

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

JUN 02 2010

PUBLIC SERVICE
COMMISSION

In the Matter of:

The Proposed Adjustment of)
Wholesale Service Rates of the) Case No. 2009-
Hopkinsville Water Environment Authority) 00373

OBJECTION TO RATE CASE EXPENSES

Christian County Water District (CCWD) by counsel, objects to the proposed rate case expenses to be included in the revenue requirement calculation in this case or as a surcharge to the CCWD. The expenses associated with the study prepared by Brent Tippey, P.E. are unrelated to the rate proposed by the Hopkinsville Water Environmental Authority (HWEA). The rate proposed to be charged Christian County Water District (District) was set forth in a letter dated July 9, 2009 (copy attached). That letter stated the amount of the proposed rate increase and the reasons for it.

In a memo dated June 29, 2009 from the HWEA's general manager to the city's Mayor (copy attached) the reasons for the proposed rate increase are discussed. The "Summary" paragraph lists the increased costs that necessitated the proposed 37% rate increase to the District. In his pre-filed testimony, Mr. Hale, manager of HWEA was asked:

9.Q What is the basis for the proposed rate increase?

A. During the spring and early summer of 2009, HWEA staff determined that a significant increase in both retail and wholesale water rates would be needed to offset increased operating expenses, including debt service. Ultimately, the Hopkinsville City Council enacted Ordinance 15-2009 on August 20, 2009. This Ordinance increased retail water rates and eliminated the declining block rate tiers for retail customers. As an overall result, the Hopkinsville Division retail water customers experienced an effective 37% increase. The wholesale water rates to the CCWD were also increased by 37%. The effective date of the retail rate increase was September 1, 2009.

In Response 21 to the District's data request filed on April 19, 2010 by the HWEA, the HWEA states that the rates proposed are those approved by the Hopkinsville city council on August 20, 2009 and filed with the Commission on September 23, 2009, which reflects a 37% increase in the wholesale rate to the District.

Thus, the rate proposed by the HWEA and submitted to the PSC for approval is based on the information and reasons provided to the District prior to the August 20, 2009 city council action. The only rate the city can impose is the one adopted by the city council. In contrast to that rate, the rate reflected in the cost study submitted by the HWEA on March 15, 2010 states that it recommends a 90% rate increase to the District. See Tippey testimony p. 8 filed on March 29, 2010. No action by the council was taken to approve that rate. Therefore, the study is of no lawful effect.

The purpose of the Tippey report is to analyze and allocate known and measurable expenses incurred by HWEA in order to ascertain the appropriateness of the proposed rate increase. HDR Engineering Report, (p1-2). The result of that analysis is to undermine the basis of the HWEA's analysis of the needed rate increase. If the Tippey study is correct, the initial rate proposed by HWEA is so flawed as to be of no

ratemaking value. However, the HWEA has rejected the recommendation of the Tippey study and reaffirmed the intention to raise the District's rate by 37%..

Because the HWEA has decided to disregard the Tippey report , the expenses associated with it should not be bourn by the District. The Tippey report is not the basis on which the HWEA is setting rates. The information presented to the District and the city council in 2009 is the only substantiation directly related to this rate increase. The HWEA made its decision to reject the Tippey report. It should pay the cost of that report.

The expenses also include significant legal fees associated with the HWEA's decision to challenge the legality of the contract terms related to the calculation of the wholesale rate. Those fees are not related to the development or justification of the 37% wholesale rate increase. The District should not be required to subsidize the legal advice sought by the HWEA on matters distinct from the rate proposal before the Commission. This issue was raised by the HWEA, not the District. It was the HWEA's misunderstanding of the contract terms that generated those legal fees. It should be the HWEA that incurs the costs of its investigation into legal issues about its interpretation of the contract.

Finally, the amount of the rate case expense sought to be recovered by the HWEA is excessive for a case of this limited scope. The conferences and associated legal fees related to the contract issue have nothing to do with the rate proposed to be charged to the District. The Tippey report is an after the fact attempt to justify a rate increase that has been discounted by the HWEA, which has chosen to rely on the

originally filed 37% increase. None of these fees was generated as a result of the actions of the PSC or of the District. They are tangential matters.

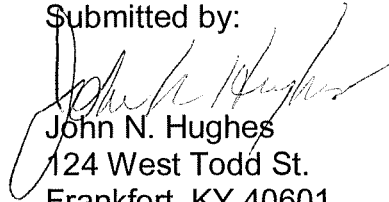
Not only are the fees unrelated to the rate increase the city is attempting to justify, they are excessive for a case of this nature. For example, in Case No. 2008-00250, the Frankfort Plant Board file a notice of rate adjustment for its wholesale water customers, just as the HWEA did in this case. However, in the FPB case there were three intervenors, two informal conferences, a cost of service study prepared by Gannett Fleming (as well as travel expenses), multiple sets of data requests from the staff and the intervenors, a formal hearing, and a post hearing brief. The total rate case expenses for that case was approximately \$68,000.00. In the HWEA there was no hearing, no brief, no out of state witness travel expenses, and only one set of data requests.

In Case No. 2008-00563, Water Service Corporation of Kentucky filed a formal rate application conforming to the requirements of 807 KAR 5:001 Section 10 including written testimony of five witnesses, one of whom was an expert witness for cost of capital issues. There were two public meetings for customer comments, three sets of data requests, including one set from the Attorney General of 105 questions, with sub-parts. There was a formal hearing with the company's five out of state witnesses incurring overnight travel expenses. A post hearing brief was also submitted. The total expense for this case was \$145,604.

The District believes it should only be response for reasonable fees directly associated with the issues involved in this case. The fees submitted by the HWEA are

for the most part unrelated to the wholesale rate proposed by the HWEA and should not be subsidized by the District's customers.

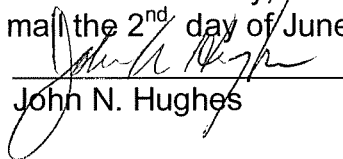
Submitted by:



John N. Hughes
124 West Todd St.
Frankfort, KY 40601
Attorney for CCWD

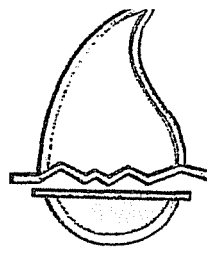
Certificate:

I certify that a copy of this response was served on Damon Talley, 112 N. Lincoln Blvd. Box 150 Hodgenville, KY 42748 by first class mail the 2nd day of June, 2010.



John N. Hughes

Leslie Hale
General Manager



HWEA

July 9, 2009

Mr. James Owen, Manager
Christian County Water District
P.O. Box 7
Hopkinsville, KY. 42241-007

Subject: Proposed Wholesale Rate Increase

Dear Mr. Owen:

HWEA will be proposing a water rate increase to the Hopkinsville City Council in August 2009. The purpose of the proposed rate increase is to support the indebtedness for the expansion and upgrade of the Moss WTP. HWEA is expanding and upgrading the Moss WTP from 10 MGD capacity to 15 MGD. Bids were received on June 18, 2009 and construction should begin in late summer or early fall. During both 2007 and 2008, the Moss WTP exceeded 85% of its capacity on 100 or more days. The expansion of the Moss WTP is needed to ensure adequate processed water for our customers.

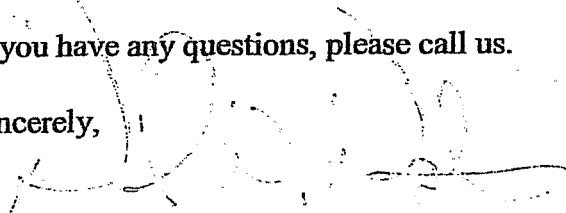
HWEA will be proposing to the Hopkinsville City Council the following wholesale water rates as established by Agreement 01-2005 between HWEA and the CCWD:

	<u>Rate/100 CF</u>	<u>Equivalent Rate/1000 Gal.</u>
First 3000 CF	\$2.96	\$3.96
Next 3000 CF	\$2.59	\$3.47
All Over 6000 CF	\$1.88	\$2.52

The new rates will go into effect for the CCWD 6 months after being approved by the Hopkinsville City Council consistent with Agreement 01-2005.

If you have any questions, please call us.

Sincerely,


Derrick W. Watson
Director of Technical Operations

HOPKINSVILLE WATER ENVIRONMENT AUTHORITY

401 E. Ninth Street, P.O. Box 628
Hopkinsville, KY 42240

MEMORANDUM

TO: Mayor Kemp and City Council Members

FROM: Len Hale, General Manager

DATE: June 29, 2009

SUBJECT: Proposed Water and Sewer Rate Increase

On July 23, 2009, we hope to present to the Council Committee a proposal for an immediate water and sewer rate increase. This increase was scheduled for last fall, but due to the Council's busy agendas, it was delayed to this summer. There are numerous factors that are contributing to the need for a water and sewer rate increase at this time. The last major water and sewer rate increase was in 2005 and was needed to support the Lake Barkley Raw Water Project and the wastewater SRF Phase Five program. A small (around 5%) rate increase was initiated by Council in 2006 to fund the REZ program. The last general rate increase occurred in 1993. Since then all of the water and/or sewer rate increases have been due to capital project indebtedness.

Some of the factors involved in this rate increase include:

Moss Water Treatment Plant (WTP) Upgrade and Expansion

HWEA has been proposing for the last two years to upgrade and expand the Moss WTP. City Council approved HWEA's request to apply for a low interest KIA loan on November 20, 2007 through MO #77-2007.

The next phase of the Federal Safe Drinking Water Act includes more stringent disinfectant by-product rules for trihalomethanes, cryptosporidium, haloacetic acid, and total organic carbon. These rules go into effect in 2 years. Also EPA is considering new limits for arsenic, nitrate, chromium, and TCE. The new groundwater rule, which affects the North Quarry, goes into effect on December 1, 2009. In order to ensure consistent and complete compliance with these more stringent federal regulations, HWEA must upgrade the filters and clarifiers at the Moss WTP.

Proposed Water and Sewer Rate Increase Memo

June 29, 2009

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In addition, the Moss WTP during 2008 exceeded 80% of its design capacity during peak conditions 103 days. In order to meet the existing and future peak water demands of Hopkinsville, Pembroke, Crofton, and Christian County, HWEA must expand the water treatment capacity of the Moss WTP. We have decided to increase the capacity by 50% to almost 14 MGD (million gallons per day).

The design of the upgrade and expansion of the Moss WTP has been approved by the State and bids opened on June 18. The lowest, most responsive bid of \$9.6 million was submitted by Smith Contractors of Lawrenceburg, KY. HWEA was fortunate to receive an \$8 million low interest loan from KIA at 1% interest for 20 years. A condition of the loan was that water rates had to be increased to support the loan by September 2009. HWEA has also been awarded a legislative grant of \$1 million for this project. The remainder of the financing for the project will be secured through a RUS loan at 3.65%. The \$8 million loan from KIA was a special arrangement for HWEA, since previously the maximum Fund F loan had been \$4 million.

Northside Wastewater Treatment Plant (WWTP) Decommissioning

In October 2007, the State issued a new permit for the Northside WWTP, which discharges treated wastewater into the North Fork of the Little River. The new permit included limits on phosphorus for the first time and was one of the first treatment plants in the State to be assigned phosphorus limits. (The State has classified the Little River as an "Impacted Stream".) Phosphorus is not a toxic contaminant, but is the first in the line of new nutrient limits that EPA and the State intend to impose on streams. Northside was issued a phosphorus limit of 1 ppm (parts per million).

The Northside WWTP was constructed in 1937 and has been upgraded three times. However, it is incapable of treating phosphorus to the level required by the State. From December 2007 through March 2008, HWEA conducted a series of in-stream tests to determine what, if any, impact the discharge of phosphorus had upon the North Fork. Our tests showed that even though Northside's discharge was above the State limit, it did not have an impact on the phosphorus concentration in the North Fork below the discharge. The tests revealed the impact was less than 0.2 ppm (parts per million).

We presented this information to the State and EPA. We had several telephone conferences, and even several meetings in Frankfort. Unfortunately, the State refused to reconsider the placement of phosphorus limits on the Northside WWTP and ordered

complete and consistent compliance with this new phosphorus limit. Although HWEA had been diligently arguing our case with the State, Kentucky began issuing Notices of Violations and placed HWEA and the Northside WWTP on its Clean Water Act watch list.

In a compliance conference in Frankfort on May 7, 2009, the State agreed to issue HWEA a KIA low interest loan at 1% for 20 years in the amount of \$7.5 million to decommission the Northside WWTP and incorporate it into the Hammond-Wood WWTP. The State has given HWEA until April 2012 to comply with the new phosphorus limits. The proposed sewer rates are needed to cover the indebtedness of the \$7.5 million loan to comply with the new phosphorus limits. City Council approved HWEA's indebtedness applications for SRF VI and VII on September 2, 2008 through MO #40-2008. (The SRF VII loan application has been denied funding by the KIA for FY 2009-10.)

Water and Sewer Revenues and Expenses

In FY 2007-08, total water and sewer revenues were down \$242,534 from the previous year. For FY 2008-09 through April, revenues are down additional \$113,357. Overall for the past two years, HWEA total revenues are down \$355,888 from the revenues of FY 2006-07. Typically we expect our revenues to increase by 2-3% annually based on urban growth. Lost industrial water and sewer revenues over the last 20 months total \$482,500, which is a loss of 42% of our typical industrial water and sewer revenues. In addition, we have received word that some of our major industrial users will shut down for several weeks this summer.

During this same period (2008-09), HWEA expenses took a tremendous impact from increases in fuel costs (47%, \$69,300), electric power costs (22%, \$289,800), and chemical costs (45%, \$45,400). As Federal and State regulations increase, so will the need to use more power and chemicals to accomplish the treatment required for compliance. For example, treating phosphorus will not only result in a capital expenditure of about \$8 million, but annually operating costs (power, chemicals, and maintenance) is expected to increase by \$350,000 to \$400,000 per year.

Reduction in Cash Flow

As expenses have increased over the last two years marked by a similar decrease in revenues, HWEA has had to use cash reserves to cover increased operation and maintenance and capital improvement projects. Over the last five years, HWEA has invested in several community capital projects for which there has been no reimbursement from federal, state or local sources. These projects include:

Proposed Water and Sewer Rates

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UK Extension Service Water and Sewer Extension	\$354,600
Conference Center Water and Sewer Extension	\$483,142
Eagle Way Water Extensions	\$89,500
Trilogy Center Sewer Extension	\$125,000
North Drive Soccer Complex Water and Sewer Extension	\$14,300
Trail of Tears Pump Station and Force Main	\$18,100
Wal Mart Distribution Center Water and Sewer Extensions	\$267,000

While all of these projects benefited the community and contributed to its economy, it may take several years for water and sewer revenues from these developments to pay for the cost of extending water and sewer facilities. For example, in 1997 and 1998, HWEA spent over \$2.4 million extending water and sewer facilities to Commerce Park. In addition, HWEA had to pay the Christian County Water District \$100,000 for the territory. To cover the cost of the capital expenditure and annual O&M costs, HWEA requires annual water and sewer revenues from Commerce Park of \$266,450. Last year, HWEA received only \$168,800 in water and sewer revenues from our customers in Commerce Park.

Proposed Water and Sewer Rates

In 2000 City Council requested that HWEA gradually convert from a diminishing rate structure to a one rate (flat rate) structure. At the time, HWEA had 6 tiers for rates with a diminishing structure for large consumers. However, research showed that little if any costs were reduced for large consumers compared to minimum or small users. Each subsequent rate increase has seen the reduction of tiers from the rate structure. Currently there are three tiers, down from 6 tiers. For this rate increase we are proposing a flat rate for all water and sewer customers.

For the HWEA Hopkinsville water system, we are proposing a flat water rate of \$2.95 per 100 cubic feet.

This translates into a monthly increase for the following customers of:

	<u>Existing Rate</u>	<u>New Rate</u>	<u>Difference</u>
Minimum customer	\$6.95	\$8.70	\$1.75
Avg. Residential (4000 gal/month)	\$13.10	\$15.50	\$2.40
Avg. Commercial (10,000 gal/month)	\$32.75	\$38.77	\$6.02
Avg. Industrial (70,000 gal/month)	\$137.10	\$271.40	\$134.30

Proposed Water and Sewer Rates
 June 29, 2009
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In a comparison with other Kentucky communities of similar size to Hopkinsville and with Clarksville, our new rates for the average residential customer look like this:

	<u>Their Rate</u>	<u>HWEA's Rate</u>
Bowling Green	\$18.50	\$15.50
Frankfort	\$16.86	\$15.50
Richmond	\$16.72	\$15.50
Madisonville	\$22.61	\$15.50
Clarksville	\$17.16	\$15.50

Prior to this rate increase, HWEA's water rate was the second lowest rate among 38 utilities in the nine-county region.

For the wastewater system, HWEA is proposing reducing the tiers to a flat rate of \$2.99 per 100 cubic feet.

This translates into the following average rate increases for the following customer classes:

	<u>Existing Rate</u>	<u>New Rate</u>	<u>Difference</u>
Minimum Customers	\$8.46	\$8.79	\$0.33
Avg. Residential (4,000 gal/month)	\$15.10	\$15.67	\$0.57
Avg. Commercial (10,000 gal/month)	\$37.70	\$39.17	\$1.47
Avg. Industrial (70,000 gal/month)	\$214.30	\$274.20	\$59.90

In comparison to other communities in Kentucky of similar size to Hopkinsville and also including Clarksville, our new rates for average residential consumption look like this:

	<u>Their Rate</u>	<u>HWEA's Rate</u>
Bowling Green	\$18.84	\$15.67
Frankfort	\$17.88	\$15.67
Richmond	\$20.12	\$15.67
Madisonville	\$31.00	\$15.67
Paducah	\$17.76	\$15.67
Clarksville	\$22.34	\$15.67

Pembroke and Crofton Divisions

Since the Pembroke and Crofton Divisions receive the benefit of the Hopkinsville water and sewer systems, we are proposing a similar rate increase for our customers in both of these Divisions. The proposed rates are:

Pembroke Water : \$3.52/100 CF

Pembroke Sewer: \$3.59/100 CF

Crofton Water: \$3.35/100 CF

Crofton Sewer: \$3.60/100 CF

These rates will be proposed to the Hopkinsville City Council with the proposed rate change for Hopkinsville.

Christian County Water District

The rates charged by HWEA to the Christian County Water District (CCWD) are regulated by the Public Service Commission (PSC). Although HWEA has a PSC approved rate contract with the CCWD that establishes the procedures for future rate increases, the CCWD can still object to any rate increase. If this should occur, HWEA will be required to participate in a PSC hearing on the rates. The 2005 rate increase resulted in an 18 month delay, costing HWEA over \$140,000 in lost revenues and \$65,000 to defend our rate increase. **The proposed water rate for the CCWD will be:**

	<u>Rate/100 CF</u>	<u>Equivalent Rate/1000 gallons</u>
First 3000 CF	\$2.96	\$3.96
Next 3000 CF	\$2.59	\$3.47
All Over 6,000 CF	\$1.86	\$2.50

These rates do not include any F&E charges, which have been prohibited by the PSC.

Summary

HWEA proposes a water and sewer rate increase to become effective September 1, 2009 that will raise the average residential water and sewer bill from \$28.19 to \$31.17. This rate increase is necessary to support the indebtedness of the expansion and upgrade of the Moss WTP, the decommissioning of the Northside WWTP, to cover increased operational costs for energy, fuel, and chemicals, to generate revenue to offset increased treatment costs required to comply with more stringent State and Federal standards, and recover lost revenues. The proposed rate increase is supported by HWEA auditors, York Neel, Inc. The rate increase proposed for HWEA customers compares favorably to other municipal utilities.