

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

INVESTIGATION INTO THE PROPOSED WATER)
PURCHASE AGREEMENT BETWEEN) CASE NO. 2013-00251
LOUISVILLE WATER COMPANY AND HARDIN)
COUNTY WATER DISTRICT NO. 1)

ORDER

On June 13, 2012, Hardin County Water District No. 1 (“Hardin District No. 1”) filed through the Commission’s Tariff Filing System a copy of a contract between Louisville Water Company (“Louisville Water”) and Hardin District No. 1 dated May 15, 2012 (“Contract”). Under the terms of the Contract, Louisville Water will supply up to 3.5 million gallons of water per day to Hardin District No. 1. Hardin District No. 1 agrees to pay Louisville Water’s standard wholesale water rate and a monthly service charge. The terms of the Contract further require that any water supplied by Hardin District No. 1 to Fort Knox must come exclusively from water supplied by Louisville Water. Hardin District No. 1 cannot replace its supply of water to Fort Knox without Louisville Water’s approval. The initial term of the Contract is 40 years.

The Contract also includes a \$4.5 million construction project for a 16-inch finished water transmission main, a master meter, a pump station, and related facilities to be designed and constructed along Dixie Highway from Louisville Water’s existing main at Kathryn Station Road to Hardin District No. 1’s existing main at the base of Muldraugh Hill. Hardin District No. 1 will fund the project with proceeds from a \$4.5

million Kentucky Cabinet for Economic Development grant. Hardin District No. 1 is required to file an application for a certificate of public convenience and necessity for the proposed project pursuant to KRS 278.020(1). In an Order issued December 23, 1998, in Case No. 98-339,¹ the Commission held that a contract similar to the one at hand cannot be viewed in isolation without the companion certificate application.

In Administrative Case No. 351,² the Commission held that municipal utilities were responsible for filing with the Commission any contracts for the provision of wholesale utility service to a public utility. In the current case, Hardin District No. 1, not Louisville Water, the supplier, filed the Contract.

The Contract contains a System Development Charge (“SDC”), which is a one-time fee charged at the time a construction project begins. The SDC increases as the customers’ meter size increases. The parties have not filed an application to assess a system development charge. An application is required pursuant to 807 KAR 5:090.

The Commission initiated this proceeding on July 3, 2013, to investigate the reasonableness and lawfulness of the Contract and to determine whether the Contract was an evidence of indebtedness under KRS 278.300 requiring Commission approval prior to execution of the Contract. Pursuant to the Commission’s July 3, 2013 Order, on August 19, 2013, Louisville Water filed a memorandum regarding the applicability of KRS 278.300 to the Contract. On August 21, 2013, Hardin District No. 1 filed its memorandum regarding the applicability of KRS 278.300.

¹ Case No. 98-339, *Kentucky-American Water Company Special Contract with Louisville Water Company* (Ky. PSC Dec. 23, 1998).

² Administrative Case No. 351, *Submission of Contracts and Rates of Municipal Utilities Providing Wholesale Utility Service to Public Utilities* (Ky. PSC Aug. 10, 1994).

Louisville Water and Hardin District No. 1 both argue that the Commission incorrectly assumed that Hardin District No. 1 is currently the sole supplier of water to Fort Knox. The parties acknowledge that the Contract could be interpreted to imply that Hardin District No. 1 is solely responsible for supplying water to Fort Knox. The Department of Defense is currently solely responsible for obtaining Fort Knox's water supply. A contract currently exists in which Hardin District No. 1 operates the Fort Knox water system, but is not responsible for providing a water supply. In the future, Hardin District No. 1 may enter into an agreement to provide water to Fort Knox.³

Louisville Water argues that the monthly service charge cannot be considered an evidence of indebtedness because nothing has been issued and no debt is being assumed.⁴ Hardin District No. 1 argues that 807 KAR 5:001, Section 17,⁵ *Application for Authority to issue Securities, Notes, Bonds, Stocks, or Other Evidences of Indebtedness*, "distinguishes between applications to issue notes, bonds or other evidences of indebtedness, as opposed to bilateral contracts."⁶

The Commission thoroughly reviewed the various sections of KRS 278.300 to determine whether a contract with a minimum purchase clause is an evidence of indebtedness.

KRS 278.300(1) states:

No utility shall *issue* any securities or evidences of indebtedness, or assume any obligation or liability in respect

³ Louisville Water's Aug. 19, 2013 Brief at 2-3; Hardin District No. 1's Aug. 21, 2013 Brief at 4-5.

⁴ Louisville Water's Aug. 19, 2013 Brief at 4-11.

⁵ An amendment to 807 KAR 5:001 was effective January 3, 2014. Section 17 is now Section 18. The amendment to the current Section 18 does not affect Hardin District No. 1's argument.

⁶ Hardin District No. 1's Aug. 21, 2013 Brief at 3.

to the securities or evidences of indebtedness of any other person until it has been authorized so to do by order of the commission.” (Emphasis added.)

Other sections of KRS 278.300 use the term *issue*. KRS 278.300(2) says, “Application for authority to *issue*” KRS 278.300(3) says, “The commission shall not approve any *issue*” KRS 278.300(6) says, “Securities and evidences of indebtedness *issued*” KRS 278.300(7) says, “The commission may require periodical or special reports from the utility *issuing*” KRS 278.300(8) says, “This section does not apply to notes *issued*” KRS 278.300(9) says, “Nothing in this section limits the power of any court having jurisdiction to authorize or cause receiver’s certification or debenture to be *issued*” KRS 278.300(10) says, “This section does not apply in any instance where the *issuance*” KRS 278.300(11) says, “This section also does not apply to the *issuance*”

KRS Chapter 278 does not define the term “*issue*.” Entering into a contract to purchase water or any other product is not generally considered an issuance by either the seller or purchaser. Black’s Law Dictionary contains several definitions for the term *issue*, including “[a] class or series of securities that are simultaneously offered for sale” and “[t]o send out or distribute officially.” Under commercial law, *issue* is defined as “[t]he first delivery of a negotiable instrument by its maker or holder.”⁷ None of the definitions indicate that an *issuance* occurs when parties enter into a contract for the purchase of a product not involving a document of title. The Contract at hand involves the supply and purchase of water, not the issuance of securities or delivery of a negotiable instrument.

⁷ Black’s Law Dictionary 907-908 (9th Ed. 2009).

As listed in KRS 278.300, an evidence of indebtedness means something different from a security. If evidence of indebtedness and security were synonymous, only one of the terms would be necessary. Because both terms are used, the terms cannot be synonymous; however, the term *issue* refers to both evidence of indebtedness and security. The term *issue* cannot mean one thing for the term *security* and something else for the term *evidence of indebtedness*.

Both the term *security* and *evidence of indebtedness* involve some form of financing arrangement. That both terms involve some form of financing arrangement is evident in KRS 278.300(3), which states:

The commission shall not approve any issue or assumption unless, after investigation of the purposes and uses of the proposed issue and the *proceeds* thereof, or of the proposed assumption of obligation or liability, the commission finds that the issue or assumption is for some lawful object within the corporate purposes of the utility, is necessary or appropriate for or consistent with the proper performance by the utility of its service to the public and will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose. (Emphasis added.)

Generally, a contract to purchase a product would not result in *proceeds*. Black's Law Dictionary defines *proceeds* as:

1. The value of land, goods, or investments when converted into money; the amount of money received from a sale <the proceeds are subject to attachment>. 2. Something received upon selling, exchanging, collecting, or otherwise disposing of collateral. UCC § 9–102(a)(67). • Proceeds differ from other types of collateral because they constitute any collateral that has changed in form. For example, if a farmer borrows money and gives the creditor a security interest in the harvest, the harvested wheat is collateral. If the farmer then exchanges the harvest for a tractor, the tractor becomes the proceeds of the wheat.⁸

⁸ Black's Law Dictionary 1325 (9th Ed. 2009).

While the term “proceeds” does not necessarily mean only cash or money, the term “*proceeds*” does not apply to a contract containing a minimum purchase clause for the purchase of water. Louisville Water and Hardin District No. 1 are not selling property or converting money into other property.

KRS 278.300(7) also implies that a contract with a minimum purchase clause is not an evidence of indebtedness.

The commission may require periodical or special reports from the utility issuing any security or evidence of indebtedness. The report shall show, in such detail as the commission requires, the disposition made of such securities or evidences of indebtedness, and the application of the proceeds thereof.

The term “*proceeds*” is again used. As already stated, the term “*proceeds*” does not apply to a contract containing a minimum purchase clause for the purchase of water.

Having considered Louisville Water’s and Hardin District No. 1’s briefs and the Contract, and having carefully reviewed the language set forth in KRS 278.300, the Commission finds that:

1. All contracts and amendments to contracts for the sale for resale of water by a city-owned utility to a Commission-regulated water utility are subject to the Commission’s jurisdiction pursuant to KRS 278.200 and are required to be filed with the Commission.

2. Any minimum purchase requirements or minimum service charges for the sale for resale of water in a contract by a city-owned utility to a Commission-regulated water utility may be investigated for reasonableness at the time of filing or upon complaint.

3. All rates, terms, and conditions for the sale of water by a Commission-regulated utility to another Commission-regulated utility are subject to the Commission's jurisdiction pursuant to KRS 278.030 and 278.040.

4. Any minimum purchase requirements or minimum service charges for the sale of water by a Commission-regulated utility to another Commission-regulated utility may be investigated for reasonableness at the time of filing or upon complaint.

5. Contracts, amendments to contracts, or tariffs containing minimum purchase requirements or minimum service charges for the sale or purchase of water should not be considered evidences of indebtedness.

6. No water utility may impose an SDC until an application has been filed as required by 807 KAR 5:090 and approval has been granted by the Commission.

7. Hardin District No. 1 must apply for and be granted a Certificate of Public Convenience and Necessity prior to commencing construction along Dixie Highway of a \$4.5 million water project to connect its main to Louisville Water's main.

8. Except for the provision of an SDC, all other provisions of the contract dated May 15, 2012 between Louisville Water and Hardin District No. 1 should be approved contingent on Hardin District No. 1's submission of an application for a Certificate of Public Convenience and Necessity and the Commission's granting of the Certificate of Public Convenience and Necessity.

IT IS THEREFORE ORDERED that:

1. Contracts and amendments to contracts for the sale for resale of water by a city-owned utility to a Commission-regulated water utility shall be filed by the seller with the Commission pursuant to KRS 278.200, but the Commission-regulated water

utility need not obtain approval as an evidence of indebtedness under KRS 278.300 of any minimum purchase requirement in such a contract or amendment.

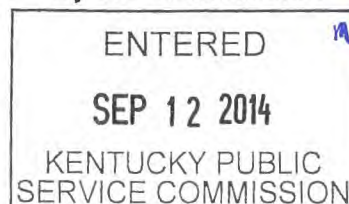
2. In the future, when Hardin District No 1 enters into a contract with a city-owned water utility that requires Hardin District No. 1 to apply for a Certificate of Public Convenience and Necessity, Hardin District No. 1 shall file with the Commission the contract for approval along with the application for a Certificate of Public Convenience and Necessity.

3. Except for the provision of an SDC, all other provisions of the contract dated May 15, 2012 between Louisville Water and Hardin District No. 1 are approved contingent on Hardin District No. 1's filing of an application for a Certificate of Public Convenience and Necessity and the Commission's granting of the Certificate of Public Convenience and Necessity.

4. Any request to impose an SDC shall be filed in an application as required by 807 KAR 5:090 and shall be charged only after approval by the Commission.

5. Hardin District No. 1 shall file an application for a Certificate of Public Convenience and Necessity prior to commencing construction along Dixie Highway of a \$4.5 million water project to connect its main to Louisville Water's main.

By the Commission



ATTEST:



Executive Director

Jim Bruce
General Manager
Hardin County Water District #1
1400 Rogersville Road
Radcliff, KY 40159-0489

Edward T Depp
Dinsmore & Shohl, LLP
101 South Fifth Street
Suite 2500
Louisville, KENTUCKY 40202

Barbara K Dickens
Louisville Water Company
550 S. Third Street
Louisville, KY 40202

Honorable David T Wilson II
Attorney at Law
Skeeters, Bennett, Wilson & Pike
550 West Lincoln Trail Boulevard
P.O. Box 610
Radcliff, KENTUCKY 40160