

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

PROPOSED ADJUSTMENT OF THE WHOLESAL E)
WATER SERVICE RATES OF THE CITY OF) CASE NO. 99-300
CYNTHIANA, KENTUCKY)

ORDER

The city of Cynthiana, Kentucky (“Cynthiana”) has moved for partial reconsideration of the Commission’s Order of April 24, 2000. Its motion poses the following issue: May the Commission give retroactive effect to a rate for wholesale water service when the municipal water supplier and public utility agree to the rate’s retroactive application? Finding in the negative, we deny the motion.

On April 24, 2000, the Commission entered an Order approving with certain modifications a settlement agreement between Cynthiana and Harrison County Water Association (“HCWA”). Among the modifications which we made to this agreement was the rejection of any retroactive application of the agreed wholesale rate to water sales on and after March 1, 2000. Finding that this provision violated the rule against retroactive rate-making, we directed that the rate apply only to sales made on or after April 24, 2000.

In its motion for partial reconsideration, Cynthiana argues that the Commission erred in making this modification. First, it asserts that the Commission’s approval of the Settlement Agreement did not “establish” rates and, therefore, approval of the agreement in its original form does not constitute retroactive rate-making. Second, it

asserts that retroactive application of the agreed rate is not contrary to the rule against retroactive rate-making as the purpose of the rule is to protect a utility's customers from unilateral rate increases for past use of services. Here, HCWA, the only affected customer, agreed to the retroactive application. Third, it argues that KRS 278.190(2) permits Cynthiana's assessment of the agreed rate for service on and after March 1, 2000.

The Commission finds no merit to Cynthiana's contention that our approval of the Settlement Agreement is not rate-making. The Settlement Agreement specifies the level of compensation that Cynthiana will receive for furnishing water service to HCWA. KRS 278.010(12) defines "rate" as

any individual or joint fare, toll, charge, rental, or other compensation for service rendered or to be rendered by any utility, and any rule, regulation, practice, act, requirement, or privilege in any way relating to such fare, toll, charge, rental, or other compensation, and any schedule or tariff or part of a schedule or tariff thereof

The Settlement Agreement therefore contains a new rate for water service that replaces the rate that is specified in Cynthiana's previous water supply contract with HCWA. As this rate differs from that which Cynthiana originally proposed and which the Commission suspended pursuant to KRS 278.190, it can become effective only upon Commission review and approval. That action is not a mere formality, but involves an extensive review of the agreed rate. It is this action, not any act of the parties, that constitutes the act of rate-making. See Kentucky Industrial Utility Customers, Inc. v. Kentucky Utilities Co., Ky., 983 S.W.2d 493, 501 (1998) ("The accountants for the Utility do not establish the rates for the consuming public. Only the regulatory commission has that responsibility.")

As a general rule, rates cannot be retroactively established. Analyzing this rule, one state supreme court succinctly explained its legal basis:

Pervading the utility rate making process is the fundamental rule that rates are exclusively prospective in application The rationale of this principle is that the Commission acts in a legislative capacity in exercising its rate making authority; that rate making orders have statutory effect; and, that, as such they are subject to the rules ordinarily applied to statutory construction.

The Supreme Court of the United States has also ruled that to accord a rate order retroactive effect, requires the “clearest mandate.”

Applicability of the principle of non-retroactivity of rate making orders, has been considered in numerous jurisdictions all of which recognize the rule that statutory authority is an indispensable prerequisite to retroactivity of such orders.

Louisiana Power and Light Co. v. Louisiana Pub. Serv. Com’n, 377 So.2d 1023, 1028 (La. 1979) (citations omitted). Most courts have endorsed this reasoning. See, e.g., Petition of Elizabethtown Water Co., 527 A.2d 354 (N.J. 1987); New England Telephone and Telegraph Co. v. Pub. Util. Com’n, 358 A.2d 1 (Me. 1976); Michigan Bell Telephone Co. v. Michigan Pub. Serv. Com’n, 24 N.W.2d 200 (Mich. 1946).

Kentucky clearly follows the general rule. Kentucky courts have recognized that rate-making is a legislative act. Kentucky Industrial Utility Customers, Inc., 983 S.W.2d at 496 (1998) (“It is well settled that rate making is a legislative function”). Absent an express declaration, retroactive effect may not be given to a law. KRS 446.080(3). KRS Chapter 278 contains no provision that allows for retroactive application of a rate based upon the facts before us.

Cynthiana next argues that an exception to the rule against retroactive rate-making exists where the utility and the affected customer agree to retroactive changes. It cites, however, no Kentucky statute or case law in support of its position. The authority presented in support of such principle appears to be isolated holdings based upon unique statutes.

The Commission has previously rejected the proposition that the parties to a Commission proceeding can expand or broaden the Commission's powers. See City of Newport, Ky. v. Campbell County Kentucky Water Dist., Case No. 89-014 (Jan. 31, 1990) at 7 ("Additional powers cannot be conferred on an administrative agency by contract of the parties."). Moreover, Kentucky courts have held that the Commission's powers are purely statutory and that the Commission may not add or subtract from those powers. See, e.g., Pub. Serv. Com'n v. Attorney General, Ky.App., 860 S.W.2d 296, 298 (1993). In light of these holdings, we find no basis to create an exception to the rule against retroactive rate-making.

Cynthiana next argues that KRS 278.190 confers upon it the right to place the agreed rate into effect on March 1, 2000 subject to refund. KRS 278.190 provides that when a utility files a schedule stating new rates and an effective date for such rates, the Commission may suspend the operation of the proposed rates for five months from their effective date to investigate their reasonableness. At the end of that five-month period, if the Commission has failed to establish new rates, the utility may place the proposed rate schedule into effect after providing written notice to the Commission. Cynthiana argues that it proposed to increase its rate for wholesale service from \$1.61 per 1,000 gallons to \$2.20 per 1,000 gallons on June 2, 1999 and that this increase was not

suspended. Accordingly, it argues that it had the legal right to place the agreed rate of \$1.85 into effect on March 1, 2000. The Commission finds nothing in the record or the law to support this argument. Cynthiana filed a proposed rate schedule on June 2, 1999 that made no reference to a wholesale rate of \$2.20 per 1,000 gallons. This schedule merely restated Cynthiana's current wholesale rates but eliminated the rate block of \$1.27 per 1,000 gallons for all sales in excess of 500,000 gallons. The schedule did not contain an effective date. Had the proposed schedule become effective, Cynthiana would have been authorized to charge HCWA \$1.61 per 1,000 gallons for all monthly purchases over 100,000 gallons. Cynthiana subsequently advised the Commission in writing that it intended to place the proposed schedule of rates into effect on August 1, 1999.¹ On July 22, 1999, the Commission suspended the proposed rate schedule until December 31, 1999. Cynthiana subsequently modified its proposed rate schedule through the filed testimony of its witnesses. On January 24, 2000, it filed a new rate schedule requesting a wholesale rate of \$2.20 per 1,000 and requested that the rate be retroactive to August 1, 1999.

KRS 278.180 clearly states that a utility must provide the Commission with 30 days' notice of a proposed rate change. As Cynthiana's last rate schedule sought a retroactive increase, it did not comply with KRS 278.180 and failed to put the Commission on notice of any intent to put the proposed rate into effect on a date certain. Without such notice, the Commission is not required to take any action to

¹ Letter from Virgie Florence Wells, Mayor of Cynthiana, Ky., to Jordan Neel, Manager - Tariffs Branch, Public Service Commission (July 7, 1999).

suspend the proposed rate and the utility had no legal right to implement the new, unapproved rate.

The Commission recognizes that permitting only prospective application of the agreed rate may appear harsh, but it is consistent with the existing law. Moreover, the parties and their legal counsel should have been aware of the state of the law when negotiating the agreement as well as the time Commission review of the Settlement Agreement would consume, given the voluminous record. These factors should have been considered during negotiations.

IT IS THEREFORE ORDERED that:

1. Cynthiana's motion for partial reconsideration is denied.
2. Cynthiana's motion for an informal conference to discuss a mechanism for the recovery of extraordinary costs is granted. The Executive Director or his designated representative shall immediately make arrangements for convening such conference.
3. This case is closed and shall be removed from the Commission's docket.

Done at Frankfort, Kentucky, this 19th day of May, 2000.

By the Commission

ATTEST:


Executive Director