

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

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IN THE MATTER OF:)
)
INVESTIGATION INTO THE PROPOSED)
WATER PURCHASE AGREEMENT BETWEEN)
LOUISVILLE WATER COMPANY AND)
HARDIN COUNTY WATER DISTRICT NO. 1)
)

CASE NO. 2013-00251 PUBLIC SERVICE COMMISSION

HARDIN COUNTY WATER DISTRICT #1's RESPONSE TO THE PUBLIC SERVICE COMMISSION'S ORDER DATED JULY 3, 2013

Comes Hardin County Water District #1 ("HCWD1") and in response to the Commission's Order entered July 3, 2013, submits the following Memorandum:

At issue is whether the Water Purchase Agreement ("Agreement") entered into between HCWD1 and the Louisville Water Company ("LWC") constitutes the issuance of "securities or evidence of indebtedness". KRS 278.300(1) If the Agreement does constitute a "security" or "evidence of indebtedness", then authorization of the Kentucky Public Service Commission ("Commission") is required. For the reasons more fully set forth herein, HCWD1 submits that the Agreement does not equate to the issuance of "securities" or "evidence of indebtedness" and therefore KRS 278.300(1) is not applicable.

The Agreement sets forth an arrangement whereby both parties agree to construct water mains in order to permit an interconnect at the Salt River near West Point in Hardin County, Kentucky. This interconnect will afford HCWD1 a redundant water supply. The cost of the water main is covered by a grant received by HCWD1 from the Kentucky Cabinet for Economic Development. The Agreement imposes upon LWC the obligation to provide a minimum quantity of water at specified quality and pressure standards. The Agreement further imposes upon LWC

the obligation to maintain and test master meter(s) at the point of service. The Agreement entitles HCWD1 to purchase water at applicable rates and further obligates it to pay meter charges to LWC at its then current rate based upon meter size. Furthermore, HCWD1 is obligated to pay system development charges in effect at the time the construction of the project begins.

The Agreement is for 40 years and imposes upon both HCWD1 and LWC ongoing obligations and, further, allows for the termination of the Agreement by either party in the event the Agreement is breached. In short, the Agreement constitutes a bilateral contract consisting of mutual promises made by both HCWD1 and LWC. See, *Combs vs. International Insurance Company*, 354 Fed.3d 568 (6th Cir., 2004).

The undersigned would respectfully submit that it requires an exceedingly strained interpretation of KRS 278.300(1) to reach the conclusion that the Agreement is the equivalent of a “security” or “evidence of indebtedness”.¹ HCWD1 would point the Commission to the 1950 decision of *Preston v. Clemons*, 232 SW2d 85, 90 (Ky.1950), wherein Kentucky’s high court held that a debt in the constitutional sense arises out of a contract wherein the creditor is unconditionally obligated to receive and the debtor is obligated to pay. Applying that definition to the agreement at hand, HCWD #1 would submit that the Agreement does not create a debt, as HCWD1 is not unconditionally obligated to pay. If the agreement does not create a debt, then the agreement is not “evidence of an indebtedness”. If the agreement is not evidence of indebtedness, then KRS 278.300(1) is not applicable.

HCWD1 would also direct the Commission’s attention to the case of *City of Russell v. City of Flatwoods*, Ky.394 SW2d 900 (Ky. 1965). This opinion involves the cities of Flatwoods

¹ Note that pursuant to KRS 292.310(19) the terms are interchangeable. That is to say security is defined to include evidence of indebtedness.

and Russell located in Greenup County. Cities officials agreed upon a plan whereby Flatwoods would build necessary sewage treatment facilities and finance their construction by the sale of revenue bonds. The City of Russell would pay the City of Flatwoods over a period of twenty (20) years a monthly sum to be determined by the amount of Russell's sewage that was collected and treated by the Flatwoods' facilities. Flatwoods began construction, but Russell officials refused to honor and perform the contract that the City had entered into. On appeal Russell argued that the contract violated Section 159 of the Constitution of Kentucky. Kentucky's high court rejected said argument concluding that "this contention is without merit because, as we construe the contract it does not create an indebtedness".

Additionally, HCWD#1 submits that the statutory framework set forth at 807 KAR 5:001(17) clearly distinguishes between applications to issue notes, bonds or other evidence of indebtedness, as opposed to bilateral contracts. For instance, the aforementioned regulation obligates the utility to identify the amount of notes, bonds or other evidence of indebtedness which the utility desires to issue along with the terms and rate of interest. As with any traditional financing, it is apparent that 807 KAR 5:001(1)(b) is describing a financing arrangement wherein the borrower repays the sum borrowed over a specified time and at an applicable rate of interest. 807 KAR 5:001(17)(1)(c) requires the disclosure of the use to be made of the proceeds of the issuance of the securities, notes or bonds or other evidence of indebtedness. Again, this verbiage contemplates a traditional advance of credit, not a bilateral contract which is the subject of this Memorandum. 807 KAR 5:001 (17) (d) obligates the utility to described what is to be acquired, constructed or improved with the proceeds of the debt financing. No verbiage found within 807 KAR 5:001(17) can be reasonably construed to extend Commission authority to the Agreement entered into between LWC and HCWD#1.

Were the Commission to conclude that KRS 278.300(1) extends to the bilateral contract in question, such an interpretation would impose upon the Commission the obligation to approve such things as HCWD1's contract with its software supplier, landscape contractor and general manager. These are but a small example of contracts executed by HCWD1 which obligates it to pay the provider of services a sum certain over a period of time if, but only if, the provider of services performed its portion of the bilateral contract.

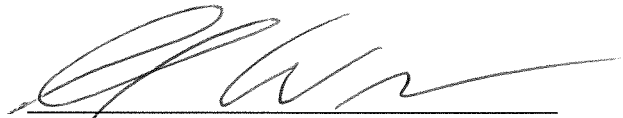
If the Commission were to conclude such contingent obligations are the equivalent of the issuance of "evidence of indebtedness", suffice to say HCWD1 and other similarly situated utilities have inadvertently issued a staggering amount of "evidence of indebtedness".

Stated differently, if General Manager Bruce abandons his position and retires to South America prior to the expiration of his contractual obligations, HCWD1 would no longer be obligated to pay his salary and benefits. Similarly, if LWC is unable or unwilling to meet its obligations to provide the quantity and quality of water required by the agreement with HCWD1, then HCWD1 is no longer obligated to pay the sum provided in the Agreement. The Agreement is a bilateral contract. It is not a "security" and it is not an "evidence of indebtedness". Rather, the Agreement imposes rights, duties and responsibilities upon both LWC and HCWD1. Accordingly, KRS 278.300(1) is not applicable to the Agreement.

Finally, it is noted that the introductory paragraph of the subject order contains the following sentence, "Pursuant to the terms of this Agreement, which has a term of 40 years, Hardin District will purchase its entire water requirements necessary to serve the Fort Knox Military Installation from Louisville Water Company and will pay a monthly service charge throughout the life of the Agreement". HCWD1 acknowledges that this is a logical inference based on Paragraph 6 of the Agreement which states as follows: "Further, HCWD1 will supply

Fort Knox exclusively with water from LWC and will not replace the supply of water to Fort Knox without the approval of LWC". This sentence is admittedly a bit confusing as it suggests that HCWD1 presently supplies water to Fort Knox when, in fact, it does not. HCWD1 has neither the legal right or obligation to supply water to Fort Knox. The intent of the above-quoted sentence found in Paragraph 6 of the Agreement is to reflect if in the future HCWD1 entered into an Agreement to provide Fort Knox with water, that source of water would come from LWC. The reason for this provision is that HCWD1 has no other available source sufficient to provide the water requirements of Fort Knox. However, the contract wherein HCWD1 agreed to operate the Fort Knox water system clearly delineates that HCWD1 is not responsible for providing a water supply, but rather for operating the system. The obligation to provide a water supply is solely the obligation of Fort Knox.

Respectfully Submitted,



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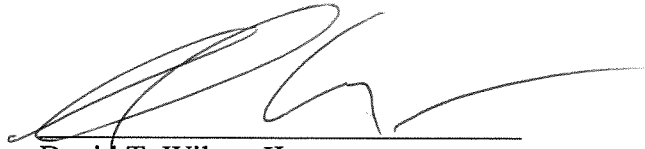
CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the foregoing has this 19 day of August,

2013 been mailed to:

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