

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

SOUTH SHORE WATER WORKS COMPANY)	
)	
COMPLAINANT)	
)	
V.)	CASE NO. 2009-00247
)	
CITY OF GREENUP, KENTUCKY)	
)	
DEFENDANT)	

O R D E R

South Shore Water Works Company ("South Shore") has filed a complaint against the city of Greenup, Kentucky ("Greenup") in which it alleges that Greenup has increased its rate for wholesale water service without prior Commission approval. In its answer, Greenup alleges that the Commission lacks jurisdiction over the matter. At issue is whether the absence of a written contract between a city and a public utility for wholesale water service deprives the Commission of jurisdiction over the rate that the city charges the public utility for such service. Finding in the affirmative, we dismiss the complaint for lack of subject matter jurisdiction.

STATEMENT OF THE CASE

South Shore, a corporation organized under KRS Chapter 271B, owns and operates facilities in the vicinity of South Shore, Kentucky that produce and distribute

water to approximately 2,282 customers for compensation.¹ It is a utility subject to Commission jurisdiction.²

Greenup is a city of the fifth class that owns and operates a water treatment and distribution system.³ It provides water service to approximately 3,123 customers in Greenup and in the unincorporated areas of Greenup County.⁴

South Shore currently obtains its water supply from a well field situated within Greenup County, Kentucky. Beginning in the late 1980s, South Shore began experiencing problems with the quality and quantity of water from this well field. Following a study of these problems, South Shore concluded that its best alternative was the purchase of water from Greenup. In 1998, it presented an application for water service to Greenup's City Council which the City Council accepted by resolution. In the following three years, South Shore and Greenup undertook actions to permit the interconnection of the two water systems and Greenup's provision of wholesale water service.

In November 2001, Greenup refused to accept South Shore's tendered deposit for service and advised South Shore of its intent not to provide wholesale water service. South Shore then filed a complaint against Greenup with the Commission in which it alleged that a contract between the two parties for water service existed.⁵ South Shore

¹ *Annual Report of South Shore Water Company, Inc. to the Public Service Commission for the Year Ended December 31, 2009* at 30.

² KRS 278.010(3)(c); KRS 278.040(1).

³ KRS 81.010(5).

⁴ See <http://wris.ky.gov/portal/DwSysData.aspx?PNum=KY0450169>.

⁵ Case No. 2002-00003, *The South Shore Water Works Company v. City of Greenup* (Ky. PSC filed Dec. 4, 2001).

requested that the Commission require Greenup to provide wholesale water service under reasonable terms. After a hearing in the matter, the Commission determined that a contract for wholesale water service had been created as a result of the Greenup City Council's resolution to accept South Shore's application, established the terms for wholesale water service, and directed Greenup to serve South Shore under those terms.

Greenup brought an action for review of the Commission's Order. While Franklin Circuit Court affirmed the Commission's Order, the Kentucky Court of Appeals in *City of Greenup, Ky. v. Public Service Commission*, 182 S.W.3d 535 (Ky. App. 2005) reversed. Noting that KRS 83A.130(8) allows only the mayor to execute a contract on behalf of a city, the Court of Appeals found that the Commission erred in concluding that the Greenup City Council's acceptance of South Shore's application created a contract and vacated the Commission's Order.

Despite the Court of Appeals decision, Greenup has continued to provide water service to South Shore. According to the amended complaint, Greenup has provided water to South Shore on several occasions since 2005 and has billed South Shore monthly for water service. On at least two occasions since 2005, Greenup has increased its monthly minimum bill for water service to South Shore.

PROCEDURE

On June 30, 2009, South Shore filed a complaint against Greenup with the Commission in which it alleged that Greenup had increased its minimum monthly charge for wholesale water service without Commission approval and was providing inadequate water service. The Commission directed Greenup to either satisfy or answer the complaint. Upon Greenup's motion and without objection, the Commission

extended Greenup's time to answer the complaint to permit the parties to negotiate a water supply agreement. On January 28, 2010, the parties advised the Commission that their negotiations had proven unsuccessful. On February 5, 2010, South Shore filed an amended complaint with the Commission to reflect its negotiations with Greenup since the filing of the initial complaint. Greenup answered this complaint on February 26, 2010.

On April 5, 2010, the Commission, on its own motion, directed the parties to submit memoranda on certain issues related to the Commission's jurisdiction over the complaint. Both parties timely submitted memoranda and reply memoranda on these issues. This matter now stands submitted for decision.

DISCUSSION

Kentucky courts have generally held that "all operations of a municipally owned utility whether within or without the territorial boundaries of the city" are exempt from Commission jurisdiction.⁶ The exception to this exemption occurs when a municipal utility contracts to provide utility service to a utility.⁷

In *City of Greenup*, the Kentucky Court of Appeals further refined the rights of a public utility obtaining wholesale utility service from a municipality when it found that a written contract between the city and public utility could only exist if all of the statutory provisions concerning the formation of a contract by a municipality had been met. In

⁶ *McClellan v. Louisville Water Co.*, 351 S.W.2d 197, 199 (Ky. 1961). See also *City of Mount Vernon v. Banks*, 380 S.W.2d 268, 270 (Ky. 1964) ("In the operation of a water plant a municipal corporation is not under the jurisdiction of the Public Service Commission").

⁷ *Simpson County Water District v. City of Franklin*, 872 S.W.2d 460, 463 (Ky. 1994) ("[W]here contracts have been executed between a utility and a city . . . KRS 278.200 is applicable and requires that by so contracting the City relinquishes the exemption and is rendered subject to PSC rates and service regulation").

City of Greenup, the Commission found that a contract had existed based upon Shore Shore's presentation of an application for utility service and a resolution of Greenup's City Council accepting the application. Reversing the Commission's Order, the Court of Appeals found that KRS 83A.130(8)⁸ permits only the mayor of a city to contract on behalf of a city. To the extent that Greenup's mayor had not executed any written agreement with South Shore for utility service, the Court of Appeals found that no contract existed. The Court of Appeals expressly rejected that a contract with a city could be made by the parties' conduct.⁹

In the present case, South Shore argues that the voluntary and periodic water supply transactions since 2005 are sufficient to create a contract. It notes that KRS 278.200,¹⁰ which the Kentucky Supreme Court found was the statutory basis for the

⁸ KRS 83A.130(8) provides:

All bonds, notes, contracts and written obligations of the city shall be made and executed by the mayor or his agent designated by executive order.

⁹ The Court stated:

The PSC's conclusion that a contract had been formed appears to have been based at least to some extent upon the conduct of the parties, which we construe as invoking the principles of contract by implication. However, it is well established that a municipality may not enter into a contract by implication.

City of Greenup at 540.

¹⁰ KRS 278.200 provides:

The commission may, under the provisions of this chapter, originate, establish, change, promulgate and enforce any rate or service standard of any utility that has been or may be fixed by any contract, franchise or agreement between the utility and any city, and all rights, privileges and obligations arising out of any such contract, franchise or agreement, regulating any such rate or service standard, shall be subject to the jurisdiction and supervision of the commission, but no such rate or service standard shall be changed, nor any contract, franchise or agreement affecting it abrogated or changed, until a hearing has been had before the commission in the manner prescribed in this chapter.

Commission's jurisdiction over municipal utilities, confers authority over any "contract, franchise, or agreement" of a city. It argues that an "agreement" is different from a contract and that, in this instance, an agreement between the parties as to wholesale water service exists as evidenced by their conduct since 2005. South Shore further attempts to distinguish the present case from *City of Greenup* by noting that, unlike the earlier case in which Greenup had not provided any water service to South Shore at the time of South Shore's complaint to the Commission, Greenup has, in the current case, been voluntarily providing service for five years.

Not surprisingly, Greenup argues that the present case is indistinguishable from the earlier case. It notes the lack of any written contract for utility service and the failure of South Shore to allege in its amended complaint the existence of such a contract. No contract, it further contends, can be created unless the statutory formalities are strictly observed. As to the assertion that Greenup's voluntary provision of service resulted in the formation of a contract, Greenup argues that the Court of Appeals expressly rejected this argument in its holding in *City of Greenup*.

Based upon our review of the facts and the existing legal precedent, we conclude that no contract presently exists. As in *City of Greenup*, there is no written contract between the parties. The only basis for finding the existence of a contract or agreement between the parties is the parties' conduct. The Court of Appeals expressly rejected such ground in *City of Greenup*. Kentucky courts have consistently held that all formalities of a contract must be met for a contract with a municipality to be created.¹¹ They have not been met in the present case.

¹¹ See, e.g., *City of Princeton v. Princeton Electric Light & Power Co.*, 166 Ky. 730, 179 S.W. 1074 (Ky. 1915).

The text of the *Greenup* decision does not support South Shore's attempt to distinguish an "agreement" from a "contract." Throughout its decision in *City of Greenup*, the Court of Appeals uses the terms "agreement" and "contract" interchangeably. Had the Court of Appeals viewed these words as distinctly separate and unique terms, it would not have used them synonymously.

Without the existence of a contract between Greenup and South Shore, the Commission has no jurisdiction over the rate that Greenup assesses. In the present case, the facts that South Shore alleges are insufficient to support the existence of a contract and thus are insufficient to confer jurisdiction over the complaint.

We recognize that our ruling today is not without perils. To disclaim jurisdiction may encourage municipalities to offer wholesale utility service without a written contract as a means of avoiding Commission jurisdiction and possibly imposing excessive rates upon wholesale customers that are public utilities. This scenario, however, is not very likely when the parties are considering a long-term contractual relationship. Few purchasers will enter into a long-term arrangement without a written contract. These purchasers will, at the start of their relationship with a supplier, have some leverage to insist upon a written contract. Furthermore, most municipal suppliers will also insist upon a long-term written contract to reduce the risk associated with any debt that they issue in conjunction with their municipal operations. Nonetheless, the potential for abuse may exist when a long-term contract expires and a wholesale customer is dependent upon its municipal supplier. In that instance, the supplier has considerable leverage and may have less incentive to renew an existing contract or negotiate a new contract. The remedy for such potential abuse lies exclusively with the General Assembly, not the Commission.

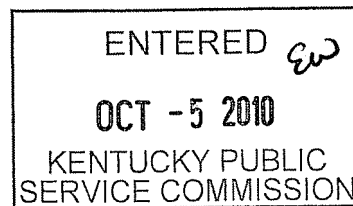
Notwithstanding these perils, the Commission has no choice but to comply with the holding of *City of Greenup* and dismiss the complaint for lack of subject matter jurisdiction.

SUMMARY

Finding that we lack subject matter jurisdiction over the complaint, the Commission, on its own motion, HEREBY ORDERS that:

1. South Shore's complaint is dismissed with prejudice.
2. This case is closed and removed from the Commission's docket.

By the Commission



ATTEST:


Executive Director

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