COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

Alleged Failure of the City of Danville to Comply with KRS 278.160 and 278.180 and the Commission's Order of August 10, 1994 in Administrative Case No. 351

Case No. 2008-00176

Response by the City of Danville

In its Order dated September 25, 2009, p.2, the Commission directs the parties to make filings "as to why Danville should or should not be subject to the penalties prescribed in KRS 278.990(1) for its alleged failure to comply with the provisions of KRS Chapter 278 and of the Commission's Order of August 10, 1994 in Administrative Case No. 351." However, the Commission also announces:

> In its review of the three settlement agreements (Danville and Parksville, Danville and Lake Village, and Danville and Garrard), the Commission finds that Danville should be subject to penalties prescribed by KRS 278.990(1) for its alleged failure to comply with KRS Chapter 278 and the Commission's Order of August 10, 1994 in Administrative Case No. 351, which has not yet been addressed in this action.

9/25/09 Order pp. 1-2. This finding is not explained or otherwise supported, and it is unclear as to the purpose of calling for the parties to make filings on the issue when the Commission has announced a finding that Danville should be fined.

The City of Danville ("Danville") has made previous filings in this proceeding as to why it is not or should not be subject to KRS 278.990(1) penalties. *See* City of Danville's Response to the Allegations filed July 18, 2008; Response to Parksville Water District's Data Request served January 12, 2009. It has sought clarification of the allegations against it, but to no avail. *See* City of Danville's Request for Informal Conference filed May 29, 2008; Proposed Agenda

filed July 18, 2008; Data Requests to the Commission served December 31, 2008; Notice re Non-Response filed January 22, 2009. Despite the lack of due notice, Danville has responded to all the data requests and formal requirements directed to it and has provided evidence showing the absence of a willful violation. Danville incorporates herein by reference all those prior filings.

1. Danville is not subject to KRS 278.990(1).

As an initial matter, Danville contends that the decision in *Simpson County Water District v. City of Franklin*, 872 S.W.2d 460 (Ky. 1994), was in error and should be overturned. Although the reversal, limitation, or modification of the decision is warranted by substantial, good-faith arguments, Danville understands that the Commission does not have the power to overturn or otherwise alter that decision. Danville here preserves the issue for any court review of decisions in this proceeding and, without waiver thereof, provides additional reasons for the inapplicability of KRS 278.990(1) and for not subjecting Danville to any penalty thereunder.

In general, the *Simpson* decision gives the Commission jurisdiction over wholesale contracts for a city to supply a KRS 278.010(3) utility. Danville has no reason to dispute the representation that each of Parksville, Lake Village, and Garrard is such a utility and admits that its contract with each of them is for Danville to supply the respective entity at wholesale. None of that, however, means that Danville is subject to fine under KRS 278.990(1).

KRS 278.990(1) provides for civil fines against utilities and those through whom utilities act (employees, agents, independent contractors, etc.). The element of a "utility" connection is made precise by specifying that "utility" is "as defined in KRS 278.010." KRS 278.990(1).[1]

[1] By contrast, subsection (6) and (7) of KRS 278.990 apply to any "company" (as to certain oil/gas from connecting lines) and "telephone company," respectively.

That definition expressly excepts cities. KRS 278.010(3).[2] In addition, nothing suggests that a state agency like the Commission may fine a municipality like Danville without explicit statutory authority to do so. The last sentence of KRS 278.990(1) — which deems the act, omission or failure, by an agent to be that of the utility — restates what has become commonplace as to nongovernmental entities but would represent a too-casual abrogation of the *ultra vires* doctrine as to a governmental entity.

2. There has been no violation or failure to obey.

Even if KRS 278.990(1) could be applicable to a city like Danville, it provides for a civil penalty only if there has been a violation of any of the provisions of KRS Ch. 278 or a regulation promulgated thereunder or a failure to obey an order of the Commission. The *Simpson* decision's construction of KRS 278.200 to give the Commission jurisdiction over wholesale contracts between a city and a utility does not subject a city to all of KRS Ch. 278 or the corresponding regulations. For example, there is no mandate that cities obtain a certificate to construct utility-type facilities (KRS 278.020(1)) or Commission approval to issue or assume any indebtedness (KRS 278.300(1)) or to sell assets or merge with another city or county (KRS 278.020(5), (6)). Since the *Simpson* decision, neither KRS 278.160 nor KRS 278.180 nor any other KRS Ch. 278 statute has been amended to refer to a city with a wholesale contract with a utility; similarly, no Commission regulation has been amended or promulgated to prescribe rules of general applicability with respect to such contracts.

Since the *Simpson* decision, the one order issued in a Commission proceeding of which Danville has had due notice and an opportunity to participate was the Order dated August 10, 1994, in Administrative Case No. 351 ("the Adm. 351 Order"). In the Adm. 351 Order (p.2), the Commission directed that Danville and other such cities "providing wholesale utility service

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[2] There is an implicit carve-out from this exception for city-owned or -controlled telephone operations. KRS 278.010(3) (omitting subsection (e) from the city exception).

to a public utility shall submit to the Commission a copy of its contract for such service and a schedule of its wholesale rates" conforming to 807 KAR 5:011. By the deadline specified, Danville fully complied, filing a tariff schedule and copies of its now-current contracts with Parksville and Lake Village. Each was stamped and returned to Danville as "effective" in October 1994. In addition, although not expressly required by the Adm. 351 Order, when Danville entered into a wholesale contract with Garrard, a copy of that contract was submitted to the Commision and expressly approved by it. *See* Order dated February 14, 2000, Case No. 99-353.

The Adm. 351 Order (p.2) had one forward-looking mandate, regarding a city's "placing into effect" or "wishing to change or revise" a contract with a public utility or the rates for wholesale service. Without reference to any statute or regulation, the Commission stated variously that the city "should file the revised contract or rate revision" or "shall ... file ... the revised contract and rate schedule" at least 30 days beforehand with the Commission. Adm. 351 Order (p.2). "Failure to make such filing will render the revision void." *Id.* This part of the Adm. 351 Order does not support assessing a penalty against Danville.

First, this mandate is a statement of general applicability, policy, or procedure that implements, interprets or prescribes law or policy and thus is required to be duly promulgated as an administrative regulation. KRS 13A.100. Inclusion in an Order, even one in a proceeding labeled as "Administrative" is not sufficient. Second, the sanction expressly stated by the Commission for failing to follow the mandate is that the revision/change would be void -- not that the city could be subject to civil penalties. The sanction stated fits the *Simpson*-declared authority, which arises from and is over a contract. Avoidance operates on the contract itself, and is not contrary to the general policy against punitive sanctions for contract violations. *Cf.*

KRS 411.184(4) ("In no case shall punitive damages be awarded for breach of contract."). KRS 278.990 nowhere permits assessment of a civil penalty based on a contract breach or arising out of a contract dispute involving a utility.

Third, the mandate does not apply to the subject purchasing-power adjustments. These were not something placed in effect or wished unilaterally by Danville, but were agreed upon by both parties in the contracts submitted to, and approved by, the Commission. No revision or change was necessary to bring the adjustments within a contract, and no party has taken the position or provided evidence that the adjustments were in breach of those contracts.

The Commission may point to the language in the Adm. 351 Order and claim that the adjustments were — regardless of their permissibility under the contracts — changes in rates requiring a prior filing. Such an argument, however, would ignore the distinction made in the Adm. 351 Order between cities' contracts and their rate schedules (or tariffs). "A schedule of ... rates" for each city is treated distinctively from its contracts with particular utilities, *id.* p.2,[3] and the language regarding changes/revisions to contracts or to rates must be similarly construed in the disjunctive. The Commission itself has treated the rates in Danville's filed schedule as distinct from the agreements as to rates in the filed contracts. In Case No. 99-353, the Commission approved Danville's contract with Garrard even though the initial rates set out therein were different from those in the filed schedule. Neither in the Adm. 351 Order, nor in 2000, nor at any time since, has the Commission ever suggested that the tariff schedule and the contracts were anything other than separate and independent of each other.

[3] The function of the tariff is particularly unclear, given the existence of contracts with each utility customer and no general obligation or offer to serve anyone under the tariff.

3. There has been no willful violation or failure.

Even if KRS 278.990(1) could be applicable and there were some violation or failure, a civil penalty still would not be supported. Subsection (1) prefaces the list of acts for which a fine may be assessed with the requirement that the acts be "willful." This comports with the principle that punishment is appropriate only if misconduct is deliberate. All the evidence here is that the purchase power adjustments began and were continued inadvertently. Furthermore, since Parksville brought the adjustments to Danville's attention, Danville has explained its authority to make the adjustments and asserted good-faith defenses to Parksville's complaint and the Commission's allegations. In addition, when the Commission issued a (somewhat ambiguous) order about restoring the contract rates, Danville took immediate steps to go back to charging the pre-adjustment rates even though it had good-faith doubts about the Commission's authority to order such a change in rates. *See* Hearing Transcript page ("Tr.") 119 (Stansbury); City of Danville's Request for Informal Conference filed May 29, 2008; City of Danville's Response to the Allegations filed July 18, 2008.

Witnesses showed that the adjustments were not taken in knowing disregard or defiance of Commission mandates. City Manager Stansbury testified to his understanding that, by ordinance, Danville had the authority to make annual adjustments to the wholesale rates charged to the three utilities without further filings with the Commission. Tr. 118-19; *see* Ordinance No. 1536 (eff. 9/23/97). Parksville's witness also noted that, when Parksville complained about the adjustment, Danville personnel explained that it was automatic and that they didn't believe they had to give notice. Tr. 179 (Feather). No evidence was presented or claim made that Danville attempted to hide the adjustments or the underlying ordinance from the utilities or the PSC.

Danville City Engineer Coffey testified that he was not aware of an increase in the wholesale rates to Parksville until late 2007 (Tr. 149). His investigation led to a conclusion that the adjustment was initially a rate clerk error (Tr. 151). No instruction had been given or conscious decision made to adjust wholesale customers' rates (Tr. 154-55; 157-58); however, once the adjustment was made in 2005, the wholesale rates were on a track to be adjusted in each subsequent year (Tr. 159-60). He did not know why the adjustment was not made to the utilities' wholesale rates before 2005 (Tr. 162), or if that was a conscious decision (Tr.163).

4. Fining Danville would violate substantive and procedural due process principles.

Assuming *arguendo* that there was otherwise statutory and evidentiary support for a KRS 278.990(1) fine against Danville, no civil penalty can be assessed consistent with due process. First, the Adm. 351 Order does not set out the requirements imposed on Danville with sufficient clarity to inform it that making adjustments expressly agreed-to in its contracts with the utilities could subject it to penalties. Second, Danville was not accorded due notice of the alleged violations that would give it an adequate opportunity to defend itself. This procedural problem was exacerbated by the failure of the Commission, Lake Village, and Garrard to respond to Danville's timely data requests[4] — which denied Danville evidence and other information with which to defend itself.

WHEREFORE, Danville submits that it should not be subject to the penalties prescribed in KRS 278.990(1)

[4] Lake Village gathered responsive information but chose not to submit it to Danville. Tr. 195 (Sanford).

Respectfully submitted,

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CERTIFICATE OF FILING AND SERVICE

I hereby certify that on this the 5th day of October, 2009, the original and ten (10) copies of this Notice were hand delivered for filing with the Commission, and a copy was sent by first-class U.S. mail for service on:

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