

THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

Before Commissioners: Chairman Mark Sievers
 Commissioner Ward Loyd
 Commissioner Thomas E. Wright

In the Matter of the Application of Suburban)
Water, Inc. d/b/a Suburban Water Company) Docket No. 11-SUBW-448-RTS
for an Order Increasing its Rates in)
Leavenworth County, Kansas.)

ORDER ON APPLICATION

The State Corporation Commission of the State of Kansas (Commission), having reviewed the files and being fully advised of all matters of record, finds and concludes as follows:

1. On December 21, 2010, Suburban Water Company, Inc. (Suburban) filed this Application under K.S.A. 66-117 and K.A.R. 82-1-231b, asking the Commission to allow an increase in rates for water service. The Application was filed to initiate an abbreviated rate case proceeding as agreed to by Suburban, Citizens Utility Ratepayer Board (CURB), and the Commission's staff (Staff).

2. In this Order, the Commission grants Suburban's request to increase rates for water service but makes this rate increase interim, non-final agency action subject to refund, or true-up, based upon Suburban's compliance with requirements listed in this Order and the Commission's decision in Suburban's subsequent rate cases. The Commission has jurisdiction over this Application under K.S.A. 66-117 and K.S.A. 66-1,231 to 66-1,233.

I. Background

3. Previously, the Commission denied Suburban's Application to approve a tariff for a purchased water adjustment (PWA) in Docket No. 10-SUBW-602-TAR (10-602).¹ In this November 3, 2010 Order, the Commission discussed several problems with Suburban's proposed PWA tariff that purported to pass through to Suburban's retail customers increased cost for

¹ *Order on Application*, Docket No. 10-SUBW-602-TAR (10-602), issued November 3, 2011 (November 3, 2010 Order).

wholesale water purchased from the Board of Public Utilities of the Unified Government of Wyandotte County/Kansas City, Kansas (BPU) to serve Suburban's retail customers.² Based upon its concerns, the Commission rejected the Application to approve a PWA tariff and directed Suburban to work with Staff to develop an appropriate abbreviated process to provide the Commission information needed to set just and reasonable rates, citing K.A.R. 82-1-231b.³

4. After filing of the November 3, 2010 Order, Suburban met with Staff and CURB to develop a rate case plan for the company, which was reflected in a letter dated November 23, 2010 (November 23, 2010 Letter or Letter), from Colleen Harrell, Litigation Counsel for Staff, to James G. Flaherty, Counsel for Suburban. The Letter summarized the parties' agreement that Suburban will use three annual, abbreviated rate case proceedings under K.A.R. 82-1-231b. The Commission discussed this Letter and the proposed abbreviated procedure during an Open Meeting on December 3, 2010. The Commission concluded a public hearing, with the Commission presiding, was not required as part of the first abbreviated proceeding. Instead, the Commission approved the Company conducting a meeting with its customers, as set out in K.A.R. 82-1-231b.

5. The Letter described the process agreed to be used as Suburban filed three abbreviated rate cases under K.A.R. 28-1-231b. In the first proceeding, which was initiated by this Application filed December 10, 2010, Suburban would rely on the cost of service the Commission approved in Docket 07-SUBW-1352-RTS, adjusted for these components: (1) the BPU's new cost of water as of January 1, 2011; (2) current retail rate charged by Suburban; (3) most recent sales volumes recorded by Suburban for 12 months ending June 30, 2010; and (4) rate case expenses minimized to the fullest extent possible. In addition, Suburban was to provide its most recent audited financial statements and planned to request a 6% margin on its operating expense. In the second docket, which is anticipated to be filed late 2011 (FY 2012), Suburban will file (1) a new cost-of-service study including cost of water increases, (2) any general cost

² November 3, 2010 Order, ¶¶ 28-40.

³ November 3, 2010 Order, ¶ 41.

increases, and (3) any cost increases related to any newly installed, automated meter-reading equipment. The Letter does not list rate case expense as an item to be requested in the second proceeding. In the third docket anticipated to be filed late 2012 (FY 2013), Suburban plans to rely on the cost-of-service results set during the second docket and adjust rates for the increased cost of water purchased from the BPU and the rate case expense for filing the rate case.⁴

6. The Letter listed items Suburban was to file in this first rate case proceeding, including those Suburban agreed to submit and additional items Staff identified to address concerns the Commission expressed in its November 3, 2010 Order. The Commission finds Suburban has not provided all the information agreed to in the November 23, 2010 Letter, page 2, and, for this reason, lists those items here. The Letter states Suburban agreed to submit the following information:

1. A comparison of what Suburban's wells were capable of producing in the year 2000 vs. customer demand at the time;
2. A comparison of what wells are currently capable of producing vs. current customer demand;
3. A list of potential water supply sources in 2000 (including the potential to drill new wells) and estimated costs of each of those sources, with supporting documentation;
4. A list of potential water supply sources in 2010 (including the potential to drill new wells) and estimated costs of each of those sources, with supporting documentation;
5. Suburban's interpretation of the terms and conditions of its contract with BPU and why the contract requires Suburban to pay BPU's wholesale water rate, including the PILOT;
6. A list of water utilities located in Leavenworth County and their source of water supply and what they pay for their water supply; and
7. A summary of Suburban's involvement in BPU's recent rate case and the outcome of that rate case (with supporting documentation of the rate increase for 2011 that is sought to be recovered in the rate case filing).

Suburban Witness Mike Breuer purported to address these items in his testimony filed with the Application. But Staff identified additional items in the November 23, 2010 Letter, page 2, that

⁴ November 23, 2010 Letter, page 1.

Suburban should discuss to address Commissioners' concerns identified in the November 3, 2010 Order, as follows:

1. Suburban's ability to mix Suburban's well water supply with BPU's water;
2. Whether the water Suburban is buying from BPU is surplus water that BPU will not need in the future;
3. Whether Suburban customers will be paying for free water services for the Kansas City Unified Government;
4. Suburban's future needs and the costs to renovate or expand its own water resources;
5. Whether the PILOT fee is a payment in lieu of taxes, as a service charge, or an administrative charge paid to the Unified Government;
6. The basis for the PILOT fee;
7. Suburban's recent attempts to find other sources of water; and
8. Evidence of anticipated growth in Suburban's service area and future water demand.

Having reviewed the record in this proceeding, the Commission finds evidence has not adequately addressed several of the items listed above. Each of these issues will be addressed more fully below, but generally they can be summarized by the following questions: (1) Is BPU using "surplus water" as anticipated in the contract to supply wholesale water to Suburban? (Staff's # 2.) (2) What legal basis exists for BPU to impose a PILOT fee on wholesale water provided to Suburban? Are rates charged Suburban ratepayers just and reasonable if the PILOT fee imposed by BPU is included and passed through to customers? (Suburban's # 5; Staff's ## 5-6.) (3) Can Suburban secure an alternative to BPU as a long-term water source for its customers? If Suburban will rely upon BPU as a long-term water source, can problems discussed in this Order be resolved? (Suburban's # 4; Staff ## 4, 7 and 8) Regarding the need for Suburban to secure an alternative water resource for Suburban to serve its customers long-term, the Commission has found it necessary to consider: (a) costs that would be required to renovate or expand Suburban's own water resources, (b) Suburban's recent attempts to find other sources of water, and (c) evidence of anticipated growth and future water demand in Suburban's service area.

7. In this Order, the Commission will discuss its reasons for granting Suburban's request to increase rates subject to true up or refund in subsequent proceedings. The Commission

will also review those items that still need to be addressed to support a permanent increase in rates for Suburban's customers. Finally, the Commission will discuss concerns regarding management of this company that must be addressed before the next rate case proceeding.

II. Pending Application.

8. In its Application, Suburban referenced the expedited process developed with Staff and CURB for making this abbreviated filing. Suburban has requested additional revenue of \$44,913.00, resulting in an increased commodity charge to customers of \$0.53 per 1,000 gallons.⁵ Suburban scheduled a public meeting with its customers for January 26, 2011, and mailed notice to each customer.⁶ With its Application, Suburban submitted an income statement based upon the cost of service in Docket 07-1352, as adjusted for (1) BPU's new cost of water effective January 1, 2011; (2) the current retail rate Suburban charges; (3) most recent sales volumes recorded by Suburban; and (4) rate case expense.⁷ Suburban provided a copy of its most recent financial statements.⁸ Testimony by Mike Breuer, Treasurer for Suburban, addressed the prudence of its purchasing practices relating to obtaining the most reliable and reasonable cost of water for its customers.⁹

9. CURB was granted intervention.¹⁰ On March 10, 2011, Staff filed a motion seeking permission to file testimony rather than file a Report and Recommendation, as customarily done in abbreviated proceedings. The Commission, granting this request, scheduled filing of testimony by Staff and CURB and allowed Suburban to file responsive testimony to Staff.¹¹ Staff witnesses Sonya A. Cushinberry, William E. Baldry, and Justin Grady submitted prefiled Direct Testimony on March 16, 2011. CURB witness Stacy Harden submitted prefiled Direct Testimony on March 30, 2011. Also on March 30, 2011, Suburban witness Gregory L. Wilson prefiled Responsive Testimony to Staff's witnesses. On April 5, 2011, Suburban filed a

⁵ Application, ¶¶ 3, 7.

⁶ Application, ¶ 4; Affidavit of Mailing by Mike Breuer, filed January 12, 2011.

⁷ Application, Exhibit B.

⁸ Application, Exhibit C.

⁹ Application, ¶ 5, and Exhibit D.

¹⁰ Order issued December 2, 2010.

¹¹ Order on March 18, 2011.

Motion to File Rebuttal Testimony to allow testimony in response to CURB's testimony; Suburban attached the Rebuttal Testimony of Gregory L. Wilson to its Motion.

10. The Commission grants Suburban's Motion to File Rebuttal Testimony of Gregory L. Wilson and has considered Wilson's Rebuttal Testimony in reaching the decisions announced in this Order.

III. Findings and Conclusions

11. The Commission recognizes that, due to the small size of this water company, Suburban has a significant challenge to provide efficient and sufficient service to its customers. The company's location has potential for significant future growth, but the recent down economy has resulted in a decline in the number of customers served. Although recognizing that a small company like Suburban faces many challenges in serving its clients during this economic downturn, the Commission has found that statements by Suburban Witness Breuer in his Direct Testimony were incorrect and misleading, which has raised serious questions about management of this company that will be addressed below in this Order.

A. Miscellaneous Public Utility

12. Before addressing the substantive issues in this proceeding, the Commission notes that Suburban is a miscellaneous public utility, as defined in K.S.A. 66-1,230. The Legislature delegated the Commission full power, authority and jurisdiction to supervise and control miscellaneous public utilities, such as Suburban. The Commission is empowered to do all things necessary and convenient to exercise that authority.¹² As a miscellaneous public utility, Suburban is required to furnish reasonably efficient and sufficient service, joint service, and facilities for use of any and all products or services rendered, furnished, supplied or produced by the utility. Thus, Suburban must provide reasonably efficient and sufficient water service to its customers. Any unjust or unreasonably discriminatory or unduly preferential rule, classification, rate, joint rate, fare, toll, charge or exaction is prohibited, unlawful and void. If Suburban does not establish and maintain just and reasonable joint rates, the Commission, after notice and hearing under the

¹² K.S.A. 66-1,231.

Kansas Administrative Procedure Act (KAPA), has power to require Suburban to establish and maintain just and reasonable joint rates that are reasonably necessary to maintain reasonably sufficient and efficient service.¹³

B. Order issued under K.A.R. 82-1-231b

13. The Commission has reviewed all prefiled testimony submitted in this proceeding pursuant to K.A.R. 82-1-229. The Commission recognizes parties asked that an interim order be issued by Friday, April 15, 2011, to allow proposed rate increases to go into effect on May 1, 2011. This was not possible due to the many other demands on the Commission's schedule as well as the Commission's desire to review the evidence in this proceeding to consider how parties have addressed concerns identified in Commission's November 3, 2010 Order. Having reviewed the evidence, the Commission approves the increase in rates set out by Staff's adjustments to rates requested in Suburban's Application but makes this increase subject to true-up or refund. Thus, the Order approves the Application with modifications, as contemplated by K.S.A. 82-1-231b(c)(5)(B).

14. If an Application is approved with modifications, K.S.A. 82-1-231b(c)(6) provides that an Interim Order will issue setting temporary rates, a 90-day comment period will be allowed for Suburban's customers, and, if the 90 days expire without receiving "substantial comment," the Commission will issue a final order making temporary rates permanent.¹⁴ If substantial comments have been received during the 90-day comment period, the Commission may order further investigation and a hearing.¹⁵ For good cause shown, the Commission may waive any requirements of this regulation.¹⁶

15. Here the Commission will allow the increase in rates requested by Suburban, but it will make this increase subject to true-up or refund based upon Suburban's subsequent rate cases. Because the Commission in this Order approves the rates subject to true-up or refund and finds

¹³ K.S.A. 66-1,232.

¹⁴ K.S.A. 82-1-231b(c)(6)(A)-(B).

¹⁵ K.S.A. 82-1-231b(c)(6)(B).

¹⁶ K.S.A. 82-1-231b(f).

further investigation and a hearing will be conducted as part of Suburban's case to be filed next year, the Commission concludes comments from ratepayers on an Interim Order are not needed at this time. During the rate case that will be filed in FY 2012, customers will be invited to submit comments and attend a public hearing. The Commission finds good cause exists to waive the 90-day comment period here and holds this Order will not be treated as interim under K.S.A. 82-1-231b(c)(6)(B). However, Suburban is ordered to mail a copy of this Order to each customer to inform them of this decision.

16. In evaluating the issues in this docket, the Commission has examined all the prefiled testimony submitted by parties and the numerous attachments to that testimony. The Commission will specifically discuss much of the testimony and address some of the attachments in reviewing issues in this Order. Even though an item in the record is not mentioned specifically, the Commission emphasizes its decision is based upon a review of the entire record submitted in this proceeding. The Commission is obligated to consider the record as a whole, including evidence that supports and detracts from its findings, and has done so in ruling on this Application.¹⁷ Also, the Commission is required under KAPA to state its findings and conclusions in writing, which it does in this Order.¹⁸ Having relied upon the entire administrative record as a whole in making its decision, the Commission concludes several issues identified in its November 3, 2010 Order still have not been adequately addressed.

C. The Commission approves Suburban's request to increase rates for water service but makes this increase subject to true-up or refund in subsequent rate case proceedings.

17. Suburban asked to change its tariff to recover additional revenues in the amount of \$44,913.00, which would be an increase in the commodity charge of \$0.53 per 1,000 gallons.¹⁹ In his Direct Testimony, Suburban Witness Breuer provided background about the company's origins in 1983 and its decision to enter into a contract for water service with the BPU in 2000.²⁰

¹⁷ K.S.A. 2010 Supp. 77-621(c)(7), (d).

¹⁸ K.S.A. 77-526; *Farmland Industries V. Kansas Corporation Comm'n*, 25 Kan. App. 2d 849, 852, 971 P12d 1213, 1217 (1999).

¹⁹ Application, ¶ 7, and Exhibit B.

²⁰ Breuer Direct, pp 2-3. Breuer's Direct Testimony is attached to Suburban's Application as Exhibit D.

18. Staff Witness William Baldry supported Suburban's request to recover additional revenues of \$44,913.00, or a 4.6% increase based upon sales for the 12 months ending December 31, 2009. Noting that Staff made five adjustments to Suburban's income statement, Baldry stated Staff's calculations resulted in a revenue requirement exceeding the increase requested by Suburban; therefore, Staff recommended Suburban's request be granted.²¹ As used in Docket 07-1352, Staff's revenue recommendation was based upon the 6% operating margin approach, which takes 6% of Suburban's adjusted operating expenses and adds the adjusted test year operating loss. Staff then added in the income tax expense using rates in effect in 2011. To determine purchased water cost, Staff used calendar year 2010 water volumes, including the calendar year 2010 volume purchased from BPU, rather than the water purchased for 12 months ending October 31, 2010. Staff also used actual rate case expense, rather than estimated costs, incurred through February 28, 2011.²² Baldry reviewed Staff's proposed adjustments and concluded these adjustments indicated Suburban understated its 2009 operating expenses in its Application.²³ After reviewing other wholesale water supply available to Suburban in the area, Baldry concluded that Suburban's contract with BPU made economic sense. Baldry pointed out all water companies surrounding Suburban Water purchase water from BPU, including the City of Tonganoxie and the City of Bonner Springs.²⁴ CURB Witness Stacey Harden criticized Baldry for including adjustments that were not part of the agreement reached among Suburban, Staff and CURB.²⁵ In Rebuttal Testimony, Suburban Witness Wilson notes that in summarizing the agreement of the parties, Harden omitted the requirement that Suburban include its most recent financial statements.²⁶

19. Staff Witness Sonya Cushinberry noted Baldry concluded Suburban was operating at a deficit and recommended approving a rate increase of \$44,913.00. Cushinberry explained

²¹ Baldry Direct, p. 2.

²² Baldry Direct, pp 6-8.

²³ Baldry Direct, pp 9-12.

²⁴ Baldry Direct, pp 16-19.

²⁵ Harden Direct, pp 11-13.

²⁶ Wilson Rebuttal, pp 1-2.

current Suburban payments to BPU for wholesale water purchases are a customer charge of \$160.00 plus \$2.05 per 1,000 gallons of water purchased and a PILOT fee percentage of 11.9%. Based upon rates established in Docket 07-1352, Suburban's retail customers currently pay a \$20.00 customer charge that includes 1,000 gallons of water used and \$7.33 per 1,000 gallons for any additional gallons.²⁷ A PILOT fee percentage of 9.9% is embedded in the \$7.33 per 1,000 gallons rate paid by retail customers.²⁸ If the increase is approved as requested in Suburban's Application and supported by its most recent audited financial statements,²⁹ rates for a residential customer using 5,000 gallons of water per month will increase \$2.12 per month, or from approximately \$49.32 to \$51.44.³⁰ CURB Witness Harden objected to Suburban's requested increased water charge because the increase appeared to apply to retail customers only and was not being passed through to Suburban's wholesale customers, which have recently experienced a dramatic increase in consumption.³¹ Suburban Witness Wilson explained how rates for wholesale customers are established, noting that any increase by BPU is passed through to Suburban's wholesale customers. Wilson pointed out that sales to Suburban's wholesale water customers produce positive net operating margins that contribute to Suburban's overall operating expenses, which results in a lower revenue deficiency for its retail customers.³²

20. The Commission finds Wilson's Rebuttal Testimony has addressed the objections raise by CURB and accepts Wilson's explanation of these issues. The Commission recognizes that evidence in the record, as cited by Staff in its recommendation, supports an increase in rates to recover increased charges being imposed on wholesale water purchased by Suburban. The Commission is aware that a company cannot operate at a deficit and continue to provide efficient and sufficient service to its customers. But the Commission concludes this record is deficient regarding issues that must be resolved before the Commission can decide to allow charges

²⁷ Application, Exhibit B.

²⁸ Cushinberry Direct, p. 15.

²⁹ Application, ¶ 5, and Exhibit C.

³⁰ Cushinberry Direct, p. 16.

³¹ Harden Direct, pp 17-22.

³² Wilson Rebuttal, p. 4.

imposed by BPU to be passed through to Suburban's customers on a permanent basis. The Commission grants Suburban's request for a rate increase of \$44,913.00 but, until these issues are resolved, the increase is approved as interim rates, subject to true-up or refund, based upon decisions in subsequent rate case proceedings addressing these issues.

D. Legal Issues concerning enforceability of the contract between Suburban and BPU still have not been fully addressed.

21. In its November 3, 2010 Order, the Commission specifically identified several legal questions regarding Suburban's increasing dependence upon its contract with BPU to supply water to its customers. The Commission pointed out that water purchased from BPU as a percentage of total water available for sale increased from 15% in 2002 to 56% in 2009.³³

22. The Commission also questioned whether the Unified Government of Wyandotte County/Kansas City, Kansas (Unified Government), which owns BPU, included rates for "free services" in the rate schedule for wholesale customers, like Suburban.³⁴ The Commission pointed out such free water service included water used by the city, city hall, parks and other operations of the Unified Government.³⁵ Suburban Witness Breuer asserted that whether the price paid to BPU included charges for free water service to the Unified Government was not relevant if Suburban acted reasonably in contracting to purchase water from BPU. Instead, Suburban argued the relevant issue is whether BPU's water supply was the least cost and most reliable alternative available in 2000 when Suburban entered into the Water Contract.³⁶

23. The Commission rejects Suburban's assertion that this issue is not relevant to a review of Suburban's request for a rate increase. All Suburban's retail ratepayers are located in Leavenworth County and receive no benefit from providing free water service to the Unified Government. Although the Commission finds the issue is relevant, Staff Witness Cushinberry concluded no cost for providing free water service was allocated to BPU's wholesale customer

³³ November 3, 2010 Order, ¶ 12, *citing* Docket 10-602, Wilson Direct Testimony, p. 5.

³⁴ November 3, 2010 Order, ¶ 24.

³⁵ November 3, 2010, *citing* Tr., 55-56 (Wilson).

³⁶ Breuer Direct, pp 12-13.

group that includes Suburban. Cushinberry, citing the Black & Veatch Report that was submitted in Docket 10-602 to show what information was considered in BPU's rate case, testified that "[c]osts associated with City and Interdepartmental service and public fire protection are not recovered through direct charges, therefore, the cost of service for these classes is reallocated to all other [BPU] retail customers in proportion to their allocated cost of service."³⁷ In addition, Cushinberry confirmed that BPU's retail customers paid all expenses associated with free water services, not BPU's wholesale customers such as Suburban.³⁸ The Commission concludes Staff Witness Cushinberry has adequately addressed this issue.

24. But other issues have not been adequately addressed. Several witnesses have attempted to explain why Suburban's proposed rates should be found reasonable without resolving the legality of certain provisions under Suburban's contract with BPU. The Commission will review these issues separately and will require parties to address these legal issues before any subsequent request for a permanent rate increase by this company will be considered.

25. (1) Surplus water: K.S.A. 13-1223 provides that the BPU has exclusive control over daily operations of the water plant and "*shall be charged with the duty of producing and supplying the city and its inhabitants with water . . . for domestic and industrial purposes and for public use in the city, and subject to the provisions in K.S.A. 66-104 and 66-131, may sell and dispose of any surplus outside of the city.*"³⁹ The Contract for Water Service between Suburban and the BPU, dated April 6, 2000, (Water Contract) states that "all water to be supplied by the BPU to [Suburban] pursuant to the terms of the Contract shall be surplus water produced by the BPU not required for use within the corporate limits of the Unified Government."⁴⁰ In its November 3, 2010 Order, ¶ 19, the Commission questioned whether the water being supplied to Suburban by BPU was surplus water as defined in the Water Contract.

³⁷ Cushinberry Direct, p. 8.

³⁸ Cushinberry Direct, pp 8-9.

³⁹ K.S.A. 13-1223 (emphasis added).

⁴⁰ Contract for Water Service between Suburban and the BPU, dated April 6, 2000, page 1, (Water Contract, p. 1)

26. According to Suburban, BPU stated it "has adequate supplies to meet the needs of its wholesale customers, including [Suburban], over the remaining primary term of [Suburban's] contract with BPU."⁴¹ Suburban pointed to information in BPU's recent rate case, noting BPU's overall sales during the past several years have declined. Suburban considered BPU to be a highly reliable source of water supply. BPU recently added the City of Tonganoxie as a new wholesale customer and Suburban "has not faced any significant interruption of service" during the 10 years BPU has provided Suburban water.⁴²

27. Staff Witness Cushinberry cited Suburban's reliance on an email from the BPU asserting the BPU believed it would have surplus water in 2020 and would include current wholesale customers in its future master planning process for capital improvements. Potentially this included further development of BPU's future water rights in the Missouri River Basin.⁴³ In addition, Staff pointed out that BPU is a member of the Kansas River Water Assurance District No. 1. As a member of an assurance district under the Water Assurance Program Act, BPU acquired rights to storage space in Milford, Tuttle Creek and Perry Reservoirs. This storage space and the water contained within it can be used or released during periods of drought to assure its members of the District will have enough water to meet their demands. Although recognizing no one can be completely sure BPU will have enough water to meet future needs of its wholesale customers, Cushinberry concluded the possibility of BPU not having adequate water reserves to meet Suburban's needs was pretty remote. Thus, Staff concluded BPU is capable of providing reliable water service to all its customers, including Suburban.⁴⁴

28. As the Kansas appellate courts have clearly stated, administrative agencies are creatures of statute and may only act within the scope of authority granted by that agency's authorizing statutes.⁴⁵ Thus, BPU must act within its authority as set out by the Legislature. The

⁴¹ Breuer Direct, p. 15.

⁴² Breuer Direct, p. 16.

⁴³ Cushinberry Direct, pp 12-13, and SAC Exhibit No. SAC 6.

⁴⁴ Cushinberry Direct, pp. 13-15.

⁴⁵ *Kansas Industrial Consumers Group v. Kansas Corporation Comm'n*, 36 Kan. App. 2d 83, 92, 138 P.3d 338, appeal following remand at *Kansas Industrial Consumers v. Kansas Corporation Comm'n*, Unpublished Slip Op. No. 99,415 (KS App. filed Feb. 11, 2008).

Commission is concerned that testimony by Suburban and Staff is hearsay and furthermore has not answered the Commission's underlying concern about surplus water as stated in the November 3, 2010 Order, ¶ 19.⁴⁶ This testimony does not address whether water used to supply BPU's wholesale customers is "surplus water" not needed to fulfill BPU's duty "of producing and supplying the city and its inhabitants with water . . . for domestic and industrial purposes and for public use in the city" as required in K.S.A. 13-1223. The area Suburban serves is adjacent to an area of significant growth in Wyandotte County. In addition to the Kansas Speedway, minor league baseball stadium, and Legends shopping district, a new major league soccer stadium for Sporting Kansas City is being completed. Also, Google recently selected Kansas City, Kansas, as the site for deployment of its ultra high-speed internet service. As this area develops, demand will increase on BPU for public use in the city. If the source of water BPU uses to serve its wholesale customers like Suburban is not clarified, the Commission can foresee that BPU may have an increased demand for water "within the corporate limits of the Unified Government" that results in it terminating its Water Contract with Suburban based upon "any other cause reasonably beyond the control of the BPU."⁴⁷ The Water Contract specifically provides that no liability will accrue to BPU during the term of any interruption of the supply of water by the BPU "due to . . . any other cause reasonably beyond the control of the BPU."⁴⁸ In addition to an increase in water demand leading BPU to terminate the Water Contract, the Commission finds it foreseeable that a third-party customer of BPU, at some time in the future, could seek an injunction to cut off Suburban's access to extra BPU water under a claim that the third-party user has priority to the water from BPU "for domestic and industrial purposes and for public use in the city . . ." under K.S.A. 13-1223.

29. The Legislative directive to BPU states that water used to supply wholesale customers like Suburban must be "surplus water," but the Water Contract with Suburban contains

⁴⁶ Breuer Direct, pp 15-16 ("BPU has informed [Suburban] it has adequate supplies to meet the needs of its wholesale customers."); Cushinberry Direct, pp 12-13 ("[A]n email from BPU [stated] it would have surplus water in 2010 and . . . BPU is including all current wholesale customers in its future master planning process.").

⁴⁷ Water Contract, pp 1-2.

⁴⁸ Water Contract, p. 1.

no covenant or other provision to insure this "surplus water" will be available in the future for wholesale customers. In this proceeding, Suburban has indicated its intent to rely upon BPU as its main long-term water source. If this is the case, the Commission will require parties to address how Suburban can receive a guarantee from BPU that water being used to provide Suburban wholesale water is surplus water under K.S.A. 66-1223 that will be available in spite of anticipated growth in Wyandotte County. Mere oral or email assurances from BPU employees is not sufficient to insure a long-term water resource. Suburban must address this issue, such as through an Addendum to the Water Contract, before the Commission will consider a subsequent request for a permanent rate increase to recover increased charges for BPU wholesale water.

30. (2) PILOT Fee: In the November 3, 2010 Order, the Commission questioned whether BPU had authority to impose a PILOT fee on Suburban under terms of the Water Contract. PILOT stands for "payment in lieu of taxes"; this PILOT fee is remitted to the Unified Government.⁴⁹ A taxing subdivision of the state of Kansas is authorized to enter into contracts for the payment of service charges in lieu of taxes with the owner or owners of property that is exempt from payment of ad valorem taxes under Kansas law.⁵⁰ Kansas law requires contracts with provisions for payment of service charges in lieu of taxes "shall provide for the making of payments there under to the county treasurer of the county receiving such payments or the county in which any other taxing subdivision receiving such payments is located."⁵¹ K.S.A. 12-148 describes how moneys from these payments are apportioned and paid.⁵²

31. Each monthly billing under the Water Contract between Suburban and BPU imposes a dollar rate per 100 cubic feet, a monthly customer charge of \$160.00, and "[t]he Unified Government Payment in Lieu of Taxes (PILOT) fees, currently 5.9 multiplied by amount due for gross monthly water sales plus the Customer charge."⁵³ The Water Contract further provides that the rate "shall be subject to annual review and adjustment commencing one year

⁴⁹ November 3, 2010 Order, ¶ 24, *citing* Black & Veatch Study, pp 2, 19, 21.

⁵⁰ K.S.A. 12-147.

⁵¹ K.S.A. 12-148.

⁵² K.S.A. 12-148(1) to (4).

⁵³ Water Contract, pp 6-7.

after the commencement of service pursuant to this contract."⁵⁴ The Commission questioned BPU's authority to impose this PILOT fee on wholesale water sold to Suburban.⁵⁵

32. Suburban Witness Breuer stated that whether Suburban paid a PILOT fee under the contract was not relevant. In his opinion, the relevant questions were (1) whether Suburban needed to obtain another source of water supply in 2000 to meet the future demand of customers, (2) whether BPU provided the least cost and most reliable source of water supply to meet this demand, and (3) whether it was reasonable for Suburban to agree to purchase water from BPU based upon the price BPU charged its wholesale customers. Breuer pointed out other supply alternatives would likely include payment of a PILOT fee in the total price it charged for water.⁵⁶ Regarding terms of the Water Contract, Breuer testified the PILOT fee is "a cost that BPU has to pay the Unified Government for the right to use the streets and public right of ways located within the boundaries of the Unified Government to locate BPU's pipes, facilities and equipment."⁵⁷ Breuer described the PILOT fee the Unified Government charges BPU as a cost of service incurred in providing utility service. Equating the PILOT fee to a franchise fee a public utility pays a municipality to use the city's streets and public rights-of-way, Breuer asserted Suburban as a utility should be allowed to pass the cost to pay the PILOT fee through to its customers.⁵⁸

33. Staff witness Cushinberry discussed the Commission's concerns regarding the PILOT fee expressed in the November 3, 2010 Order. Cushinberry noted that, by Charter Ordinance, the BPU is required to contribute a portion of its gross operating revenues to the Unified Government, which amount must be no less than 5% and no more than 15% of BPU's gross revenues. The Unified Government has proposed to reduce the PILOT percentage fee that BPU charges its retail and wholesale customers, including Suburban, from the 2010 rate of 12.8% to 11.9% in 2011, 9.9% in 2012, and 9.9% in 2013.⁵⁹ Staff noted the Commission questioned (1)

⁵⁴ Water Contract, p. 7.

⁵⁵ November 3, 2010 Order, ¶¶ 25-27.

⁵⁶ Breuer Direct, pp 12-13.

⁵⁷ Breuer Direct, pp 14-15.

⁵⁸ Breuer Direct, pp 15-16.

⁵⁹ Cushinberry Direct, pp 3-4.

BPU's taxing authority under K.S.A. 12-147, (2) the Commission's authority to pass through to Suburban's customers the PILOT fee charged by BPU, and (3) the fact communities and customers served by Suburban were located in Leavenworth County and, therefore, would not benefit from the PILOT fee paid to the Unified Government of Wyandotte County.⁶⁰ Reviewing K.S.A. 12-147, Staff concluded that BPU-owned property is exempt from income and property taxes and, therefore, the Unified Government may assess a PILOT fee against the BPU. Staff reasons the BPU can recover the PILOT fee as a business cost by passing this expense through to retail and wholesale customers. Although agreeing with the Commission that Suburban customers are located in Leavenworth County and outside the jurisdiction of the Unified Government, Staff concluded Suburban's customers benefit directly from imposition of the PILOT fee due to the water Suburban purchases from the BPU.⁶¹ Finally, Staff compared the PILOT fee with taxes an Investor Owned Utility would be required to pay and allowed to recover from customers. Staff concluded BPU's PILOT fee is reasonable and Suburban should be allowed to recover these costs through rates if the PILOT fee is "uniformly applicable to all wholesale customers,"⁶² and if Suburban incurs this cost to provide service to its customers.⁶³

34. The Commission finds Suburban's and Staff's analysis is flawed. The Unified Government, not BPU, "owns and operates [the] waterworks plant."⁶⁴ The BPU is not a taxing subdivision authorized to enter into agreement with owners of tax exempt property under K.S.A. 12-147. Instead, the BPU is an administrative agency that manages, operates, maintains and controls the daily operation of the publicly-owned water plant that serves the Unified Government. Staff and the company have missed the point of the Commission's concern in concluding the charge a private company would impose for water would be more than what BPU is imposing through a PILOT fee percentage. Even if the amount of the PILOT is reasonable, imposing *any* PILOT fee charges on Suburban ratepayers cannot be "just and reasonable" under

⁶⁰ Cushinberry Direct, pp 4-6.

⁶¹ Cushinberry Direct, p. 6.

⁶² Water Contract, p. 7.

⁶³ Cushinberry Direct, pp 6-7.

⁶⁴ K.S.A. 13-1220.

K.S.A. 66-1,232 if BPU has no authority to impose such charges on Suburban. Thus, the question at this juncture is not whether the amount imposed by the PILOT fee is reasonable but whether legally BPU can impose any PILOT fee. The Water Contract is between BPU and Suburban; BPU is not a taxing subdivision. The parties have not cited legal authority giving BPU the ability to assess a PILOT fee. Therefore, the Commission still questions BPU's authority to impose a PILOT fee as part of the Water Contract with Suburban. If BPU has no power to impose a PILOT fee, a contract that contains a provision in which BPU asserts its authority to do so is ultra virus and cannot be enforced as written.⁶⁵

35. Nor does BPU have authority to impose a PILOT fee on behalf of the Unified Government on parties located outside Wyandotte County. To the extent BPU has any authority to impose a PILOT fee on behalf of the Unified Government for providing services within Wyandotte County, that power does not extend into Leavenworth County. A taxing subdivision does not have legal authority to impose a PILOT fee outside its jurisdiction; therefore, BPU has no authority to pass through such a PILOT fee in rates to customers located outside the taxing subdivision. If charging for the PILOT fee is prohibited, including those charges in Suburban's rates would make them unjust and unreasonable, and unlawful and void.⁶⁶ The Commission has granted the increase in rates requested by Suburban subject to true-up or refund and concludes charges for the PILOT fee cannot be passed through to Suburban's customers. Therefore, the Commission directs parties to determine, for purposes of Suburban's next rate case, what portion of the revenue increase granted in this Order is attributable to PILOT fee charges. Any amount recovered by Suburban between this decision and the next rate case that is attributable to PILOT fee charges shall be determined and addressed in the next rate case.

36. (3) Setting just and reasonable rates: A miscellaneous utility may charge its customers "just and reasonable rates" but unjust or unreasonably discriminatory or unduly preferential rates are "prohibited, unlawful and void." K.S.A. 66-1,232. The Commission has

⁶⁵ *Genesis Health Club v. City of Wichita*, 285 Kan. 1021, 181 P.3d 549 (2008).

⁶⁶ K.S.A. 66-1,232.

authority to require miscellaneous public utilities to establish and maintain "just and reasonable joint rates" needed "to maintain reasonably sufficient and efficient service." K.S.A. 66-1,232. The problem is determining whether charges Suburban has agreed to pay BPU for wholesale water under the Water Contract are "just and reasonable" to include in rates passed through to Suburban's retail customers. The question of what constitutes "just and reasonable" rates is the same dilemma underlying whether BPU's wholesale water is "surplus water" under the contract and whether BPU has authority to impose a PILOT fee on wholesale water purchased by Suburban. If the water BPU is using to supply Suburban is not surplus, then selling the water to Suburban violates K.S.A. 66-1,232 and cannot be considered in establishing just and reasonable rates for a miscellaneous utility like Suburban. Similarly, if BPU has no authority to impose a PILOT fee on wholesale water purchased by Suburban, then the Commission cannot approve rates that pass through charges that are prohibited, unlawful and void.

37. Due to these continuing questions, the Commission finds it difficult to determine whether charges the BPU has set for wholesale water sales are just and reasonable. At the time the Commission issued its November 3, 2010 Order, BPU was conducting an ongoing proceeding to establish rates but had not adopted a rate schedule. As a result, the Commission pointed out it was not known what rates Suburban would be passing through to customers under a PWA if the parties' agreement was approved.⁶⁷ Here, Suburban Witness Breuer has described Suburban's intervention and participation in BPU's rate case. Suburban was the only wholesale water supply customer to intervene. Suburban attended a BPU public hearing and participated in technical hearings. At its June 16, 2010 hearing, BPU approved an 8% increase in water rates, as recommended by Black & Veatch, but BPU did not decide on proposed rate increases for 2011, 2012, and 2013.⁶⁸ In September 2010, Black & Veatch and the BPU Staff filed rebuttal testimony that revised downward the original increase recommended for rates. During its October 6, 2010 Open Meeting, the BPU voted unanimously to adopt the increase in rates originally recommended

⁶⁷ November 3, 2010 Order, ¶¶ 19-22.

⁶⁸ Breuer Direct, Exhibit MB-13, *In the Matter of BPU 2010 Rate Hearing*, October 6, 2010 Transcript, page 5 (Exhibit MB-13, p. 5).

by Black & Veatch and instructed BPU Staff to provide an annual analysis of whether BPU's financial metrics were met. The BPU indicated that, if those metrics were exceeded, BPU Staff was to consider recommending a downward adjustment in rates during later years of the rate plan. Suburban pointed out that the BPU did not discuss its Staff's rebuttal testimony, which recommended a smaller increase in rates.⁶⁹ BPU issued an Order on October 20, 2010, rejecting its Staff's proposal to reduce the previously proposed rates in 2011, 2012, and 2013; instead, BPU stated it preferred to reduce rates at the end of a study period rather than initially because another rate proceeding would be required to increase rates.⁷⁰

38. The Commission questions whether BPU exceeded its authority in deciding to initially set higher rates than those ultimately recommended by its Staff and its consultant in order to avoid conducting a rate proceeding in the future. The Legislature specifically stated that the BPU "shall fix reasonable rates for water furnished to consumers which: (a) Will secure an income sufficient to pay all salaries and wages of all officers and employees in such departments; (2) will cover the cost of all materials and supplies used in the operation of the plant; (3) will cover the cost of all repairs; (4) will cover all miscellaneous expenses; (5) will pay the principal of and the interest on all revenue bond indebtedness . . .; and (6) will cover the cost of all repairs and renewals of the plant and all material used, together with a reasonable allowance for emergency and unforeseen expenses."⁷¹ An agency may only act within the scope of authority granted by its authorizing statute.⁷² This statute contains no provision allowing BPU to fix rates for water higher than needed to cover the expenses specifically listed in the statute in order to avoid the need to conduct a rate case in the future. The Commission questions how rates established by the BPU for expenses articulated by statute can be considered just, reasonable and necessary if those rates are set at an amount higher than allowed by K.S.A. 13-1227. Rather than adopting rates its Staff proposed to cover those costs specified by statute, BPU ordered its Staff to

⁶⁹ Breuer Direct, pp 9-11; Breuer, Exhibit MB-13, pp 29-31, 38-42.

⁷⁰ Breuer Direct, pp 10-11; Breuer, Exhibit MB-14, *In the Matter of the 2010 Electric Revenue Changes and Water Revenue Changes*, Board of Public Utilities, Order issued October 20, 2010, page 8, ¶ 11.

⁷¹ K.S.A. 13-1227.

⁷² *Industrial Consumers Group*, 36 Kan. App. 2d at 92.

do an analysis at the end of the fiscal year to determine if rates needed to be adjusted downward to establish reasonable rates. In deciding this issue, members of the BPU recognized the rates set exceeded the amount needed to cover costs and expressed an expectation that rates would need to be lowered. One BPU Board Member explained the BPU was at a critical junction and the Board needed "to restore our cash reserves."⁷³ The Board's reasoning suggested it decided to recover higher rates for water than needed to pay the expenses listed in the statute.

39. The Commission does not have jurisdiction over the BPU, but a reasonable analysis of BPU's decision leads to the conclusion that BPU may have exceeded its authority by setting rates that accumulate more money than needed to cover expenses specifically listed in K.S.A. 13-1227. If the Commission finds the BPU has exceeded its authority in setting rates, the Commission, after full hearing and investigation, has power to fix and order substituted rates that are just and reasonable.⁷⁴ In using this abbreviated proceeding, the parties recommended and the Commission agreed that an evidentiary hearing was not needed. However, the Commission finds parties have not fully addressed the legal arguments regarding whether BPU has imposed higher-than-needed rates and whether such rates can be passed through to Suburban's customers as just and reasonable under K.S.A. 66, 1,232. Because this abbreviated proceeding did not provide a full hearing and investigation into what just and reasonable rates should be fixed to substitute those requested by Suburban, the Commission holds the increase approved in this Order will be interim, subject to true-up or refund, to allow parties to address this issue in Suburban's next rate case proceeding. That proceeding will be a full rate case under K.A.R. 82-1-231, which the Commission understands will be filed late in 2011 during FY 2012 .

E. Suburban must secure a long-term water source to insure efficient and sufficient service to its customers.

40. The Commission is still concerned about Suburban's growing dependence upon purchasing water from BPU as its only long-term water resource to serve customers for reasons

⁷³ Exhibit MB-13, p. 47.

⁷⁴ K.S.A. 66-1,234 and 66-1,236.

expressed in this Order. Suburban's dependence on purchased water as a percentage of total water available for sale increased from 15% in 2002 to 56% in 2009.⁷⁵ The Commission pointed out that the record in Docket 10-602 did not make clear whether wells owned by Suburban were less productive because water was not available or because of mechanical or technical problems. Also, the record was not clear about what other water sources might be available as an alternative to purchasing water from BPU either by obtaining new water rights or by improving the ability to intake and treat raw water using Suburban's facilities. Finally, the Commission was concerned that Suburban was not actively pursuing other wholesale water sources to develop an alternative to purchasing water from BPU. The Commission concluded the record developed in Docket 10-602 contained many unanswered questions about Suburban's present and future water supply and left for speculation what other water sources might be available to serve Suburban customers.⁷⁶

41. Suburban Witness Breuer described the origins of Suburban, beginning in 1983 as a water utility service for a small number of customers. Water was supplied from groundwater the company was authorized to appropriate from its two water fields: The Moran Well Field, which at its peak contained 5 wells, and the Harper Well Field, which contained 3 lower capacity wells. Both are located in Leavenworth County. During the late 1990s, demand increased and Suburban became concerned about whether its own water fields would be sufficient to meet demands of the significant increase in the number of customers connected to its system. A report by Kramer Engineering in 1999 evaluated Suburban's projected meter growth and the adequacy of Suburban's water supply and water storage capacity. Breuer stated this report supported Suburban's decision to contract for water service with BPU. The Kramer Report, which was updated in April 2003 and revised again in July 2004, was submitted in KCC Docket No. 07-SUBW-1352-RTS (07-1352) to support Suburban's decision to construct and place a 1.5 million gallon storage tank into operation. Breuer incorporated information in the revised Kramer Report as part of his testimony here to address KCC concerns regarding Suburban's water supply and

⁷⁵ November 3, 2010 Order, ¶ 12, *citing* Wilson Direct, p. 5.

⁷⁶ November 3, 2010 Order, ¶¶ 13-16.

water use between 2000 and 2004.⁷⁷ In this Order, reference to the Kramer Report will be to this Preliminary Engineering Report dated April 2003, Revised July 26, 2004 (Kramer Report).

42. Breuer provided information that compared what Suburban's wells were capable of producing and customer demand in 2000 with what Suburban's wells were capable of producing and customer demand in 2010.⁷⁸ In addition, a graph was submitted showing well production versus customer demand for years 2000 and 2010 and the static level of Suburban's Moran well field from 1998 through 2010.⁷⁹ Suburban described the water supply sources available in 2000 and asserted that BPU was the only practical wholesale supplier available then, providing the least cost alternative. The City of Leavenworth County, Kansas, and Johnson County Water District, n/k/a Water One, were not interested in making wholesale water sales due to lack of excess water; also, distance and other geographical impediments made it not economically practical to contract with them. Water tables at Suburban's two existing well sites would likely be adversely affected by increased production, resulting in insufficient additional capacity.⁸⁰ Breuer claimed the potential water supply sources in 2010 would be the same as in 2000 and the same problems remain, making these sources not economically feasible. Although not citing support for its statements, Suburban estimated the cost to find a new ground water supply and drilling wells to obtain the water would be approximately \$400,000.00 and doubted its ability to obtain water rights near its distribution system because of existing water rights of other property owners.⁸¹ Suburban provided a table comparing just the price of potential water supplies without including investment expenses to connect to other suppliers.⁸² Suburban listed water utilities located in Leavenworth County, Kansas, showing their water supply and cost of water and noting all smaller water utilities obtain water from BPU and pay the same price as Suburban.⁸³

⁷⁷ Breuer Direct, pp 1-3.

⁷⁸ Breuer Direct, pp 2-3; Compare Exhibit MB-2 with Exhibit MB-3.

⁷⁹ Breuer Direct, pp 3-4; Exhibit MB-4.

⁸⁰ Breuer Direct, pp 4-5.

⁸¹ Breuer Direct, p. 6.

⁸² Breuer Direct, pp 6-7; Exhibit MB-5.

⁸³ Breuer Direct, p. 7.

43. Staff Witness Justin Grady analyzed Suburban's water supply practices regarding concerns expressed in the November 3, 2010 Order.⁸⁴ Reviewing Suburban's past and present water supply efforts, Grady discussed Suburban's company-owned wells, its previous applications with the Division of Water Resources to gain additional groundwater rights, and the characteristics and limitations of the aquifers that provide groundwater in Suburban's area. Grady reviewed Staff's investigation into Suburban's water supply efforts, keeping in mind the Commission's desire to lessen the burden of rate case expense. Staff examined Suburban's responses to data requests, publicly available information, and informational interviews with staff of the Division of Water Resources (DWR), a division of the Department of Agriculture, and of the Kansas Water Office.⁸⁵ Staff learned that some aquifers in Suburban's territory have a history of declining water tables, limited production, and special characteristics that require enhanced levels of information before water rights will be granted. These factors have limited Suburban's production from its own wells and have inhibited Suburban's ability to secure additional ground water resources.⁸⁶

44. Staff reasoned ground water, if available, would likely be more economical than purchasing water from BPU. But currently BPU is Suburban's least-cost wholesale water option among available providers, and surface water collections and treatment do not appear to be economical for Suburban at this time. Grady noted Suburban feels a study is needed that focuses on the best potential for groundwater availability, for success at receiving water rights, etc., before pursuing additional ground water resources. Staff, on the other hand, pointed out pursuing a study presents risks and benefits and suggested the Commission may want an expert hydrologist to provide more information before deciding upon a further study.⁸⁷

45. Grady began by examining groundwater aquifers in Suburban's territory. Glacial drift aquifers or alluvial aquifers are the major source of groundwater in Suburban's service area,

⁸⁴ Grady Direct, pp 2-5.

⁸⁵ Grady Direct, pp 6-7.

⁸⁶ Grady Direct, 7.

⁸⁷ Grady Direct, pp 7-8.

existing along surface water drainages such as Stranger Creek.⁸⁸ Suburban's Moran well field site is a Glacial Drift aquifer with unique characteristics that limit further development, including declining water levels and claims of interference between two wells using the same aquifer. Enhanced information requirements are needed when seeking water appropriation from this aquifer.⁸⁹ Suburban's Harper field taps into the edge of another area of glacial drift aquifers, but Staff found little information about this aquifer.⁹⁰ Staff reported that Suburban filed for water appropriation rights in 1989 for an area that appears to overlap with this aquifer, but later Suburban dismissed the application. Through discovery, Staff learned that the site Suburban proposed could not support the requested quantities of water and DWR denied the Application.⁹¹

46. Next, Grady discussed Suburban's well production, noting that historically Suburban has used wells from the Moran well field and the Harper well field to serve its customers.⁹² The Harper field originally had three wells and initially was Suburban's sole source of water. Suburban closed this facility in 2008 and relinquished its water rights on August 13, 2009, after the water table declined significantly and it was not cost effective to continue operating.⁹³ The Moran field previously had five wells. One well is no longer pumping, Suburban attributes to a lower water table due to interference by the Rural Water District Number 7 (RWD No. 7) at approximately ½ mile south east of the Moran field. Grady explained that a phenomenon referred to as a "Cone of Depression" can affect the amount of water that can be drawn from an aquifer if the water column surrounding a well is lowered to a point below the intake of the well.⁹⁴

47. Grady described an impairment investigation Suburban requested to determine if the RWD No. 7 well was impairing the ability of the Moran field to pump Suburban's senior water rights. The DWR granted RWD No. 7 an application for water rights, but RWD No. 7 had

⁸⁸ Grady Direct, pp 9-10; Exhibit JTG-2 (geologic map showing aquifers).

⁸⁹ Grady Direct, pp 10-11.

⁹⁰ Grady Direct, pp 11-12.

⁹¹ Grady Direct, pp 12-13.

⁹² Grady Direct, p. 13; Exhibit JTG-4 (map of well fields).

⁹³ Grady Direct, pp 13-17; Exhibits JTG-7, JTG-8, JTG-9.

⁹⁴ Grady Direct, pp 17-19.

to reduce the size of its pump to account for limitations of the aquifer. During the impairment investigation, the DWR discovered that Suburban was pumping water from two illegal wells, i.e. wells that were not permitted by the DWR, between the Moran field and RWD No. 7's well. The pumping of these wells invalidated any data collected by the DWR during the investigation and resulted in dismissal of the impairment investigation triggered by Suburban.⁹⁵ In notifying Suburban that the impairment investigation was being dismissed, the DWR advised Suburban that dismissal "did not restrict or any way preclude" Suburban from filing a future complaint if Suburban believed its prior right to the use of water was being impaired by junior users. In response to Staff's inquiry, Suburban stated it has not filed another complaint against RWD No. 7 because data previously collected was rendered invalid and Suburban is currently discussing possible water supply options with RWD No. 7. Staff was puzzled by this response and could not recommend whether Suburban should pursue reopening an impairment claim or continue its efforts to secure another groundwater supply option with RWD No. 7.⁹⁶

48. Grady reviewed correspondence by DWR regarding wells Suburban drilled at or near the location of its application for water rights that reflected concern the pumping rates requested by Suburban were not possible. Upon Suburban's request, DWR dismissed Suburban's application for water rights. Suburban explained this decision was made because, at the time, Suburban did not have legal access to the land with the proposed sites.⁹⁷ Suburban presented no discussion of any effort on its part to gain access to these water rights through an implied easement or other legal remedy.⁹⁸ Also, DWR denied an application by Suburban to secure additional groundwater in the aquifer feeding the Moran field because minimum spacing requirements between domestic wells was not met.⁹⁹

49. Staff issued discovery regarding Breuer's proposal to study the likelihood of success if Suburban applied to acquire additional groundwater sources. Staff reviewed the

⁹⁵ Grady Direct, pp 19-22.

⁹⁶ Grady Direct, pp 22-26.

⁹⁷ Grady Direct, pp. 34-36.

⁹⁸ *Sebree v. Board of Shawnee County Comm'rs*, 251 Kan. 776, 840 P.2d 1125 (1992).

⁹⁹ Grady Direct, pp. 36-38.

variables affecting the calculations, assumptions, and results impacting the economics of developing ground water versus purchasing wholesale water from BPU. Having reviewed these variables, Staff concluded that if more than 40,000,000 gallons a year could be pumped, it was more cost effective for Suburban to pump its water rather than buying wholesale water from BPU.¹⁰⁰ Staff did not recommend Suburban pursue a groundwater study during this proceeding, noting the small size of its customer base should be considered before committing significant resources on a study that has no guarantee of success. Before ordering Suburban to undertake such a study, Grady suggested the Commission might want a hydrological expert with experience in this area to gather more information upon which to decide whether to order a study.¹⁰¹

50. Finally, Grady considered whether surface water was an option for Suburban to secure a long-term water supply for its customers. Without citing support, Suburban claimed it would be too expensive for such a small water company to build a surface water treatment plant, water diversion works, and a distribution system.¹⁰² Grady also concluded surface water was not a viable option for a small utility like Suburban because the utility would need to construct a pipeline or other delivery device to transport the water. If Suburban constructed a pipeline to the Kansas River, major treatment expenditures would still be needed to treat that water. In light of the cost estimate for a 1 Million gallon per day surface water treatment facility, Grady concluded it would not be economical for a small utility like Suburban to pursue surface water collection and treatment as opposed to buying water from a wholesale supplier or pumping groundwater.¹⁰³

51. Suburban did not discuss ground water supply issues in Direct Testimony. In response to Staff's testimony, Suburban Witness Wilson noted Grady described the problems Suburban faces in developing existing and new water well fields as a result of declining water tables and limited production capability. Wilson noted that, to determine whether a groundwater water supply existed, Suburban would need to expend already scarce resources to perform

¹⁰⁰ Grady Direct, pp 38-41.

¹⁰¹ Grady Direct, pp 41-42.

¹⁰² Wilson Response, p. 2.

¹⁰³ Grady Direct, pp 43-44.

complex hydrological studies with no guarantee of finding an adequate groundwater water supply for which it would be allowed water rights. Wilson asserted the contract with BPU for wholesale water purchase continues to be Suburban's least-cost option as well as its most economical option among the available wholesale suppliers that have been identified. Wilson further stressed that building a surface water treatment plant, water diversion works, and connection to a distribution system was not economical for a small water utility serving approximately 1,500 customers.¹⁰⁴

52. The Commission is still concerned that Suburban is relying solely upon the BPU as its long-term water source for its customers. Without the benefit of a long-term contract, Suburban's increasing dependence upon the BPU for wholesale water places its customers at risk for the many reasons discussed in this Order. Evidence presented by Staff has examined whether Suburban should explore further the possibility of acquiring additional groundwater supply. Another possibility would be for Suburban to aggressively develop a relationship with another wholesale water supplier. In its November 3, 2010 Order, the Commission stressed its concern that Suburban should develop a long-term plan to assure a future water supply to serve its customers.¹⁰⁵ Suburban, not the Commission, has this responsibility. But in responding to the Commission's questions about long-term planning, Suburban argued the right decision was made in 2000 when Suburban entered into its Water Supply contract with the BPU. Suburban's argument misses the point. The 20-year Water Contract with BPU is well over half over. Suburban needs to plan for the future. If Suburban wants to continue serving its customers beyond 2020, an alternative long-term water supply needs to be developed. Before the Commission will approve any additional increase in rates to cover the cost of water purchased from BPU, Suburban must establish that a plan has been undertaken to ensure a long-term water supply for its customers either that provides an alternative to the Water Contract with BPU for purchase of wholesale water or resolves the many problems with the existing Water Contract with BPU.

¹⁰⁴ Wilson Responsive Testimony, p. 2, *citing* Grady Direct, p. 8.

¹⁰⁵ November 3, 2010 Order, ¶¶ 14-15.

F. Due to misleading representations by Suburban's management, this Commission must examine Suburban's ability to fulfill obligations under its Certificate of Convenience.

53. The Commission is disturbed by evidence in the record showing that Suburban mislead the Commission and its Staff about the utility's efforts to secure additional groundwater water supply to serve its customers, appropriated water illegally through unpermitted wells, and committed perjury in its dealings with the DWR. As Grady discussed, Suburban did not disclose to Staff that DWR's investigation into impairment of Suburban's water rights by RWD No. 7's well in the Moran field was ended because Suburban drilled two unpermitted wells in the field. Staff only learned that Suburban had operated two illegal wells through discussions with the DWR, not from Suburban.¹⁰⁶

54. A public utility is not allowed to transact business in this state until it has been issued a certificate based upon the Commission finding that public convenience will be promoted by transaction of the business and permitting the applicant to transact that business. K.S.A. 66-131. An applicant for a certificate must show that public convenience and necessity will be promoted by authorizing its facilities as envisioned in the application. To promote public convenience and necessity, the applicant must show evidence of its ability to provide effective management. Public convenience refers to the convenience of the public, not the convenience of particular individuals. Public necessity does not necessarily mean a showing must be made of absolute need, but instead means a public need without which the public is inconvenienced to the extent of being handicapped.¹⁰⁷ The Supreme Court has noted that, in determining whether to grant a certificate of convenience, the Commission's primary concern should be the public convenience and its secondary concern the interest of public utility companies already serving the territory; the desires and solicitations of the applicant should be a relatively minor consideration of the Commission.¹⁰⁸ Suburban has been permitted to transact business of a miscellaneous

¹⁰⁶ Grady Direct, pp 21-22.

¹⁰⁷ *Central Kansas Power Co. v. State Corporation Commission*, 206 Kan. 670, 676, 482 P.2d 1 (1971).

¹⁰⁸ 206 Kan. at 677.

public utility.¹⁰⁹ The Commission has plenary authority to supervise and control all miscellaneous public utilities doing business in Kansas and is empowered to do all things necessary and convenient for the exercise of such power, authority and jurisdiction.¹¹⁰

55. The Commission is troubled by Suburban's lack of candor in dealing with the Commission and its Staff. Although Suburban is a small company, a utility regardless of its size has the responsibility to submit information needed to evaluate its Application and must provide information otherwise requested by the Commission and its Staff. Furthermore, a witness submitting prefiled testimony before this agency cannot be allowed to file deceiving or misleading testimony under oath, particularly when that witness is an officer of a public utility. Although the Commission has no desire to manage this utility, the Commission has authority to investigate the operations of a company to determine if that utility is able to provide the services for which it is certificated. In this Order, the Commission has again set forth many concerns regarding the long-term water supply for customers of this utility and provisions in the Water Contract with BPU. Those issues must be addressed in this company's next rate case to ensure that Suburban's management is both serious about its intent to continue serving its customers and capable and competent to do so.

56. CURB has questioned whether Suburban should be allowed to recover the entire amount of rate case expense requested in its Application. CURB Witness Harden has suggested the Commission has caused increased rate case expense by rejecting Suburban's proposed Purchase Water Adjustments. Harden argued against the Commission assessing Suburban's ratepayers with additional costs for this rate case.¹¹¹

57. The Commission notes that Suburban incurs rate case expense from two sources. First, Suburban incurs expenses in filing a rate case, including attorney fees, consultant fees if one is hired, and miscellaneous incidental expenses for pursuing the docket, such as notifying Suburban's customers of its meeting and conducting the meeting. Second, Suburban is assessed

¹⁰⁹ K.S.A. 66-1,230.

¹¹⁰ K.S.A. 66-1,231.

¹¹¹ Harden Direct, pp 22-26.

for expenses incurred by the Commission's Staff and CURB. Regarding the assessment by the Commission, a review of assessments in Docket 10-602 shows that Suburban has already been billed the entire amount it is allowed to be assessed by statute during this fiscal year.¹¹² As a result, Suburban will not be billed more for rate case expense by the Commission and CURB during FY 2011. However, K.S.A. 66-1502 provides: "The commission may render bills in one fiscal year for costs incurred within a previous fiscal year." The Commission concludes it is appropriate to consider assessing Suburban for expenses incurred for Staff and CURB to investigate and pursue this docket during a later fiscal year.

58. Generally, prudently incurred rate case expenses are among the reasonably necessary expenses a public utility is entitled to recover in a rate case proceeding, but, as with all expenses, the utility has the burden to establish rate case expense is reasonable and prudent.¹¹³ The Commission has made clear its concern about management of this utility and the misleading testimony filed in this docket. Additional work was required by Staff and CURB due to the conduct of Suburban's management. Suburban's lack of candor in Breuer's testimony lead the Commission's Staff to incur many hours of work sorting out the truth about why Suburban's Application for water rights was denied, which increased costs needed to investigate this Application. Rather than requiring Suburban's customers to pay this rate case expense, the Commission believes Suburban's shareholders should be responsible for rate case expenses cause by misdeeds of its management. The Commission notes that, in the Letter, parties agreed that rate case expense for this proceeding would be minimized to the fullest extent possible. Due to Suburban's action, minimal rate case expense was not possible. The letter also states that Suburban plans to recover in its third rate case, to be filed late in 2012, the cost of filing the rate case. The Commission concludes a decision regarding how much rate case expense should be allowed to be recovered from Suburban's customers and how much rate case expense should be borne by Suburban's shareholders from this series of rate cases will best be resolved in the third

¹¹² K.S.A. 66-1502.

¹¹³ *Kansas Industrial Consumers*, 36 Kan. App. 2d at 111.

rate case to be filed in FY 2013. Therefore, the Commission will decide the issue of rate case expense in that proceeding.

IT IS, THEREFORE, BY THE COMMISSION ORDERED THAT:

(A) The Commission grants Suburban's request for a rate increase of \$44,913.00 but this increase is subject to true-up or refund until issues articulated in this Order are resolved in subsequent rate case proceedings, as discussed in this Order. Suburban's next rate case proceeding shall be a full rate case under K.A.R. 82-1-231 and will be filed during FY 2012.

(B) Before the Commission will approve any additional increase in rates to cover the cost of water purchased from BPU, Suburban must establish a plan has been undertaken to ensure a long-term water supply for its customers either that provides an alternative to the Water Contract with BPU for purchase of wholesale water or that resolves the many problems with the existing Water Contract with BPU, as discussed in this Order.

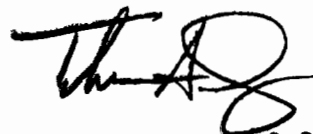
(C) This Order will be served using electronic service without follow-up hard copy as agreed to by the parties. Parties have fifteen days, plus three days if service of this Order is by mail, from the date of service of this Order in which to petition the Commission for reconsideration of any matter decided herein. K.S.A. 66-118b; K.S.A. 2010 Supp. 77-529(a)(1).

(D) The Commission retains jurisdiction over the subject matter and parties for the purpose of entering such further order or orders as it may deem necessary.

BY THE COMMISSION IT IS SO ORDERED.

Sievers, Chmn (not participating); Loyd, Com.; Wright, Com.

Dated: JUN 03 2011



ORDER MAILED JUN 03 2011

Executive Director

mjc

CERTIFICATE OF SERVICE

JUN 03 2011

11-SUBW-448-RTS

I, the undersigned, hereby certify that a true and correct copy of the above and foregoing Order on Application was served by electronic mail this 3rd day of June, 2011, to the following parties who have waived receipt of follow-up hard copies:

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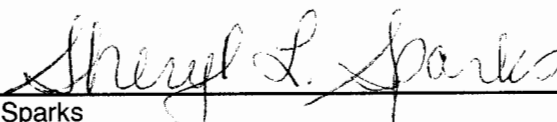
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ORDER MAILED JUN 03 2011