p. 3.

cheaply than KAW's proposal.<sup>5</sup> Likewise, the Commission stated that Mr. Heitzman offered "no supporting documentary evidence" for that claim other than a copy of a presentation made to the LFUCG Council.<sup>6</sup> The additional time allowed LWC more than sufficient time to fully develop its pipeline idea and related discovery responses.

In accordance with the Commission's procedural schedule, public hearings were conducted in Owen County, Lexington and Frankfort on September 10, 12 and 13, 2007, respectively. Those hearings were held for the purpose of receiving oral comment from members of the public wishing to provide such comment.

The Commission also conducted the first evidentiary hearing in the case from November 26 – 28, 2007 (the "November Hearing"). In the course of the November Hearing, hearing data requests were made upon LWC and KAW. LWC and KAW responded to those requests on December 10, 2007. Post-hearing briefs were due no later than December 27, 2007, but, on December 21, 2007, the Commission amended the procedural schedule and ordered certain parties to provide responses to post-hearing data requests no later than January 9, 2008. The Commission's December 21, 2007 Order also directed the parties to submit post-hearing briefs no later than January 16, 2008. Finally, the December 21, 2007 Order directed all parties to address in their post-hearing briefs four issues identified in Appendix E to the order.

On January 11, 2008, even though three days' worth of evidentiary hearing and exhaustive discovery had occurred, the LFUCG moved the Commission to amend the procedural schedule to allow more time for "the Louisville Water Company or any other party offering a

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<sup>5</sup> September 5, 2007 Order, p. 2.

<sup>6</sup> Id.

responsible solution to present their most thorough, comprehensive, and final proposals”<sup>7</sup> to the LFUCG.<sup>8</sup> The Commission granted the LFUCG’s motion and amended the procedural schedule again. In its January 16, 2008 Order, the Commission imposed a deadline of February 11, 2008 for all parties to submit new evidence regarding alternative means of expanding KAW’s water supply and required that any new evidence be in the form of verified written testimony. February 11, 2008 came and went and the LFUCG filed nothing.

Although the LFUCG filed nothing on February 11, 2008, LWC and CAWS seized the opportunity to file “new” and revised testimony. LWC submitted the supplemental testimony of Mr. Heitzman and LWC expert witness Dr. Edward Wetzel and CAWS submitted the testimony of Dr. Martin Solomon. In accordance with the procedural schedule issued on January 16, 2008, several parties requested another evidentiary hearing. That evidentiary hearing took place on March 5 – 6, 2008 (the “March Hearing”) and was conducted for the “limited purpose of considering [the February 11, 2008 new testimony] and affording those parties the opportunity to cross-examine those persons who have presented written testimony and to present verbal rebuttal evidence.”<sup>9</sup>

### **III. OVERVIEW OF THE PROPOSED PROJECT**

KAW owns and operates facilities for the production of treated water for its area of service formerly known as its Central Division.<sup>10</sup> The Kentucky River Station I ("KRS I") is located adjacent to Pool 9 of the Kentucky River and utilizes raw water from Pool 9. It has a

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<sup>7</sup> See the Exhibit No. 1 (Resolution No. 8-2008) attached to LFUCG’s January 11, 2008 Motion.

<sup>8</sup> On January 15, 2008, LWC, did, in fact, make a presentation to the LFUCG Council.

<sup>9</sup> January 16, 2008 Order, p. 2.

<sup>10</sup> During the pendency of this case, the Commission approved the imposition of single tariff pricing in Case No. 2007-00143 which, for practical purposes, results in the elimination of different “divisions” of KAW’s service territory.

rated production capacity of 40 million gallons per day ("MGD"). The Richmond Road Station ("RRS") is located at 2300 Richmond Road, Lexington, Kentucky, and utilizes raw water either pumped from Pool 9 of the Kentucky River or Jacobson Reservoir. It has a rated production capacity of 25 MGD. Jacobson Reservoir has a capacity of 500 million gallons of water, a limited geographical watershed, and most of the water that refills the reservoir is pumped from Pool 9 of the Kentucky River; therefore, Pool 9 of the Kentucky River is essentially the only source of supply of raw water for KAW.

As set forth in more detail in Section IV below, the supply and production capacity of KAW's current treatment plants, KRS I and RRS, are inadequate to meet its current obligations. To address these inadequacies, KAW has concluded that the most cost-effective and feasible solution to the source of supply and treatment deficits is the construction of KRS II, which includes a raw water intake, raw water pumping station, and water treatment plant located adjacent to Pool 3 on the Kentucky River with an associated transmission main and required booster station and water storage tank.

A copy of the plans for KRS II is attached to KAW's Application in this case as Exhibit A-Plans. A copy of the specifications for KRS II, including the Basis of Design Report and its Addendum No. 1, are attached to KAW's Application in this case as Exhibit A-Specifications. KRS II has a design capacity of 20 MGD. The intake, pumping station and water treatment plant will be located approximately two miles north of Swallowfield on the Kentucky River along the Owen and Franklin County line. A copy of the plans for approximately 160,000 linear feet of the 42-inch diameter transmission main is attached to KAW's Application as Exhibit B-Plans. A copy of the specifications for approximately 160,000 linear feet of the 42-inch diameter transmission main is attached to KAW's Application as



Exhibit B-Specifications. The transmission main will generally follow the established transportation corridors of US 127, KY 2919, KY 1707, KY 1262, US 460 and KY 1973 from the new plant site to Fayette County. A copy of the plans and specifications for the booster pump station and water storage tank are attached to KAW's Application as Exhibit C-Plans and Exhibit C-Specifications, respectively.

As with any project of this nature, many permitting requirements exist that must be met prior to the commencement of construction. KAW listed the required permits at Paragraph 14 of its Application. In his November 13, 2007 rebuttal testimony,<sup>11</sup> Mr. Rich Svindland explained that all pre-construction permits had been obtained except the USACE 404 Permit (which has since been obtained and was filed in the record on November 20, 2007) and utility highway encroachment permits. Based on discussions with the Kentucky Transportation Cabinet, those utility highway encroachment permits are expected but will not be issued until after the Commission decides this case. Receipt of those permits will mean that KAW has obtained all pre-construction permits.

When KAW filed its Application, it estimated the cost to construct the Facilities to be approximately \$160 million. Since that estimate was made, KAW received bids for the construction of the Facilities which substantiated the reasonableness of KAW's \$160 million estimate (which included a construction-only estimate of \$122,633,961<sup>12</sup> and "soft costs" for legal, permitting, engineering, land, administrative, financing, and contingency estimates). The actual bids received (with the options KAW is likely to choose) were for a construction estimate

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<sup>11</sup> Svindland November 13, 2007 Rebuttal Testimony, p. 2.

<sup>12</sup> See A.W. Turner's December 19, 2007 e-mail to all parties.

of \$121,529,787 for a 20 MGD facility.<sup>13</sup> In other words, KAW's construction estimate missed the mark by less than 1%.

KAW has the opportunity to secure the requisite financing for the Facilities through American Water Capital Corp., another wholly-owned subsidiary of American Water Works Company. As described in the Direct Testimony of Mr. Lou Walters, Assistant Treasurer of American Water, KAW intends to finance the initial cost of construction of the Facilities through short-term debt and, when required by financial considerations, convert the short-term debt to an appropriate percentage of long-term debt and equity to be contributed by American Water Works Company.

The BWSC was created pursuant to KRS 74.420, et seq., and presently has as its members the Frankfort Water and Electric Plant Board, Georgetown Municipal Water and Sewer Service, Paris, Cynthiana, Nicholasville, Mt. Sterling, Lancaster, Berea, Winchester Municipal Utilities and the LFUCG. It is a regional alliance of government agencies and water utilities that has been working cooperatively with KAW to address the water supply deficit in Central Kentucky. In furtherance of the cooperative effort with KAW, BWSC contracted with KAW for the plans and specifications of KRS II to include an additional design capacity of 5 MGD of potable water for BWSC use.<sup>14</sup> Additionally, during the pendency of this case, KAW and BWSC executed a contract that allows BWSC several participation options, including the possibility of a 20% equity ownership position in the Facilities.<sup>15</sup> If BWSC exercises one of the options available to it under that contract, the Facilities will be built to provide 25 MGD instead

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<sup>13</sup> Id.

<sup>14</sup> A copy of that contract is attached to KAW's Application as Exhibit E.

<sup>15</sup> See LWC November Hearing Exhibit No. 6.

of 20 MGD. Therefore, KAW respectfully requests that the Commission grant a certificate that will allow construction of the Facilities for 20 MGD and that further allows construction of the Facilities at 25 MGD in the event BWSC elects one of the options set forth in the November 20, 2007 contract between KAW and BWSC.

#### **IV. ARGUMENT**

##### **A. KAW’S REQUEST FOR A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY SHOULD BE GRANTED.**

The statutory requirement for certificates of public convenience and necessity is contained in KRS 278.020(1), which states:

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

Kentucky’s highest court has construed “public convenience and necessity” to mean: (1) there is a need for the proposed facility or service; and (2) the new facility or service will not create wasteful duplication.<sup>16</sup>

A finding of “need” is supported where there has been a showing of “a substantial inadequacy of existing service” due to a deficiency of service facilities beyond what could be supplied by normal improvements in the ordinary course of business.<sup>17</sup> “Substantial inadequacy of existing service” is not required to be a currently-existing deficiency, but rather may be a deficiency expected a number of years into the future “in view of the long range planning

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<sup>16</sup> Kentucky Utilities Co. v. Public Service Commission, 252 S.W.2d 885, 890 (Ky. 1952).

<sup>17</sup> Id.

necessary in the public utility field.”<sup>18</sup> The prevention of “wasteful duplication” has been interpreted to mean not only a physical multiplicity of facilities, but also an avoidance of “excessive investment in relation to productivity or efficiency.”<sup>19</sup> In considering the efficiency of a proposed project, the Commission is not restricted to making a close comparison of the rates that would result from various options.<sup>20</sup> In other words, although cost is a factor, it is not the only factor to be considered. As long as the project is reasonable and feasible, it meets that standard set forth in 278.020(1).<sup>21</sup> The standard has been succinctly described as follows:

As we view it, if the . . . proposal is feasible (capable of supplying adequate service at reasonable rates) and will not result in wasteful duplication, the Public Service Commission is authorized to grant a certificate . . . .<sup>22</sup>

#### **1. THE FACILITIES ARE NEEDED.**

The record in this case is replete with proof that the Facilities are needed. Indeed, the fact of need was all but uncontested in this case until February 11, 2008. As a public utility in the Commonwealth of Kentucky and regulated by the Commission, KAW must comply with the following regulations:

(1) 807 KAR 5:066, Section 3(2)(c) – “In absence of comparable requirements of the Natural Resources Cabinet, water supplied by any utility shall be: (c) From a source reasonably adequate to provide a continuous supply of water.”

(2) 807 KAR 5:066, Section 4(1) – “Emergency interruptions. Each utility shall make all reasonable efforts to prevent interruptions of service and when such interruptions occur shall

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<sup>18</sup> Kentucky Utilities Co. v. Public Service Commission, 390 S.W.2d 168, 171 (Ky. 1965).

<sup>19</sup> Kentucky Utilities Co., 252 S.W.2d at 890.

<sup>20</sup> South Central Rural Telephone v Public Service Commission, 453 S.W.2d 257, 259 (Ky. 1970).

<sup>21</sup> Kentucky Utilities Co., 390 S.W.2d at 172 – 173.

<sup>22</sup> Kentucky Utilities Co., 390 S.W.2d at 175.

endeavor to reestablish service with the shortest possible delay consistent with the safety of its consumers and the general public."

(3) 807 KAR 5:066, Section 10(4) – "Water supply requirements. The quantity of water delivered to the utility's distribution system from all source facilities shall be sufficient to supply adequately, dependably and safely the total reasonable requirements of its customers under maximum consumption."

With those regulatory requirements in place, on November 19, 1993, the Commission initiated an investigation into the demand projections and sources of supply for KAW. In an Order dated March 14, 1995, the Commission found:

the range of the demand projections presented by Kentucky-American . . . is within the realm of reasonableness. Kentucky-American has used reputable sources for data and nationally accepted methodologies in developing its demand projections. Over the years Kentucky-American has made numerous revisions to its methodology for projecting water demand resulting in a state-of-the-art, dynamic process.<sup>23</sup>

The Commission also addressed the safe yield of Pool 9 of the Kentucky River by stating, "Using the drought of record, the safe yield from the Kentucky River and existing reservoirs is only 35 MGD."<sup>24</sup> Subsequent to that Order, on April 24, 1995, the Commission ordered that Case No. 93-434 should remain open to await a new safe-yield analysis of the Kentucky River to be performed by The Kentucky Water Resources Research Institute ("KWRRRI").

The KWRRRI analysis showed a source of supply deficit for KAW of 6.57 billion gallons of water, or 35.95 MGD during the recurrence of the drought of record. Recognizing the inadequacy of the Kentucky River during a drought of record, by Order dated August 21, 1997, the Commission pointed out that additional steps should be taken and financial resources would

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<sup>23</sup> Case No. 93-434, *An Investigation of the Sources of Supply and Future Demand of Kentucky-American Water Company*, Order dated March 14, 1995, pp. 4-5.

<sup>24</sup> *Id.*, p. 6.

have to be committed to develop an adequate and reliable source of supply for all citizens served by the Kentucky River. Finally, and most importantly, the Order also directed KAW 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."<sup>25</sup> In short, the Commission has already determined that a need exists. As a result, on May 15, 2001, the Commission instituted Case No. 2001-117, *An Investigation into the Feasibility and Advisability of Kentucky-American Water Company's Proposed Solution to its Water Supply Deficit*, in part to ascertain the cost and likelihood of the implementation of plans to meet KAW's source of supply deficit.<sup>26</sup>

In Ms. Linda Bridwell's Direct Testimony in this case, she provided an exhaustive account of the 20-year history of KAW's efforts to solve the source of supply problem and its treatment capacity deficit.<sup>27</sup> KAW will not repeat that history here, but the single most important conclusion to be drawn from the 20-plus years of work that has been performed is reflected in Tables 1 and 2 of Ms. Bridwell's Direct Testimony. Those tables show that there is an immediate, not future, need for an increased source of supply and treatment capacity. For example, if another drought of record recurs in 2010, KAW projects that the average daily demand for treated water by its customers would be 55 MGD. During such a recurrence, the safe yield of Pool 9 of the Kentucky River, as confirmed by multiple studies and as recognized by the Commission, is 35 MGD of raw water. Thus, a source of supply deficit is clear. Table 2 of Ms.

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<sup>25</sup> Case No. 93-434, Order dated August 21, 1997, p. 6.

<sup>26</sup> Case No. 93-434 and Case No. 2001-00117 were incorporated into this case by the Commission's Order of August 1, 2007.

<sup>27</sup> Bridwell March 30, 2007 Direct Testimony, pp. 3 – 26.

Bridwell's Direct Testimony shows that, in 2010, KAW's treatment plant rated capacity of 65 MGD falls 10 MGD short of meeting the projected 2010 maximum day demand. Of course, as shown in Table 2 of Ms. Bridwell's Direct testimony, the deficits increase over time.

Up until February 11, 2008, the intervenors in this case who had addressed the issue of need all agreed that a need exists. First, the AG's expert witness, Mr. Scott Rubin, opined that a need exists.<sup>28</sup> Additionally, LWC agrees that a need exists by virtue of its own idea on how to solve the source of supply problem in Central Kentucky.<sup>29</sup> Further, Mr. Heitzman testified at the November Hearing that a need exists.<sup>30</sup> Interestingly, in Mr. Heitzman's later February 11, 2008 testimony, he claims that KAW's urgency is "purely a manufactured emergency,"<sup>31</sup> yet on the very same page of that testimony he says "LWC takes no issue with the urgent need for a solution to Central Kentucky's water supply deficit."<sup>32</sup> Finally, even CAWS' witness, Ms. Elizabeth Felgendreher, testified that a need exists:

CAWS accepts that, using the drought of record as the benchmark for determining need for water supply for KAWC's customer base, that demand would exceed available supply during a prolonged drought absent some action.<sup>33</sup>

Both Mr. Rubin and Ms. Felgendreher opine that KAW should take steps toward better demand management, and Mr. Rubin recommends that KAW hire a qualified conservation consultant to develop a program that is consistent with the best conservation practices existing in

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<sup>28</sup> Rubin July 30, 2007 Direct Testimony, pp. 5 – 7.

<sup>29</sup> Heitzman October 1, 2007 Rebuttal Testimony, p. 4.

<sup>30</sup> TE November Hearing, Volume III, p. 323.

<sup>31</sup> Heitzman February 11, 2008 testimony, p. 17, line 18.

<sup>32</sup> Heitzman February 11, 2008 testimony, p. 17, lines 3 – 4.

<sup>33</sup> Felgendreher July 30, 2007 Direct Testimony, p. 3.

the water industry. KAW has committed to that hiring.<sup>34</sup> However, KAW has also proven that conservation alone has been and would be an inadequate method to solve the supply deficit and treatment capacity problems,<sup>35</sup> a conclusion with which Mr. Rubin agreed.<sup>36</sup>

Despite the findings in Case No. 93-434 and the consensus of the parties who had addressed the issue, on February 11, 2008, CAWS submitted the pre-filed testimony of Dr. Martin Solomon. In his testimony, Dr. Solomon opines that KAW has not established a need for the Facilities. In support of that opinion, he prepared a graph<sup>37</sup> that projects water demand through 2030. As depicted in the graph and discussed by Dr. Solomon at the March Hearing, he merely took two data points (one point for the average daily demand for 2000 and another point for the average daily demand for 2006) and, using a ruler, “extrapolated” those two data points to project demand through 2030.

The problems with Dr. Solomon’s “demand analysis” are legion. First, he is not qualified as an expert on the issue of water demand forecasting. He testified that, before this case, he has never prepared a water demand forecast analysis and that he has never provided sworn testimony on the subject of water demand forecasting.<sup>38</sup> Although he claims that additional treated water can be obtained with “technology” without adding treatment plant, he could only describe the technology as “tubes” and “sand” with no further elaboration.<sup>39</sup> Second, he admitted on cross-examination that he has no familiarity with Case No. 93-434 which, of course, was the case

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<sup>34</sup> TE November Hearing, Volume I, p. 128 and Bridwell November 13, 2007 Rebuttal Testimony, p. 9.

<sup>35</sup> Bridwell March 30, 2007 Direct Testimony, pp. 28 – 30.

<sup>36</sup> Rubin July 30, 2007 Direct Testimony, p. 4.

<sup>37</sup> See Exhibit 3 to Dr. Solomon’s February 11, 2008 Testimony.

<sup>38</sup> TE, March Hearing, Volume I, p. 248.

<sup>39</sup> TE, March Hearing, Volume I, p. 274.



established to investigate KAW's demand model, projections and source of supply. Indeed, he testified that he is not even *aware* of that case, despite its incorporation into this case.<sup>40</sup> Certainly, for any testimony concerning demand to be taken seriously, the offering witness should have become familiar with the two cases that investigated demand and source of supply that have been incorporated into this case.

If Dr. Solomon had taken the time to review Case No. 93-434, he would have learned that KAW's demand model, which was used to derive the demand projections set forth in Tables 1 and 2 of Ms. Bridwell's Direct Testimony, utilizes a host of relevant variables such as population growth, historical demand, weather, leakage, non-revenue usage, conservation measures, plumbing code changes, and price elasticity for indoor and outdoor water use.<sup>41</sup> Certainly, that model is much more comprehensive and provides much more valid demand projection results than Dr. Solomon's "extrapolation by ruler" results. As mentioned above, the Commission has described KAW's demand model as "state of the art" and "dynamic."<sup>42</sup> Finally, it is clear that Dr. Solomon fails to understand the difference between average day demand and peak day demand. He claims that KAW need only meet its customers' average day demand. Of course, this Commission and the governing regulations require KAW to meet its customers' "maximum consumption."<sup>43</sup>

In conclusion, KAW has a source of supply deficit and the rated capacities of its current treatment plants, KRS I and RRS, are inadequate to meet its future obligations.

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<sup>40</sup> TE, March Hearing, Volume I, pp. 248, 276.

<sup>41</sup> See March 14, 1995 Order in Case No. 93-434 (KAW March Hearing Exhibit No. 10), pp. 2-3.

<sup>42</sup> See March 14, 1995 Order in Case No. 93-434 (KAW March Hearing Exhibit No. 10), p. 5.

<sup>43</sup> See August 21, 1997 Order in Case No. 93-434 (KAW March Hearing Exhibit No. 11), p. 6 and 807 KAR 5:066, Section 10(4).

**2. THE FACILITIES WILL NOT RESULT IN A WASTEFUL INVESTMENT OR DUPLICATION OF FACILITIES, AND, THEREFORE, ARE REASONABLE UNDER EXISTING AND FORESEEABLE CIRCUMSTANCES.**

KAW has determined that the Facilities are the best solution to meet the established need. In making that determination, KAW had to answer the most basic question in this case: what is the best available source of supply. After much study, KAW determined that Pool 3 of the Kentucky River would be best because it has adequate supply through any reasonable planning horizon and is the least cost alternative.

**a. Pool 3 Has An Adequate Supply Through Any Reasonable Planning Period**

Pool 3 of the Kentucky River has more than adequate flow to supply the long-term needs of KAW and BWSC. In response to Chairman Goss' pointed questions on this issue at the November Hearing, KAW witness Mr. Rich Svindland explained<sup>44</sup> that he has reviewed the data provided by the United States Geological Survey, which tracks Kentucky River flows at Pool 2, Pool 4 and Elkhorn Creek as it enters Pool 3. He reviewed voluminous historical flow information and was even able to review flow information for 2007, which was an extremely dry year. That information<sup>45</sup> shows that the lowest seven-day average at Pool 2 in 2007 was 81 MGD<sup>46</sup> and that the lowest seven-day average at Pool 4 plus Elkhorn inflow was 67 MGD.<sup>47</sup> KAW has demonstrated that the expected seven-day average low flow at Pool 3 during a major drought is estimated to be 78 MGD<sup>48</sup> without pool mining or improvements to Lock and Dam 3.

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<sup>44</sup> TE November Hearing, Volume II, pp. 336 – 341.

<sup>45</sup> KAW also attached the data to its response to November Hearing Data Request No. 5.

<sup>46</sup> See attachment to KAW's Response to November Hearing Data Request No. 5, p. 8 of 30.

<sup>47</sup> See attachment to KAW's Response to November Hearing Data Request No. 5, p. 30 of 30.

<sup>48</sup> KAW Response to November Hearing Data Request No. 5.

Clearly, Pool 3 contains adequate flow for the 20-25 MGD proposed Facilities. These numbers provide further support for the KAW November Hearing testimony that the KRA-planned capital improvements (for example, crest gates) to Dam 3 are not necessary for Pool 3 to have an adequate supply for KRS II.<sup>49</sup>

In addition to Mr. Svindland's testimony, the record in this case contains a safe yield analysis for Pool 3.<sup>50</sup> That analysis states, "based on the USGS gaging station data, it appears that Pool 3 has a safe yield greater than 30 mgd" and "based on the information reviewed, Pool 3 of the Kentucky River has a safe yield in excess of 30 mgd."<sup>51</sup> In his February 11, 2008 testimony, Mr. Heitzman strongly criticized KAW for not having a safe yield analysis for Pool 3. However, that criticism is clearly misplaced as evidenced by the very existence of the safe yield analysis that has been in the record since May 21, 2007. Indeed, upon cross-examination, Mr. Heitzman admitted that he has never reviewed the safe yield analysis and that he has no information that would support disagreement with the conclusions of the safe yield analysis.<sup>52</sup> Eventually, Mr. Heitzman admitted "there appears to be an adequate supply on Pool No. 3."<sup>53</sup>

LWC and CAWS made much ado at the November Hearing about the Kentucky Division of Water's issuance of a withdrawal permit<sup>54</sup> to KAW that allows withdrawal from Pool 3 of "only" 20 MGD in June, July and August and 6 MGD in all other months. As Ms. Bridwell

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<sup>49</sup> TE November Hearing, Volume I, pp. 173 – 174.

<sup>50</sup> See Appendix A of Gannett Fleming's March 2007 Water Supply Study filed by KAW on May 21, 2007 in response to Item No. 6 of the Commission Staff's First Set of Interrogatories and Request for Production of Documents. Also see KAW March Hearing Exhibit No. 7.

<sup>51</sup> See page A-9 of the Gannett Fleming March 2007 Water Supply Study.

<sup>52</sup> TE March Hearing, Volume I, pp. 75, 78.

<sup>53</sup> TE March Hearing, Volume I, p. 109.

<sup>54</sup> Withdrawal Permit No. 1572 is attached to KAW's Application as Exhibit G.

explained, KAW's permit application, in keeping with customary DOW permit practice,<sup>55</sup> was for only the amounts it projects it will need on a regular basis. Moreover, the withdrawal amounts are considered excessive only if they exceed the permitted amounts by 15% on a 30-day *average*.<sup>56</sup> Furthermore, the permit explicitly states that the conditions in the permit may be temporarily altered in emergency situations. Given that 2007 flows at Pool 3 were approximately three times the amount KAW and BWSC project they will need, it is reasonable to assume that, in the event of an emergency need to withdraw more than the permitted amount, the DOW would allow it.

AG November Hearing Exhibit No. 4<sup>57</sup> provides even further support that Pool 3 is adequate. That DOW document, which was generated as part of KAW's Pool 3 permit application process, acknowledges that KAW "withdrawals could be up to 30.5 MGD." When cross examined, Mr. Heitzman admitted that he has no safe yield information to dispute the fact that Withdrawal Permit No. 1572 was properly issued.<sup>58</sup>

KRA's March Hearing exhibits establish that the planned refurbishing of Dam 3 will occur timely and will be completed close in time to the completion of the Facilities. The U.S. Army Corps of Engineers has given permission for the replacement of Dam 3.<sup>59</sup> The engineering design for the work is near completion<sup>60</sup> and the construction schedule shows a construction

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<sup>55</sup> TE November Hearing, Volume II, p. 107.

<sup>56</sup> TE November Hearing, Volume II, p. 106.

<sup>57</sup> AG November Hearing Exhibit No. 4 entitled "Surface Water Permit Fact Sheet" is the Permit Fact Sheet that was created by DOW personnel as a result of KAW's Pool 3 Permit Application.

<sup>58</sup> TE March Hearing, Volume I, pp. 204 – 205.

<sup>59</sup> KRA March Hearing Exhibit No. 1.

<sup>60</sup> KRA March Hearing Exhibit No. 3.

completion date in mid-2010.<sup>61</sup> Funding for the Dam 3 project was approved as part of the KRA's 2006-2008 budget.<sup>62</sup> Thus, there is no basis for the argument that the KRA will not refurbish Dam 3 as necessary to ensure the reliability of Pool 3. Indeed, the KRA has specifically endorsed KRS II by a June 8, 2007 resolution that has been submitted to the Commission as part of this case.<sup>63</sup> Here again, Mr. Heitzman's strong criticism of KAW on the issue of the reliability of Dam 3 is misplaced as evidenced by the KRA documents that demonstrate Dam 3 will be refurbished no later than 2010. Upon cross-examination, Mr. Heitzman had to admit that the KRA March Hearing Exhibits establish that KRA's Dam 3 project is moving forward.<sup>64</sup>

**b. KAW's Proposal is the Least Cost Option to Address the Need.**

Independent consultants hired by the BWSC concluded that a Pool 3 solution is less expensive than any solution involving a pipeline to Louisville. The February 27, 2004 "O'Brien & Gere study," which was the subject of much discussion at the November Hearing, was prepared for the BWSC. That study was an exhaustive analysis of a Pool 3 solution compared to a "pipeline to Louisville"<sup>65</sup> solution. All things considered, the study concluded that the Pool 3 alternative is the preferred option based on its "highest overall score," which included first place rankings in implementability, flexibility and water quality."<sup>66</sup>

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<sup>61</sup> KRA March Hearing Exhibit No. 3, Appendix B.

<sup>62</sup> KRA March Hearing Exhibit No. 4.

<sup>63</sup> See KRA Executive Director Stephen Reeder's June 6, 2007 letter (with the KRA resolution enclosed) to Beth O'Donnell that has been filed in this case.

<sup>64</sup> TE March Hearing, Volume I, p. 180.

<sup>65</sup> The study considered information and proposals submitted by the Louisville Water Company. (O'Brien & Gere Study at 20).

<sup>66</sup> O'Brien & Gere Study at 3.

At the November Hearing, a statement in the O'Brien & Gere study that the Louisville Water Company proposal considered in that study was the "lowest cost alternative" engendered some discussion. However, that statement came under serious question as a result of a subsequent letter of clarification<sup>67</sup> in which O'Brien & Gere states that a Pool 3 solution "was both the highest rated and lowest cost, when compared 'apples to apples.'" (Emphasis in original). As the letter explains, an "apples to apples" comparison of a Pool 3 solution to a Louisville Water Company solution requires a comparable *guaranteed availability* of water.<sup>68</sup> The letter further explains that the LWC proposal O'Brien & Gere considered actually guaranteed an amount of water far *less* than the Pool 3 option to which it was compared. When that variable was controlled by imputing a cost to the LWC proposal to guarantee an equivalent amount of water, the Pool 3 option was "both the highest rated and lowest cost."<sup>69</sup> As explained in more detail below, one *must* include the cost of reserving an amount to drought-proof the region into any analysis of LWC's idea in this case. With that inclusion, any of the many LWC ideas that LWC has floated over time (including the various revisions of the idea that LWC has put forward in this case) become indisputably more expensive than the KAW proposal.<sup>70</sup> Indeed, the AG's witness, Mr. Rubin, testified that even under certain assumptions such as public

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<sup>67</sup> A copy of the October 12, 2005 clarification letter to Don Hassall of the BWSC from O'Brien & Gere was discussed at the November Hearing and is attached to KAW's May 21, 2007 response to Item No. 6 of the Commission's Staff's First Set of Interrogatories.

<sup>68</sup> O'Brien & Gere October 12, 2005 letter, p. 1.

<sup>69</sup> *Id.*

<sup>70</sup> A more detailed discussion of the cost comparison of the proposal that LWC made in this case versus the KAW proposal is set forth in Section IV.B. below.

ownership of the Louisville pipeline, the LWC idea would not cost significantly less than KAW's proposal.<sup>71</sup>

**c. Use of a 20-Year Planning Period is Reasonable.**

KAW has correctly used a 20-year planning horizon as part of its demand projection analysis. Water demand planning must necessarily be tied to population projections. For its demand study and projections, KAW uses Kentucky State Data Center population projection information, which goes out to the year 2030 and no further.<sup>72</sup> Any water demand planning based on a period longer than that time is therefore inherently suspect. Indeed, when the Commission ordered KAW to solve the water supply problem, it directed KAW "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."<sup>73</sup> In short, the Commission imposed a planning horizon of just over 20 years.

While LWC's cross-examination of Ms. Bridwell tried to make the point that the Commission should look beyond 2030 for water demand planning purposes, the Commission has already condoned KAW's 20-year demand planning horizon. Moreover, even if it had not, LWC's own documents and admissions prove that planning beyond a 20-year period is not only useless, it is dangerous. At the November Hearing, Mr. Heitzman admitted that a 1968 engineering report commissioned by LWC containing demand projections for a 32-year period

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<sup>71</sup> TE November Hearing, Volume II, p. 203.

<sup>72</sup> Bridwell November 13, 2007 Rebuttal Testimony, pp. 3 – 4.

<sup>73</sup> Case No. 93-434, Order dated August 21, 1997, p. 6.

had serious errors.<sup>74</sup> For example, it projected a daily average demand for the year 2000 of 260 MGD. In actuality, the LWC 2000 average daily demand was only 127 MGD – more than a 100% error. Likewise, the 1968 report projected the LWC 2000 maximum day demand to be 366 million gallons. In actuality, the maximum daily demand for LWC as of 2000 was only 188 million gallons. Thus, according to LWC’s own documents, use of such long planning periods is folly. LWC seems to have learned from its mistake in using such a lengthy planning period as evidenced by LWC’s use in its current strategic plan<sup>75</sup> of a planning horizon of just 14 years.<sup>76</sup> Additionally, Mr. Heitzman admitted that use of a 20-year planning period is reasonable.<sup>77</sup> Finally, Kentucky regulations contemplate, at most, a 20-year planning horizon for water demand planning.<sup>78</sup> Undoubtedly, KAW’s use of a 20-year planning horizon is appropriate.

**d. Many Changes Since the Late 1990’s Required KAW to Discard its Earlier Louisville Pipeline Plan and Implement its Current Pool 3 Proposal.**

KAW explained at the November Hearing why it has proposed the Facilities in this case when, in the late 1990’s, it actually favored and pursued a solution that included a pipeline to Louisville. While KAW did pursue a pipeline to Louisville nearly a decade ago, many changes have occurred since that time, all of which support a regional solution that draws from Pool 3 of the Kentucky River. Mr. Nick Rowe and Ms. Bridwell explained those changes at the November Hearing.

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<sup>74</sup> TE November Hearing, Volume III, p. 224.

<sup>75</sup> LWC provided its current strategic plan as an attachment to LWC’s October 1, 2007 response to Item No. 99 of KAW’s data request to LWC. The first page of the strategic plan is numbered “LWC 3087.”

<sup>76</sup> TE November Hearing, Volume III, p. 147.

<sup>77</sup> TE November Hearing, Volume III, p. 181.

<sup>78</sup> 401 KAR 4:220, Section 5(5); 401 KAR 4:220, Section 6(7); and 401 KAR 4:220, Section 6(8). See also TE November Hearing, Volume III, pp. 220 – 222.



First, when KAW was considering solutions in the late 1990's, it considered only Pool 9 of the Kentucky River (where its existing facilities are) as a possible Kentucky River solution.<sup>79</sup> It never considered a solution at Pool 3 of the Kentucky River.<sup>80</sup> Then, when KAW began working on the problem as part of a regional solution with BWSC, it learned of the many advantages of a Pool 3 solution. That solution was recommended by O'Brien & Gere, and the part<sup>81</sup> of that solution that includes facilities at Pool 3 forms the basis of KAW's Facilities in this case.

Second, the KRA,<sup>82</sup> a fledgling agency a decade ago, now has the experience and respect to fulfill its primary mission -- the protection of the Kentucky River watershed. KRS 151.720 authorizes the KRA to provide for the maintenance and reconstruction of the Kentucky River basin locks and dams, issue bonds, contract with other state agencies or others to assist in its mission, develop long range water resource and drought response plans, develop comprehensive management plans for the river basin and its watershed, develop plans to protect and use ground water in the basin, and develop recreational opportunities there. The KRA has taken ownership of Dams 5 – 14 and has made significant progress towards the replacement of Dam 9. Further, as discussed above, the KRA has already implemented a plan to ensure the long-term reliability of Dam 3. It has heartily endorsed KRS II. It stands ready to work with KAW to solve the

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<sup>79</sup> TE November Hearing, Volume I, pp. 186 – 187.

<sup>80</sup> TE November Hearing, Volume I, pp. 183 – 187.

<sup>81</sup> While the O'Brien & Gere preferred solution pointed out that Pool 3 facilities offered a possible connection to the Ohio River, KAW's proposal in this application includes nothing with regard to any future connection to the Ohio River because, in fact, a connection to the Ohio River is simply not necessary. As demonstrated in detail above, Pool 3 will have an adequate source of supply under any reasonable planning horizon.

<sup>82</sup> The KRA is a statutorily created agency that acts pursuant to the authority granted to it by KRS 151.700, et. seq.

region's supply problem through use of Pool 3. A certificate of public convenience and necessity will only augment the KRA's ability to fulfill its mission, which includes as a top priority the refurbishing of Dam 3.

Third, when KAW considered a pipeline to Louisville in the late 1990's, it was acting alone. It had no regional partner. Now, its regional partner is the BWSC. While it is true that KAW's first and foremost obligation is to ensure an adequate supply of potable water for its customers, the presence of the BWSC as KAW's regional partner is a significant change from the late 1990's. By collaborating with the BWSC, KAW learned of the great advantages of a Pool 3 solution, which is also the BWSC's preferred solution. Moreover, both BWSC members and KAW customers will benefit from the economies of scale that will result if the BWSC exercises any of the options available to it under the November 20, 2007 contract between the BWSC and KAW. In short, a regional solution to the problem is desirable and, for the first time ever, has a real chance to work.

Fourth, one of the many reasons KAW abandoned the idea of a pipeline to Louisville in the late 1990's was that, in December 1999, the LFUCG Council passed a resolution urging a Kentucky River solution. KAW concluded it was inappropriate to implement a plan that included a pipeline to Louisville in the face of that resolution. Certainly, much has happened with respect to KAW's relationship with the LFUCG since that time, including a failed effort by the LFUCG to condemn KAW. Indeed, in a transparent effort to oppose any KAW effort, some of the same forces behind the failed condemnation attempt tried to rescind the December 1999 resolution despite the fact they had supported it in 1999. The attempted rescission failed.

Even though the attempted rescission of the December 1999 resolution failed, the LFUCG continued to engage in much discussion about this case. As a result of the

Commission's December 21, 2007 Order in this case, the LFUCG moved the Commission for an amendment to the procedural schedule to allow the LFUCG to receive more information from LWC about the LWC idea. The Commission granted LFUCG's motion and amended the procedural schedule so that the LFUCG would have time to gather information and submit testimony no later than February 11, 2008. Although the LFUCG heard another presentation from LWC on January 15, 2008, it submitted *nothing* by the February 11, 2008 deadline. Thus, the sum total of all LFUCG activity since the November Hearing as it relates to the LFUCG's position in this case is zero. By its charter, the LFUCG Council can act officially only through ordinance or resolution.<sup>83</sup> Therefore, in the end, the LFUCG's position *remains* as written in its December 1999 resolution: a Kentucky River solution is the LFUCG's *preferred* solution.

Fifth, the opposition from those affected by the pipeline considered in the late 1990's was substantial and was one of the many reasons KAW abandoned that effort. It is true that there is opposition from CAWS and others who will be affected in some regard by the pipeline KAW has proposed. However, with all due respect to CAWS and those others who will be affected by the Facilities, there is a glaring and important difference between the Louisville pipeline that was proposed in the late 1990's and the pipeline that has been proposed by KAW in this case. As explained in KAW's Response to November Hearing Data Request No. 3, 96-100% of the various alternative pipeline alignments that KAW considered in the 1990's were going to be placed on private property. In contrast, significant portions of the pipeline KAW has proposed in this case will be located in the state right-of-way.<sup>84</sup> Although it is impossible to measure the

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<sup>83</sup> LFUCG Charter, Section 4.07. Letters from LFUCG Council Members to the Public Service Commission about this case are not official acts of the Council.

<sup>84</sup> See the maps KAW provided in response to November Hearing Data Request No. 2.

level of opposition to any project, to the extent a pipeline can be placed in a state right-of-way, the impact on nearby landowners will be less than if it is placed on private property. KAW is firmly committed to making the installation and presence of its proposed pipeline as painless as possible for all those affected by it.

Sixth, the AG did *not* support KAW's Louisville pipeline proposal of the late 1990's. Here, acting as the statutory representative of *all* consumers in the Commonwealth, including LWC and KAW customers, the AG supports the Kentucky River solution at Pool 3 as KAW has proposed (with some conditions, most of which KAW has endorsed).

Finally, in addition to everything mentioned above, KAW was accused of acting alone or being a "lone ranger" when it pursued an agreement with LWC in the late 1990's. Additionally, KAW was accused of acting only in its own interest and not in the best interest of the public. The LFUCG strongly encouraged KAW to work with regional water utilities to come up with a solution – which is exactly what KAW has done. BWSC became the recognized entity leading the regional evaluation and KAW participated in that effort every step of the way. LWC made numerous presentations to BWSC knowing that, eventually, BWSC would select a preferred alternative. In the end, BWSC's preference became a Pool 3 solution and KAW has partnered with the BWSC in pursuit of that solution. Based on years of analysis and many developments, KAW and BWSC have concluded that a Pool 3 regional solution is the best solution for all concerned parties. Taking into account all of that effort, study and history, KAW stands before this Commission and represents that the proposed Pool 3 solution is the best solution for KAW's customers and the members of the BWSC.

**B. THE LWC IDEA IN THIS CASE, IN ALL OF ITS ITERATIONS, HAS BEEN CONSIDERED AND REJECTED BY KAW AND BWSC FOR NUMEROUS REASONS.**

The November Hearing testimony of LWC's President, Mr. Heitzman, in response to very pointed questions posed by Chairman Goss, establishes beyond any doubt that the KAW Pool 3 proposal is needed *and* is reasonable. That testimony<sup>85</sup> is as follows:

**Chairman Goss:** I've got a question or two I want to ask you, Mr. Heitzman. The standard that this Commission must employ in considering Kentucky-American's Application is, first of all, whether or not there is a need for the plan, the plant in its entirety, that Kentucky-American in proposing and whether or not the construction of that entire utility plant, the intakes, the booster stations, and the pipe, would provide a wasteful duplication of services, and that includes a review of whether or not, from an economic standpoint, the certificate that's the subject of the Application is efficient or is cost-effective. First of all, let me ask you if, in your opinion, there is a need for the provision of additional water to the Kentucky-American/Bluegrass Water Supply Commission area.

**Mr. Heitzman:** My opinion is I clearly believe that there is a need of water for Central Kentucky.

\* \* \* \* \*

**Chairman Goss:** All right. Let's turn, then, to the second prong of the test and that is wasteful duplication or an economic efficiency or cost-effectiveness, or however you want to characterize it. Tell me whether or not you believe, first of all, that the Kentucky-American Application is reasonable in its scope . . . .

\* \* \* \* \*

**Mr. Heitzman:** I believe the Kentucky-American Pool 3 Project is a reasonable alternative to consider to be able to solve the water supply needs in Central Kentucky.

\* \* \* \* \*

**Chairman Goss:** All right. Do you believe that the Kentucky-American – does Louisville Water Company believe that the Kentucky-American proposal is cost-effective or cost-efficient?

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<sup>85</sup> TE November Hearing, Volume III, pp. 322 – 325.

**Mr. Heitzman:** In order to render an opinion related to cost-effective, I need something to compare it to . . .

**Chairman Goss:** Okay.

**Mr. Heitzman:** . . . and so, to my knowledge, the short list of two alternatives that are being deliberated is a proposal from the Louisville Water Company and a proposal to build a plant on Pool 3, and it is my belief, from all the deliberations and the evaluations that we and others have performed, that the Louisville Water Company proposal is the least cost solution.

**Chairman Goss:** Okay. Now, I didn't say "least-cost solution."

**Mr. Heitzman:** Okay.

**Chairman Goss:** That's not what I asked you. I asked you if you believed that the Kentucky-American proposal, which is the only proposal that has been applied for in this docket, whether or not you believe that proposal is cost-effective or cost-efficient.

**Mr. Heitzman:** And I would respond by saying that the proposal need to be compared to another alternative for me to render an opinion of cost-effectiveness . . .

**Chairman Goss:** Okay.

**Mr. Heitzman:** . . . and, when I compare that alternative to the Louisville Pipeline alternative, my belief is that Louisville Pipeline is more cost effective.

**Chairman Goss:** All right, and tell me, if you can, tell me specifically why you believe that is the case.

**Mr. Heitzman:** From the analysis that has been performed by R.W. Beck.

In summary, Mr. Heitzman admitted that a need exists and that KAW's proposal is reasonable. Further, by testifying that the LWC idea is "more cost effective" than KAW's proposal, he by implication admitted that the KAW proposal is also cost-effective. Finally, as set forth below, Mr. Heitzman's reliance on the R.W. Beck Report for his belief that the LWC idea is "more cost effective" than the KAW proposal is misplaced. Given these candid and stark admissions from LWC, it is clear that KAW has met all criteria necessary for its requested certificate.

## **1. MR. HEITZMAN'S "ABOUT-FACE" AND INTERIM MEASURES**

Given a chance to recant these admissions at the March Hearing that arose from the LFUCG's January 11, 2008 motion, Mr. Heitzman did so. Realizing that his admissions prove that a certificate should be granted, Mr. Heitzman testified at the March Hearing that he "would change my position."<sup>86</sup> Apparently, he no longer thinks KAW's proposal is reasonable. He supports his "about-face" by citing "newly discovered" interim measures by which KAW can allegedly obtain water from Frankfort and Versailles. He further supports his "about-face" by claiming that he now knows of cheap public financing that is available for the LWC idea (that has now evolved to break down what used to be "Section 2" of the LWC pipeline to "Section 2A" and "Section 2B").

At the March Hearing, the support for Mr. Heitzman's "about-face" was destroyed. The alleged ability of Versailles and Frankfort to provide finished water to KAW is the basis for the "interim solutions" discussed in Mr. Heitzman's February 11, 2008 testimony. However, Mr. Heitzman was forced to make wholesale changes to that testimony to account for his ignorance of the problems with a "Georgetown interconnection." Although Mr. Heitzman testified that LWC employee Jim Smith had discussions with Billy Jenkins<sup>87</sup> about getting water to KAW from Frankfort via Georgetown, those discussions must not have been very thorough. After Mr. Heitzman provided sworn testimony that water could be provided to KAW from Frankfort via Georgetown, Mr. Jenkins wrote Mr. Heitzman and advised that the Georgetown system "is not capable of transferring . . . water . . . to KAWC." Mr. Jenkins went on to insist that Mr.

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<sup>86</sup> TE March Hearing, Volume I, p. 166.

<sup>87</sup> Mr. Jenkins is the General Manager of Georgetown Municipal Water & Sewer Service. See LWC March Hearing Exhibit No. 1 which included Mr. Heitzman's corrected testimony and a February 26, 2008 letter to Mr. Heitzman from Mr. Jenkins.

Heitzman correct his testimony before his Commission. Clearly, the ability of Frankfort to provide an “interim solution” via Georgetown is not feasible.

Even if the “Georgetown interconnection” could be used to move water from Frankfort to KAW, Frankfort does not have the water to do so. Frankfort has previously taken the position that it will not provide more than 1 MGD to Central Kentucky because of the need to serve its existing retail and wholesale customers.<sup>88</sup> Additionally, KAW demonstrated in verbal rebuttal testimony that it is erroneous to think water can be moved to KAW from Frankfort without a pipeline connecting the two systems.<sup>89</sup> KAW also demonstrated that Frankfort has “no reliable treatment plant capacity available for BWSC without substantial improvements to expand the water treatment plant and distribution system in the range of \$17 to \$32 million.”<sup>90</sup> Finally, Mr. Heitzman admitted that he has no commitment from Frankfort to expand its water treatment plant.<sup>91</sup>

Mr. Heitzman’s “interim solutions” also include the notion that Versailles can provide 5 MGD to KAW. In his February 11, 2008 testimony, Mr. Heitzman relies on an April 14, 2006 letter from GRW Engineers, Inc. to Bruce Southworth, Utilities Director for Versailles<sup>92</sup> as support for his “5 MGD from Versailles” concept. In fact, Mr. Heitzman testified that there is *no*

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<sup>88</sup> KAW March Hearing Exhibit No. 3, p. 3.

<sup>89</sup> TE March Hearing, Volume II, p. 9.

<sup>90</sup> See KAW March Hearing Exhibit No. 4, page 2 of 5 of the Program Manager Status Report that is attached to the BWSC January 22, 2007 minutes. Interestingly, Jim Smith of LWC was present at that BWSC meeting (see attendee list) and, thus, LWC was aware of Frankfort’s inability to provide an interim solution for more than a year *before* Mr. Heitzman’s February 11, 2008 testimony was submitted.

<sup>91</sup> TE March Hearing, Volume I, p. 69.

<sup>92</sup> The letter is attached to Mr. Heitzman’s February 11, 2008 testimony as Exhibit No. 2.



difference between his concept of 5 MGD from Versailles and the 5 MGD option addressed in the GRW letter.<sup>93</sup> Significantly, with respect to the 5 MGD option, the GRW letter states:

If an additional 5 mgd in demand were given to BWSC, the [Versailles] plant would be operating at capacity, leaving no room for expansion within Versailles or even daily maintenance at the Water Plant . . . . It would further appear that a 5 mgd purchase by BWSC would be impractical with the limiting factor being the capacity of the Versailles Water Treatment Plant.<sup>94</sup>

Clearly, Mr. Heitzman is simply wrong to suggest that Versailles can provide 5 MGD to KAW and even if Versailles could provide 5 MGD to KAW, Versailles' water withdrawal permit limits Versailles' ability to withdraw water from the Kentucky River when KAW/BWSC would need it most – when the flow in the Kentucky River decreases.<sup>95</sup> For example, when the water level is at or below the dam's crest, Versailles cannot withdraw more than 3.5 MGD.<sup>96</sup> In 2007, there were over 50 days when Versailles was limited to 3.5 million gallons.<sup>97</sup> As the flow in the Kentucky River decreases, the restrictions become more severe to the point that Versailles is only permitted to withdraw a total of 2.1 MGD.<sup>98</sup> When shown these restrictions and asked whether LWC has performed any investigation to support the notion that Versailles' source of supply is adequate to supply 5 MGD to KAW, Mr. Heitzman admitted it had not.<sup>99</sup> Finally, Mr. Heitzman admitted that there is no commitment from Versailles to provide any amount of water

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<sup>93</sup> TE March Hearing, Volume I, p. 53.

<sup>94</sup> See Exhibit No. 2 to Mr. Heitzman's February 11, 2008 testimony, p. 3.

<sup>95</sup> KAW March Hearing Exhibits Nos. 2 & 13.

<sup>96</sup> KAW March Hearing Exhibit No. 2, p. 3.

<sup>97</sup> TE March Hearing, Volume II, p. 8.

<sup>98</sup> KAW March Hearing Exhibit No. 2, p. 4.

<sup>99</sup> TE March Hearing, Volume I, p. 58.

to KAW<sup>100</sup> (including the 2 – 3 MGD that Mr. Heitzman admitted would require hundreds of thousands of dollars in additional expense).

Finally, the issue of crest gates at Dam 9 was discussed at the March Hearing. Although Mr. Heitzman relies on the addition of crest gates at Dam 9 to support his suggestion of getting more water to KAW while he attempts to get the LWC idea off the ground, Ms. Bridwell testified at length about the numerous and unique challenges of crest gates for Dam 9.<sup>101</sup> Moreover, even if all those challenges could be overcome in the timeframe Mr. Heitzman suggests (which they cannot), and even if KAW received every drop of additional water that crest gates would provide (which it will not), KAW would only be able to obtain an additional 5 MGD during the drought of record, which is only 25% of KAW's source of supply deficit.<sup>102</sup>

## **2. THE R.W. BECK REPORT**

The R.W. Beck Report ("Beck Report")<sup>103</sup> is full of miscalculations and improper assumptions,<sup>104</sup> but the Commission only needs to focus on the combination of the sensitivity

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<sup>100</sup> TE March Hearing, Volume I, p. 53.

<sup>101</sup> TE March Hearing, Volume II, pp. 32 – 38, 66 – 71.

<sup>102</sup> TE March Hearing, Volume II, pp. 82 – 83.

<sup>103</sup> The Beck Report appears in at least seven editions/versions. First, under cover letter of October 1, 2007, LWC filed the original Beck Report. Second, by letter of October 29, 2007, LWC revised the Beck Report to correct a mistake in calculating the municipal bond interest rate. Third, by letter of November 9, 2007, LWC filed sensitivity analyses as a supplement to the Beck Report. Fourth, by letter that was misdated November 9, 2007 (it should have been dated at least several days later), LWC filed a November 13, 2007 Beck letter that gave notice of another error in the Beck Report relating to ultra-violet treatment costs for the KAW proposal. Fifth, by letter of November 20, 2007, LWC filed a November 14, 2007 Beck letter which corrected the ultra-violet treatment costs problem and enclosed revised sensitivity analyses. Sixth, by letter of November 21, 2007, LWC filed yet another version of the Beck Report. Finally, LWC submitted the seventh version of the Beck Report on February 11, 2008 along with the supplemental pre-filed testimony of Dr. Wetzel.

<sup>104</sup> A detailed listing of all the Beck Report errors is set forth in KAW's December 10, 2007 Response to November Hearing Data Request No. 11. KAW incorporates in full into this brief

analyses contained in the Beck Report to understand that the LWC idea is more expensive than KAW's proposal. KAW's KRS II proposal is sized<sup>105</sup> so that it will "drought-proof" KAW's service territory in accordance with Kentucky regulations that require KAW to have a source of supply that is "sufficient to supply adequately dependably and safely the total reasonable requirements of its customers under maximum consumption."<sup>106</sup> To ensure that same level of supply under LWC's idea, KAW would be required to "reserve" or "take or pay" at least 10 MGD (to equate with a 20 MGD plant) or 12.5 MGD (to equate with a 25 MGD plant). Hence, the Commission must measure the cost of the LWC idea at a minimum flow of 10 – 12.5 MGD to fairly compare the LWC idea with KAW's proposed Facilities.<sup>107</sup> *But, until February 11, 2008, the Beck Report never even attempted to make that "apples to apples" comparison.* KAW demonstrated this serious flaw to the Commission at the November Hearing.<sup>108</sup>

Given the opportunity for LWC to file another round of testimony, it unsurprisingly attempted to correct that flaw by submitting yet another version of the Beck Report.<sup>109</sup> In that February 11, 2008 version, Dr. Wetzel included several "sensitivity analyses" in which assumptions used in Dr. Wetzel's "base case" scenario were adjusted. One of those sensitivity analyses tries to account for the flaw mentioned above by computing the present worth of the

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the discussion of the Beck Report errors set forth in that response.

<sup>105</sup> It is sized at 20 MGD if BWSC elects not to participate and 25 MGD if BWSC does participate.

<sup>106</sup> 807 KAR 5:066, Section 10(4).

<sup>107</sup> TE November Hearing, Volume III, p. 167 (KAW must "enter into a take-or-pay contract for half the capacity it wants to reserve.")

<sup>108</sup> TE November Hearing, Volume III, p. 337.

<sup>109</sup> Surprisingly, the February 11, 2008 Beck Report does not attribute any cost to the LWC idea for the "interim measures" suggested in Mr. Heitzman's testimony of the same date. (TE March Hearing, Volume I, pp. 233 – 234).

LWC idea at different levels of flow.<sup>110</sup> Dr. Wetzel also included sensitivity analyses for: various ownership scenarios for the LWC idea;<sup>111</sup> various cost of debt assumptions for the LWC idea;<sup>112</sup> and various wholesale rate increases for the LWC idea above the level of inflation.<sup>113</sup>

Although the February 11, 2008 Beck Report claims that a flow rate of 12 MGD through a Louisville pipeline has a present worth of \$55 - \$60 million less than a Pool 3 solution, that analysis is flawed. First, Dr. Wetzel testified that, in his “base case” scenario, the only changes he made since the November Hearing were the elimination<sup>114</sup> of ultra-violet treatment costs from the KAW proposal and an adjustment to his inflation assumptions for the LWC wholesale rate to exactly “mimic”<sup>115</sup> the LWC idea.<sup>116</sup> Therefore, all of the errors<sup>117</sup> that existed in the November 21, 2007 Beck Report continue to exist in the “base case” scenario in the February 11, 2008 Beck Report.

Second, Dr. Wetzel’s sensitivity analyses are misleading. He tries to show the effects of adjusting different variables, but he cleverly shows all those adjustments in a vacuum. For

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<sup>110</sup> See Table 3-2 of the February 11, 2008 Beck Report.

<sup>111</sup> See Table 3-1 of the February 11, 2008 Beck Report.

<sup>112</sup> See Table 3-3 of the February 11, 2008 Beck Report.

<sup>113</sup> See Table 3-4 of the February 11, 2008 Beck Report.

<sup>114</sup> TE March Hearing, Volume I, p. 227.

<sup>115</sup> TE March Hearing, Volume I, p. 227.

<sup>116</sup> Even after having the opportunity to correct the inflation factor in the Beck Report so that it “mimics” the LWC idea, Dr. Wetzel failed to get it right. He specifically testified at the March Hearing that he included inflation for the years 2009 – 2015 to derive the new wholesale rate that would become effective in 2016. (TE March Hearing, Volume I, p. 229). However, the LWC idea proposed by Mr. Heitzman specifically states that the 2016 wholesale water rate would be adjusted to account for inflation from “December 31, 2007 to December 31, 2015.” (Mr. Heitzman’s October 1, 2007 Rebuttal Testimony, p. 6). Thus, Dr. Wetzel uses a fewer number of years in computing the cumulative inflation adjustment than set forth in the LWC idea. The fact that LWC’s standard wholesale rate remained at \$1.71 for 2008 has no relevance because there is nothing in the LWC idea that guarantees the price in that idea will mimic LWC’s standard wholesale rate.

<sup>117</sup> See KAW’s December 10, 2007 Response to November Hearing Data Request No. 11.

example, he only adjusts ownership scenarios in relation to the “base case.” Likewise, he only adjusts wholesale water rate adjustments in relation to the “base case.” He never combines his sensitivity analyses to show the effects of adjusting more than one variable at a time. While that methodology does provide the ability to see the effects of a single change in relation to the “base case,” it *fails* to show the overall effect of the most appropriate mix of variables.

The most appropriate mix of variables must include, at a minimum: (1) a flow rate for the LWC idea of 12.5 MGD to provide the same drought protection the KAW proposal does; (2) a 100% privately owned Section II or some corresponding accounting for the fact that 26 USC 141 severely limits the availability of public tax-exempt financing because of the “private activity” status<sup>118</sup> of the LWC idea; (3) increases to the \$1.71 rate over and above inflation as allowed for in Mr. Heitzman’s October 1, 2007 proposal; and (4) some accounting for the wheeling costs that will be charged to KAW by whomever owns Sections 2A and 2B of the Louisville pipeline. While Dr. Wetzel addresses some of these factors in his sensitivity analyses, he fails to account for all of them or even for the overall effect of the ones he does address. In fact, Dr. Wetzel admitted that if one looks at the cumulative effect of his sensitivity analyses in the light most favorable to the KAW proposal, KAW’s proposal is less expensive than the LWC idea.<sup>119</sup> Fortunately, KAW expert witness Mr. Harold Walker has provided a valid present value

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<sup>118</sup> As described by KAW witness Mr. Michael Miller at the March Hearing, the notion that the LWC idea can be fully funded with tax-exempt funds is wrong. Since the LWC idea includes more than a 10% use by a private entity (KAW), any bonds used to finance the LWC idea must be “private activity bonds” pursuant to 26 USC 141(a)-(b). As Mr. Miller testified, there are annual state limits as to the amount of private activity bonds that can be used for a project. In Kentucky, that limit was approximately \$17.5 million for 2007. (TE March Hearing, Volume II, pp. 98 – 102). Thus, the Beck Report assumption concerning tax-exempt financing is fundamentally flawed.

<sup>119</sup> TE March Hearing, Volume I, p. 231.

analysis. In his March Hearing verbal rebuttal testimony, Mr. Walker testified that the present value of KAW's solution is \$234,775,260<sup>120</sup> and the present value of the LWC idea is \$288,003,650.<sup>121</sup> Thus, from a present value perspective, KAW's solution is over \$53 million cheaper than the LWC idea.<sup>122</sup>

Third, the numbers Dr. Wetzel provides in Table 3-2 (his flow rate sensitivity analysis) do not add up. According to that table, the 20-year present worth of the LWC idea is \$172,696,000 at 6 MGD and \$228,840,000 at 12 MGD for a difference of \$56,144,000. As Dr. Wetzel states, that change is driven by the "higher wholesale water costs" in the LWC idea.

Simple arithmetic proves Dr. Wetzel's numbers are wrong. The cost of purchasing an additional 6 MGD (from 6 MGD to 12 MGD) from LWC is \$74,898,000. That number is derived from multiplying \$1.71 (the LWC stated wholesale rate) times 6 MGD (12 MGD – 6 MGD) times 365 (days per year) times 20 years (the present worth period).<sup>123</sup> The February 11, 2008 Beck Report does not show the math Dr. Wetzel used, but, clearly, this nearly \$20 million mistake is, at the least, a cause for concern. Of course, the same mistake gets carried through to

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<sup>120</sup> See KAW March Hearing Exhibit No. 14, Schedule 4.

<sup>121</sup> See KAW March Hearing Exhibit No. 14, Schedule 5.

<sup>122</sup> Mr. Walker's present value analysis of the LWC idea includes a cost of \$390 per foot of pipe and all other infrastructure prices used in his November 13, 2007 Rebuttal Testimony. The \$390 per foot figure is reasonable for many reasons, including the reason that the LWC pipeline will have to cross the Kentucky River. However, even if one were to use KAW's *original* Pool 3 bid prices of approximately \$300 per foot and all other infrastructure bid prices (which is inappropriate because the cost per foot for the KAW proposal is actually \$319 based on the *increased* bids), the resulting decrease in present value of the LWC idea is only approximately \$13.7 million. Likewise, because of the delays in this case, the total amount of the bids offered for the KAW proposal has increased by over \$5 million prior to pricing negotiations by KAW. These potential price increases are not reflected in Mr. Walker's present value analysis of the KAW proposal. However, the inclusion of an additional \$5 million in that analysis would mean an increase of only approximately \$6.8 million in the present value of the KAW proposal.

<sup>123</sup> Neither inflation nor discounting to present value needs to be included in this arithmetic because they cancel each other out.

the 30-year and 40-year present worth values in Table 3-2 at an even greater level due to the increased cost of purchasing water from the LWC pipeline over time.

The large increase in the cost of the LWC idea to give it a drought-proof feature was discussed at the November Hearing. The AG's expert witness, Mr. Rubin, stated:

Q: Do you have any idea of what the effect of having to purchase 10 million gallons a day from the Louisville Water Company to be as opposed to the analysis you performed in your rebuttal testimony?

A: I can get close. After I saw Ms. Bridwell's Rebuttal Testimony, I looked at what would happen if 12.5 MGD had to be paid for from the outset, because that's assuming half of the 25 MGD for Kentucky-American plus the Bluegrass Water Supply Commission, and that would increase the cost of the pipeline option, the net present value, from about \$255 million, as I discuss in my Rebuttal, up to about \$277 million on a present value basis, and that's about \$4 million higher than the Pool 3 Option under base case conditions, and then obviously, as more water is needed, when you go out 15 years or so, then, you know, the two models – or the cost of the pipeline becomes even more.<sup>124</sup>

Clearly, Mr. Rubin agrees that when one accounts for the need to “drought-proof,” the high cost of wholesale water purchase under the LWC idea makes the LWC idea more expensive than KAW's/BWSC's Pool 3 proposal.

At the March Hearing, KAW presented verbal rebuttal testimony on the estimated rate impact of the KAW proposal and the LWC idea. KAW witness Michael Miller testified that, by the year 2016, the rate impact on the average residential customer for a 20 MGD solution is less under the KAW proposal than it would be under the LWC proposal.<sup>125</sup> Further, for a 25 MGD

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<sup>124</sup> TE November Hearing, Volume II, pp. 253 – 254.

<sup>125</sup> KAW March Hearing Exhibit No. 12.

solution, the savings to the average residential customer under the KAW solution are even greater.<sup>126</sup>

Finally, the Beck Report fails to include wheeling costs that KAW would have to pay if the LWC idea were to become a reality, and those wheeling costs would be substantial. Under the latest version of the LWC idea, some entity would own Section 2A from the Shelby County line to Frankfort. Regardless of who that owner is, it *will* charge KAW wheeling costs to move water through the line to KAW. As Chairman Goss explained to Mr. Heitzman at the March Hearing, those wheeling costs are going to “make a heck of a difference as to the ultimate cost.”<sup>127</sup> Chairman Goss recognized the significance of the wheeling costs when he asked Mr. Heitzman:

Well, except that isn’t the other side of the coin that there’s going to be wheelage to have to pay and, if so, is there any evidence that tells the Commission what that’s going to be so that we can try to compare the cost of that scenario that’s out there, blowing in the wind, versus what Kentucky-American has provided to us?<sup>128</sup>

In Mr. Walker’s March Hearing testimony and KAW March Hearing Exhibit No. 14 (Schedule 5), the wheeling costs associated with the LWC idea are shown to be substantial. In the year 2010 alone, the wheeling costs would be nearly \$4.3 million.<sup>129</sup> As further demonstrated in KAW March Hearing Exhibit No. 14, the annual wheeling costs increase over time.

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<sup>126</sup> Id.

<sup>127</sup> TE March Hearing, Volume I, p. 211.

<sup>128</sup> TE March Hearing, Volume I, p. 212.

<sup>129</sup> See KAW March Hearing Exhibit No. 14, Schedule 5, lines 56 – 58. For further discussion of wheeling costs, see KAW’s March 12, 2008 Response to Item No. 1 of the March Hearing Data Requests.



### 3. OTHER PROBLEMS WITH THE LWC IDEA

Of course, another undisputed and critical problem with the LWC idea is that, even according to LWC, its pipeline will not be able to provide the amount of water that the Pool 3 option can provide until 2012 – two years later than the KAW proposal will be in service. Further, Mr. Heitzman admitted that LWC’s 2012 schedule failed to include any time necessary to obtain the certificate of convenience and necessity that would be required for KAW to purchase water from LWC.<sup>130</sup> Moreover, it appears that LWC has never considered the tremendous amount of regulatory and legal complications that could and would arise from its idea.<sup>131</sup> For example, the issue of whether LWC is able to provide service beyond counties adjacent to Jefferson is a significant one<sup>132</sup> (and is addressed in more detail below). Additionally, under cross-examination by Mr. Wuetcher, Mr. Heitzman admitted that LWC has not considered the significant issue of whether some or all of the LWC idea would be subject to PSC regulation and approval.<sup>133</sup> Finally, the issue of LWC’s legal ability to own some or all of the pipeline it proposes is significant and would have an impact on the regulatory permits that would be required.<sup>134</sup> All of this means that if the LWC idea is implemented, it is subject to significant legal and regulatory delays and risks, none of which exist for the KAW proposal. Of course, if those delays occur, Central Kentucky would be susceptible to all the consequences of inadequate water for years longer than it need be.

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<sup>130</sup> TE November Hearing, Volume III, p. 185.

<sup>131</sup> TE November Hearing, Volume III, p. 293 and see, generally, TE Volume III at 278 – 308 (cross-examination of Mr. Heitzman by Mr. Wuetcher).

<sup>132</sup> At the November Hearing, Mr. Heitzman testified that LWC can provide service to counties beyond those adjacent to Jefferson, but that testimony flatly contradicts the provisions of KRS 96.265, which allows LWC service only in Jefferson and adjacent counties.

<sup>133</sup> TE November Hearing, Volume III, pp. 278 – 280.

<sup>134</sup> TE November Hearing, Volume III, pp. 283 – 284.

The LWC idea fails in another regard. LWC has steadfastly refused to guarantee to KAW/BWSC 25 MGD of plant capacity,<sup>135</sup> but only 25 MGD of “pipeline capacity.”<sup>136</sup> The impact of this twist on words cannot be overlooked. A guarantee of “pipeline capacity” is meaningless without a corresponding guarantee of plant capacity. Mr. Heitzman admitted on questioning from Chairman Goss that LWC does not have the plant capacity to supply its existing customers, provide 25 MGD to KAW/BWSC, and also maintain its 15% reserve capacity.<sup>137</sup> Furthermore, LWC has made numerous water sales pitches to communities throughout Central Kentucky.<sup>138</sup> To the extent those communities accept those proposals, LWC will have even less capacity to deliver to KAW/BWSC.

Mr. Heitzman admitted that LWC has not done a hydraulic analysis for its idea.<sup>139</sup> He also admitted that LWC has not modeled the Frankfort water system to determine whether LWC’s idea of using the Frankfort system to deliver water to Central Kentucky will actually work.<sup>140</sup> He admitted that LWC has done no water blending analysis to determine whether LWC water is compatible with Frankfort’s water,<sup>141</sup> which compatibility would have to exist. LWC has not performed an engineering study for its idea. LWC does not have the amount of water storage capacity that is required of regulated utilities by Kentucky regulations.<sup>142</sup> Mr. Heitzman

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<sup>135</sup> TE November Hearing, Volume III, p. 169.

<sup>136</sup> TE November Hearing, Volume III, p. 167.

<sup>137</sup> TE November Hearing, Volume III, p. 173.

<sup>138</sup> See, generally, LWC’s response to the Commission’s open records request in this case and TE November Hearing, Volume III, pp. 170 – 171.

<sup>139</sup> TE November Hearing, Volume III, p. 155.

<sup>140</sup> Id.

<sup>141</sup> TE November Hearing, Volume III, p. 161.

<sup>142</sup> TE November Hearing, Volume III, p. 153.

admitted that LWC has not performed a routing study for its pipeline idea.<sup>143</sup> LWC has not conducted an environmental study for its idea,<sup>144</sup> it has not studied the wetlands that will be impacted by its idea,<sup>145</sup> it has not studied the impact of its idea on Waters of the U.S.,<sup>146</sup> and it has not studied the effects its idea would have on threatened or endangered species.<sup>147</sup> LWC claims that it has begun investigating “environmental/cultural impact” issues, but the support for that claim amounts to an exchange of letters<sup>148</sup> with state officials that are generously described as extremely preliminary in nature.

LWC’s efforts since the November Hearing to cure these deficiencies have resulted in little progress. The only progress that has been made is that LWC has cobbled together a “working group”<sup>149</sup> of entities to pay an engineering firm to perform a *feasibility* study of the LWC idea.<sup>150</sup> Even though Mr. Heitzman called this group a “partnership” in his February 11, 2008 testimony, he admitted on cross examination that there is no legal partnership agreement with those entities<sup>151</sup> and that there are no written agreements whatsoever between any of those entities in furtherance of the LWC idea.<sup>152</sup>

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<sup>143</sup> TE November Hearing, Volume III, pp. 326 – 327.

<sup>144</sup> LWC’s October 1, 2007 Response to Item No. 67 of KAW’s First Data Request.

<sup>145</sup> LWC’s October 1, 2007 Response to Item No. 107 of KAW’s First Data Request.

<sup>146</sup> LWC’s October 1, 2007 Response to Item No. 108 of KAW’s First Data Request.

<sup>147</sup> LWC’s October 1, 2007 Response to Item No. 109 of KAW’s First Data Request.

<sup>148</sup> See Exhibits 9 & 10 to Mr. Heitzman’s February 11, 2008 testimony.

<sup>149</sup> This “working group” is called the Shelby-Franklin Water Management Group and consists of LWC, the Frankfort Plant Board, North Shelby Water Company, West Shelby Water District, Shelbyville Water and Sewer and the U.S. 60 Water District. (Heitzman February 11, 2008 testimony, pp. 6 – 7).

<sup>150</sup> See Exhibit No. 7 to Mr. Heitzman’s February 11, 2008 testimony.

<sup>151</sup> TE March Hearing, Volume I, pp. 125 – 126.

<sup>152</sup> TE March Hearing, Volume I, pp. 126 – 127.

None of these deficiencies<sup>153</sup> is surprising given the extremely preliminary nature of the LWC idea. Indeed, the version of the LWC idea set forth in LWC's February 11, 2008 testimony first surfaced while Mr. Heitzman was on the witness stand at the November Hearing. At the very end of the last day of the November Hearing, Mr. Heitzman offered yet another "alternative" to the LWC "base proposal" that includes a section of pipe being owned by Frankfort.<sup>154</sup> That "alternative" morphed into the LWC idea set forth in the "new" testimony LWC submitted on February 11, 2008. Tellingly, there are so many routing and ownership unknowns about the LWC idea that Mr. Heitzman could not even count them as they were discussed during the cross-examination of him.<sup>155</sup> All of this is in stark contrast to KAW's proposal that has been studied, designed, bid and will be ready to be constructed soon after a certificate is granted.

The LWC idea is also full of ill-considered notions that will never come to fruition. For example, Mr. Heitzman's representation that the LWC pipeline can be installed in the I-64 right-of-way is proven false by LWC's own documents. In response to Mr. Heitzman's inquiry about using the I-64 right-of-way to Roger Recktenwald of the Kentucky Association of Counties, Mr. Recktenwald correctly stated that the Kentucky Transportation Cabinet would only allow use of the I-64 right-of-way "in the most dire circumstance and only for extremely short distances

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<sup>153</sup> Although not a "deficiency" with LWC's proposal, KAW has grave concerns about the LWC practice of reducing expenses and deferring capital projects (which necessarily increases the risk of water quality and quantity problems) so that it can meet a *budgeted* dividend requirement. (See TE November Hearing, Volume III, pp. 215 – 218). Of course, KAW, like most companies, pays its dividends based on the level of its earned income, regardless of the amount of dividend that was estimated in the budgeting process.

<sup>154</sup> TE November Hearing, Volume III, pp. 318 – 320.

<sup>155</sup> TE November Hearing, Volume III, p. 317.

would they ever consider the possibility of a parallel line on their right-of-way.”<sup>156</sup> Mr. Recktenwald’s opinion is fully supported by KAW November Hearing Exhibit Nos. 4 & 5 that set forth the Kentucky Transportation Cabinet’s policies on utilities’ use of state right-of-way. Moreover, even if LWC is permitted to use short stretches of the I-64 right-of-way as it now claims it can, the very document upon which LWC relies for that claim proves that it takes *two years* to obtain permission to do so.<sup>157</sup> Of course, there is nothing in the LWC idea timeline that accounts for that long process.

While some might think that the idea of using the I-64 right-of-way is a magical solution, the fact is that use of that right-of-way is not going to happen. In fact, when KAW considered a Louisville pipeline in the late 1990’s, one of the routes it considered was the very same route LWC now proposes.<sup>158</sup> Of course, the vehement opposition to that route is well-documented and there is no reason to believe that same opposition would not result if the LWC idea progresses.

Likewise, the issue of how to offset revenue the KRA would lose if the Pool 3 option is not implemented has led to much confusion. LWC has suggested that it make some donation or contribution to the KRA, but when asked to make a firm commitment in that regard, Mr. Heitzman *refused*.<sup>159</sup> Notions like using the I-64 right-of-way, hanging the Louisville pipeline from a bridge to cross the Kentucky River and making a contribution to the KRA may seem appealing on first blush. But the November Hearing testimony showed that those ideas were never fully studied and, in fact, are never going to materialize.

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<sup>156</sup> TE November Hearing, Volume III, p. 196.

<sup>157</sup> See Exhibit No. 13 to Mr. Heitzman’s February 11, 2008 testimony.

<sup>158</sup> Bridwell November 13, 2007 Rebuttal Testimony, pp. 5 – 7.

<sup>159</sup> TE November Hearing, Volume III, p. 213.

#### 4. KAW'S CONSIDERATION OF THE LWC IDEA

LWC has made much ado about the fact that KAW has not, in recent years, approached LWC and asked for a water sale proposal. However, the AG's witness, Mr. Rubin said it best when he described why such an approach was not necessary. He said that it was reasonable for KAW to file its Application in this case without requesting a proposal from LWC because: (1) LWC has made a series of proposals to the BWSC or its predecessor of which KAW had knowledge so KAW was in a position to know LWC's pricing; (2) a great deal of opposition to a Louisville pipeline solution has existed over the last ten years that required KAW to consider a more regional approach; and (3) LWC has always had a published wholesale rate that anybody could use to get an estimate of what LWC would charge.<sup>160</sup> In fact, Mr. Rubin confirmed that KAW has "fully explored all reasonable options of water supply for Central Kentucky."<sup>161</sup>

Ms. Bridwell testified that KAW has considered various LWC proposals at least four times over the years (in the late 1980s, in the late 1990s, as part of the BWSC's consideration of five different LWC proposals, and, for the fourth time, by Gannett Fleming, KAW's outside consultant).<sup>162</sup> All of that occurred prior to the commencement of this case. After LWC intervened and raised its idea in this case, KAW evaluated it again in depth, even as it evolved from month to month. The latest version of LWC's idea is as expressed in Mr. Heitzman's February 11, 2008 pre-filed testimony (as corrected by Mr. Heitzman at the March Hearing). As it has at every step, KAW examined that idea from all angles: economic, rate impact, timing,

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<sup>160</sup> TE November Hearing, Volume II, p. 180.

<sup>161</sup> TE November Hearing, Volume II, pp. 203 – 204.

<sup>162</sup> TE March Hearing, Volume II, pp. 14, 77 - 78.

engineering feasibility, etc. Then, KAW provided sworn rebuttal testimony at the March Hearing that proved LWC's idea to be inferior to KAW's proposal.

KAW logically and rightfully assumes that LWC's idea as expressed in *sworn* testimony is as attractive as LWC can make it. LWC has spent months and vast resources describing its idea to this Commission, any community that will listen, legislators and the press. In fact, on January 15, 2008, LFUCG Council Member Don Blevins specifically asked Mr. Heitzman to "sharpen his pencil" in an effort to make LWC's idea more economically attractive. However, after having had time to "sharpen his pencil," the LWC idea expressed in Mr. Heitzman's February 11, 2008 testimony is the same as he described to the LFUCG Council on January 15, 2008 (and that was before his "Georgetown interconnection" correction). Clearly, LWC's idea is as attractive as LWC can make it.

On the issue of a recent meeting between LWC and KAW, KAW reported the details of a recent discussion between the presidents of KAW and LWC in its March 13, 2008 Response to LWC's Motion for an Informal Conference. On March 6, 2008, during the March Hearing, Mr. Rowe and Mr. Heitzman had a discussion in the lobby of the Public Service Commission. In that discussion, Mr. Heitzman expressed LWC's interest in KAW's possible ownership of part of the Louisville pipeline. That suggestion is nothing new – LWC has always mentioned KAW as a possible owner of a portion of the pipeline LWC has proposed. In that discussion between the two presidents, Mr. Heitzman gave no indication that LWC can make the LWC idea any more attractive. He merely expressed a need that has always existed: LWC needs an owner – any

owner – for the portion of the Louisville pipeline that LWC is prohibited by statute<sup>163</sup> from owning.

Mr. Rowe understood Mr. Heitzman's comments to mean that KAW should abandon its proposal in this case and join in the LWC idea. Again, that is nothing new. Thus, that discussion revealed no ability for LWC to revise or refine its idea to make it a better solution than KAW's solution. Accordingly, Mr. Rowe correctly responded that KAW believes that its proposed solution is the right solution for KAW customers for all of the numerous reasons that have been demonstrated in this case, including the reason that it is the most timely solution and, therefore, minimizes KAW's customers' risks.

LWC's presence in this case has forced KAW to prove its case to a standard well beyond that set forth in KRS 278.020(1). This Commission has left no stone unturned. LWC and CAWS have been given every conceivable opportunity to prove that KAW's proposal does not meet the required standard. In the end, after voluminous discovery and five full days of evidentiary hearing, KAW's proposal has withstood the onslaught of LWC's and CAWS' efforts -- legal, political and otherwise.

**C. THE COMMISSION SHOULD NOT BE DISTRACTED BY ENVIRONMENTAL ISSUES.**

At the beginning of the public comment hearings in this case, Chairman Goss indicated that the Commission has "no authority whatsoever over environmental matters."<sup>164</sup> That statement is accurate and perfectly consistent with the Commission's well-defined jurisdiction under state law that does not, in any way, authorize the Commission to address environmental,

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<sup>163</sup> KRS 96.625 sets forth a geographical limitation to LWC facilities. LWC cannot extend its facilities beyond "counties adjoining its county of origin."

<sup>164</sup> September 13, 2007 public comment hearing, 5:21 p.m.



historical or cultural issues in ruling upon whether a proposed project will serve the public convenience and necessity.<sup>165</sup> Of course, KAW intends to comply with any and all state and federal laws that govern its project. In fact, KAW submitted the rebuttal testimony of Mr. Cy Whitson (and Mr. Whitson's environmental survey report that concluded no threatened or endangered species were found during the survey<sup>166</sup>), which, along with KAW's cultural resources assessment,<sup>167</sup> demonstrate KAW's deep commitment to minimize to the fullest extent possible any effects the Facilities might have on the environment or cultural resources. Nevertheless, at the November Hearing, CAWS engaged in questions relating to the environment and has submitted testimony on environmental issues. The Commission has not considered environmental issues in the past and should not do so now.

"The Public Service Commission's powers are purely statutory; like other administrative boards and agencies, it has only such powers as are conferred expressly or by necessary or fair implication."<sup>168</sup> "The manifest purpose of a public service commission is to require fair and uniform rates, prevent unjust discrimination and unnecessary duplication of plants, facilities and service and to prevent ruinous competition."<sup>169</sup> Its powers are thus "clearly and unmistakably limited to the regulation of rates and service of utilities."<sup>170</sup> The only statutes that the Commission is empowered to enforce are those found within the provisions of KRS Chapter

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<sup>165</sup> Kentucky Utilities Co., 252 S.W.2d at 890.

<sup>166</sup> See p. 8 of the Threatened and Endangered Species Survey Report attached to Mr. Whitson's November 13, 2007 Rebuttal Testimony.

<sup>167</sup> See KAW's Response to November Hearing Data Request No. 9.

<sup>168</sup> Croke v. Public Service Commission of Kentucky, 573 S.W.2d 927, 929 (Ky. App. 1978).

<sup>169</sup> City of Olive Hill v. Public Service Commission, 203 S.W.2d 68, 71 (Ky. 1947).

<sup>170</sup> Public Service Commission v. Blue Grass Natural Gas Co., 197 S.W.2d 765, 768 (Ky. 1946).

278.<sup>171</sup> KRS Chapter 278 contains no delegation of power authorizing the Commission to address environmental issues, and the “public convenience and necessity” requirement in KRS 278.020 has not been construed to include consideration of environmental issues.

It is well recognized in other jurisdictions as well that the expressed authority to regulate utility rates and services does not authorize a commission to consider environmental issues:

The jurisdiction of the P.U.C. is derived from the powers conferred by §16-243 of the General Statutes. That section confers on the P.U.C. exclusive jurisdiction over ‘technical matters such as the quality and finish of the materials, wires poles, conductors, fixtures and the method of their use.’ (citation omitted). This section does not expressly or by implication require the commission to consider the environmental, recreational or aesthetic impact of its findings and order.<sup>172</sup>

See also Country Place Waste Treatment Co. v. Pennsylvania Public Utility Commission<sup>173</sup> (Commission had no jurisdiction to address complaint that sewage treatment plant was emitting offensive odors); Massachusetts Electric Co. v. Department of Public Utilities<sup>174</sup> (“The department does not have responsibility for the protection of the environment.”); Borough of Moosic v. Pennsylvania Public Utility Commission<sup>175</sup> (Commission is not empowered to consider the environmental impact which might result from permitting a public utility to transfer property to a grantee outside the commission’s administrative control); and Arippa v. Pennsylvania Public Utility Commission<sup>176</sup> (“Because any issues regarding emission regulations were for the federal EPA or Pennsylvania’s Department of Environmental

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<sup>171</sup> See KRS 278.040(1) (“The Public Service Commission shall regulate utilities and enforce the provisions of this chapter”).

<sup>172</sup> City of New Haven v. Public Utilities Commission, 345 A.2d 563, 579 (Conn. 1974).

<sup>173</sup> 654 A.2d 72, 75 (Pa. 1995).

<sup>174</sup> 643 N.E.2d 1029, 1033 (Mass. 1994).

<sup>175</sup> 429 A.2d 1237, 1240 (Pa. 1981).

<sup>176</sup> 792 A.2d 636, 657 (Pa. 2002).

Protection to determine, the Commission did not err in granting the merger without considering the environmental factors presented by Clean Air and Citizens.”). “As a statutory agency of limited authority, the PSC cannot add to its enumerated powers.”<sup>177</sup> Therefore, this is not the forum to address environmental or cultural resources issues, and the Commission should refrain from consideration of those issues.

**D. APPENDIX E TO THE COMMISSION’S DECEMBER 21, 2007 ORDER**

The Commission’s December 21, 2007 Order directed the parties to answer four questions in their post-hearing briefs. Those questions and answers are set forth below.

**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?**

No. Without question, LWC can make wholesale water sales in Jefferson County and counties adjoining Jefferson County in accordance with KRS 96.265. However, LWC is a corporation whose stock is owned by a municipality and, therefore, it has only the authority granted to it by the General Assembly.<sup>178</sup> Since Louisville is a consolidated local government, KRS 96.230 requires LWC to be controlled and managed pursuant to the authority set forth in KRS 96.240 to 96.310. KRS 96.265<sup>179</sup> specifically addresses the territorial limitations of LWC’s authority to extend its facilities:

The board of waterworks may extend the waterwork corporation’s facilities to provide water service to persons within and outside of

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<sup>177</sup> Boone County Water and Sewer Dist. v. Public Service Commission, 949 S.W.2d 588, 591 (Ky. 1997).

<sup>178</sup> Grayson v. Rural Electric Corp. v. City of Vanceburg, 4 S.W.3d 526, 528 (Ky. 1999); see also City of Nicholasville v. Blue Grass Rural Electric Coop., 514 S.W.2d 414, 416 (Ky. 1974).

<sup>179</sup> LWC relied on KRS 96.265 when it responded to a data request concerning the geographic boundaries of LWC’s service territory. See LWC’s October 1, 2007 response to Item No. 55 of KAW’s First Data Request to LWC.

the city of the first class, including extensions into counties adjoining its county of origin.

KRS 96.265 limits LWC's operations to Jefferson County and counties adjoining Jefferson County. Realizing that limitation, LWC has always proposed that it will own the pipeline to the edge of Shelby County and that the metering point for water would be at the same place. Mr. Heitzman provided additional support for LWC's realization of the law on this point when he testified that he envisions LWC selling water to a possible Section 2A owner (at Ky. Highway 53) who, in turn, would sell it to a possible Section 2B owner, who, in turn would sell the water to KAW. Of course, as Chairman Goss noted, those middlemen are going to impose wheeling costs on KAW that will drastically increase the \$1.71 rate set forth in the LWC idea.

**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?**

No. As described above, LWC's territorial limits are set forth in KRS 96.265. That statute geographically limits LWC facilities to Jefferson County and counties adjoining Jefferson County. No other statute expands LWC's authority beyond this unequivocal limitation. In no event can LWC's facilities extend beyond this territorial limitation of Jefferson and adjoining counties. Here again, this is precisely why the LWC has always sought Section 2A and Section 2B owners other than LWC.

**3. Does the LFUCG have the statutory authority to construct, own and operate a joint public-private venture to supply water to Kentucky-American and any other regional water suppliers?**

No. The LFUCG does not currently own any waterworks.<sup>180</sup> Therefore, any such foray into supplying water would be undertaken pursuant to the LFUCG's municipal powers as opposed to any proprietary powers. The LFUCG is limited to only legitimate municipal purposes, which must serve the public welfare of the LFUCG's inhabitants and therefore do not include providing water to private consumers outside the territorial limits of the LFUCG.<sup>181</sup> Even making a profit that could ultimately benefit Lexington-Fayette County inhabitants through extra-territorial sales of water is not a proper public purpose.<sup>182</sup> Because there is no proper public purpose, KRS Chapter 58, which authorizes certain public projects, does not authorize the LFUCG to construct, own and operate a joint public-private venture as contemplated by this question.<sup>183</sup>

Additionally, although KRS Chapter 106 authorizes the establishment of waterworks by cities in certain situations, that power is limited to "the purpose of supplying the water district [if it is a district-established waterworks] or *the city and its inhabitants thereof with water.*"<sup>184</sup> Under Chapter 106, the LFUCG's authority to establish a waterworks is limited to the purpose of supplying Lexington-Fayette County inhabitants with water – it does not extend to establishing a waterworks to supply KAW and other regional water suppliers as contemplated by this question.

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<sup>180</sup> Because the LFUCG does not own any waterworks, the powers granted to cities under KRS 96.130 to 96.150 and KRS 107.700 to 107.770 are not available to the LFUCG.

<sup>181</sup> City of Corbin v. Kentucky Utilities Co., 447 S.W.2d 356, 358 (Ky. 1969).

<sup>182</sup> *Id.*

<sup>183</sup> *Id.*

<sup>184</sup> KRS 106.010 (emphasis added).

Finally, the LFUCG was created by the adoption of the LFUCG Charter, which limits LFUCG's powers to the geographical boundaries of Fayette County. The operative section, entitled "Territorial Limits of the Merged Government," states:

The [LFUCG] shall have power and jurisdiction throughout the total area embraced by the official boundaries of the County of Fayette as the same may be fixed upon the date of this Charter is put into effect.<sup>185</sup>

Therefore, the LFUCG is self-limited to only the territory within Fayette County and cannot supply water regionally as contemplated by this question.<sup>186</sup>

**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 rate-making purposes to the estimated cost of the proposed facilities at the time a CPCN is issued?**

No. The AG's witness, Mr. Rubin, has suggested that the Commission impose a maximum cost or "cap" as a condition of a certificate. The Commission, though, lacks the power to do so. The Commission is a statutorily created body whose authority and power is defined by the General Assembly.<sup>187</sup> The Commission's statutory powers are to be strictly construed.<sup>188</sup> This proceeding is governed by KRS 278.020(1), which does *not* confer any authority to the Commission to impose conditions upon the approval of a certificate. "When a statute prescribes the procedures that an administrative agency must follow, the agency may not

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<sup>185</sup> LFUCG Charter, Section 1.02.

<sup>186</sup> See McQuillin, The Law of Municipal Corporations, § 15.19 (3rd ed. 2003) (stating "the charter bears the same general relation to the ordinances of the city that the constitution of the state bears to statutes."); City of Louisville v. Parsons, 150 S.W. 498, 502 (Ky. 1912) (stating "all the charter limitations and directions are at all times in full force and effect, and are, in all states of case, applicable; and whatever the city does must be measured and controlled by the powers granted in the charter.").

<sup>187</sup> Boone County Water, 949 S.W.2d at 591 (PSC cannot add to its enumerated powers).

<sup>188</sup> South Cent. Bell Tel. Co. v. Utility Regulatory Comm'n., 637 S.W.2d 649, 653 (Ky. 1982).

add or subtract from those requirements.”<sup>189</sup> For instance, the Commission cannot add to its ratemaking powers under KRS 278.270 by penalizing a utility for poor service when such penalties are specifically provided by other statutory means.<sup>190</sup>

Perhaps Mr. Rubin is thinking of KRS 278.020(6) which does confer upon the Commission the ability to impose conditions upon approval of a “change in control” of a regulated utility. However, KRS 278.020(1), the statute that controls this proceeding, has no such language. “It is a primary rule of statutory construction that the enumeration of particular things excludes ideas of something else not mentioned.”<sup>191</sup> In other words, when the General Assembly allowed for conditions in KRS 278.020(6), its silence as to conditions in KRS 278.020(1) means that conditions are not permissible. If the General Assembly intended for the Commission to be able to place conditions upon a certificate, it would have expressly provided that power in KRS 278.020(1) as it did in KRS 278.020(6).

To the extent the cost of the Facilities is excessive, wasteful, or does not result in plant that is “used and useful,” KAW would not be allowed to include those costs in its rate base, and, thus, would not be permitted to recover that expenditure. Therefore, not only is there no authority for the imposition of a cap, there is no need for it because of the Commission’s power to regulate KAW’s rates. To take Mr. Rubin’s proposal to its logical conclusion, if the Commission can limit rate recovery as a condition in a certificate case (and it cannot), then it follows that the utility should be guaranteed the recovery of that exact amount with no questions asked and regardless of whether the full amount was actually necessary. Otherwise, any

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<sup>189</sup> Public Service Comm’n v. Attorney General, 860 S.W.2d 296, 298 (Ky. App. 1993)

<sup>190</sup> South Central Bell Tel. Co. v. Utility Regulatory Comm’n, 637 S.W. 2d 649, 653 (Ky. 1982).

<sup>191</sup> Lewis v. Jackson Energy Cooperative Corp., 189 S.W.3d 87, 91 (Ky. 2005).

limitation is arbitrary, unfair and violates due process. Under the statute, though, neither limiting rate recovery nor guaranteeing rate recovery is appropriate because the statutory scheme reserves those decisions for a rate case. Therefore, a cap cannot be imposed as a condition in a certificate case.

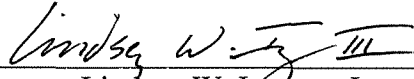
## **V. CONCLUSION**

KAW has met all the requirements set forth in KRS 278.020(1) to obtain a certificate of convenience and necessity for the construction of the Facilities. It has demonstrated a need for the Facilities. It has also demonstrated that the Facilities are both reasonable in size and cost. In fact, KAW has demonstrated that the Facilities will be less costly than those included in LWC's idea. It has demonstrated that the Facilities can provide for the growth and drought protection to which its customers are entitled. Finally, KAW's plan allows for a regional solution so that KAW and its regional partner, BWSC, can meet the water needs of the entire Central Kentucky region. For all of these reasons, the Commission should grant a certificate that will allow construction of the Facilities for 20 MGD and that further allows construction of the Facilities at 25 MGD in the event BWSC elects one of the options set forth in the November 20, 2007 contract between KAW and BWSC.



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CERTIFICATE OF SERVICE

This is to certify that the original and eight (8) copies of the foregoing have been filed with the Public Service Commission this the 20<sup>th</sup> day of March, 2008, and a copy mailed to:

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