

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

SOUTH SHORE WATER WORKS COMPANY)	
)	
COMPLAINANT)	
)	
v.)	CASE NO. 2002-00003
)	
CITY OF GREENUP, KENTUCKY)	
)	
DEFENDANT)	

O R D E R

South Shore Water Works Company (South Shore) has brought a formal complaint against the city of Greenup, Kentucky (Greenup) in which it requests enforcement of its wholesale water purchase contract. At issue is whether Greenup has modified the terms of a wholesale water purchase contract without Commission approval. Finding in the affirmative, we direct Greenup to provide wholesale water service to South Shore pursuant to the parties agreement of April 7, 1998.

PROCEDURE

On December 4, 2001, South Shore filed a formal complaint against Greenup in which it alleged that Greenup had failed to provide water service in accordance with the terms of a wholesale water contract between the entities. Upon our initial review of this complaint, we found that this complaint failed to state a prima facie case and, on our own motion, dismissed the complaint.

South Shore petitioned for rehearing and moved for leave to amend its complaint. On February 15, 2002, we granted this petition, permitted South Shore to amend its complaint, and directed Greenup to satisfy or answer the amended complaint. On February 22, 2002, Greenup answered that complaint and denied South Shore's allegations that a contract between the two entities for water service existed.

On March 27, 2002, the Commission established a procedural schedule to address those issues related to the existence of a contract for utility service between Greenup and South Shore. After the completion of discovery in this proceeding, Greenup moved to dismiss on the grounds that the Commission lacked subject matter jurisdiction over the Complaint. South Shore filed a response in opposition to this motion.

On May 3, 2002, the Commission held a hearing in this matter. The parties agreed that, in lieu of hearing evidence, the Commission should decide the matter based upon the existing record. The parties further agreed that no decision would be issued pending additional efforts to settle their dispute. On May 24, 2002, Greenup advised the Commission in writing that its City Council had not accepted South Shore's proposed terms, but approved continued efforts to resolve the matter.¹

On July 9, 2002, citing problems with its water supply and its need for immediate service from Greenup, South Shore moved for an expedited ruling in the matter. On July 12, 2002, Greenup filed a response to this motion in which it states no objections to an expedited ruling.

¹ Letter from John N. Hughes, Counsel for city of Greenup, Kentucky, to Thomas M. Dorman, Executive Director, Public Service Commission (May 24, 2002).

STATEMENT OF THE CASE

South Shore, a corporation organized under the laws of Kentucky, owns and operates facilities in the vicinity of South Shore, Kentucky, that distribute water to approximately 2,264 customers for compensation.² It is a utility subject to Commission jurisdiction. KRS 278.010(3)(c); KRS 278.040(1).

Greenup is a city of the fifth class that owns and operates a water treatment and distribution system. KRS 81.010(5). It provides water service to approximately 2,900 customers in Greenup and in the unincorporated areas of Greenup County.³

South Shore currently obtains its entire water supply from a wellfield situated within Greenup County, Kentucky. Beginning in the late 1980s, South Shore began experiencing problems with the quality and quantity of water from this wellfield. On March 6, 1998, South Shore issued a report on its sources of supply in which it concluded that a source of supply deficit existed.⁴ It concluded that within 5 years it would be unable to produce its maximum daily demand, within 10 years its maximum month daily demand, and within 15 years its average daily demand.⁵ It further concluded that the most reasonable remedy to this deficit was a connection for

² Annual Report of South Shore Water Company, Inc. to the Public Service Commission for the year ended December 31, 2001 at 31.

³ Water Resource Development Commission, Water-Resource Development: A Strategic Plan (Oct. 1999) at App. B-FIVCO Area Development District, 23-25, http://wrisc.state.ky.us/wrdc_plan/pdfs/greenup.pdf.

⁴ South Shore Water Works Co., Investigation of Sources of Supply and Future Demand (March 6, 1998) at 6.

⁵ Id.

supplement and emergency backup with Greenup.⁶ It provided copies of this report to Greenup and to the Natural Resources and Environmental Protection Cabinet (NREPC).

NREPC commented favorably upon South Shore s proposal. It urged South Shore to move forward with a proposed interconnection with Greenup. In a letter to South Shore, the Director of NREPC s Division of Water advised South Shore that Greenup had sought funding through the Community Development Block Grant Program and Rural Development for a water main extension project known as the Phase VI Project.⁷ This project involved the extension of Greenup s water mains into areas adjacent to South Shore s service territory. NREPC suggested that South Shore contact those agency s [sic] to verify their participation in the projects and whether the applications may be amended to provide for the interconnection between the two systems.⁸ Ten days later, NREPC advised South Shore that it had no objection to the proposed interconnection and that it supported efforts by water systems to make interconnections to provide better service to customers and water availability to citizens who currently do not have a reliable potable supply of drinking water.⁹

⁶ Id. at 10.

⁷ Letter from Jack Wilson, Director, Division of Water, NREPC to Joe Hannah, President, South Shore Water Works Company (Mar. 17, 1998).

⁸ Id. at 2.

⁹ Letter from Vicki L. Ray, Manager, Drinking Water Branch, Division of Water, NREPC, to Joe Hannah, President, South Shore Water Works Company (Mar. 27, 1998).

Apparently also responding favorably to the report, Greenup through its mayor requested that South Shore appear at the next meeting of its City Council to discuss the matter.¹⁰ On April 7, 1998, Joe Hannah, South Shore's President, appeared before the Greenup City Council and presented an application for water service. In this application, South Shore proposed:¹¹

- Greenup provide water service to South Shore through two 4-inch meter connections to Greenup's Phase VI extension. The location of the first connection would be at the north end of the Phase VI extension and South Shore's existing water main on East Tygart Road. The second connection would be located at the south end of the Phase VI extension at the intersection of East Tygart Road and Tygart Creek.
- South Shore would reimburse Greenup for the cost of these connections based upon the actual cost of making the connection or the rate set forth in Greenup's rate schedule.
- When taking water from these connections, South Shore would isolate certain areas of its water distribution system to ensure that only Greenup's water flowed to those areas.
- South Shore would faithfully pay for water service at a wholesale rate per 1,000 gallons that does not exceed the wholesale rate or reduced rate charged to any other individual, person, company, business, corporation, governmental entity [sic] or water supplier.
- The minimum bill for water service through the proposed connections should not exceed the rate for 1,000 gallons of water or be based upon the size of the meter connection.
- Greenup provide 90 days notice of any proposed change in the rates or charges to South Shore.
- Greenup pursue with all possible haste its funding efforts for the Phase VI Project.

¹⁰ Letter from Joe Hannah, President, South Shore Water Works Company, to Charles Veach, Mayor, city of Greenup, Kentucky (Mar. 11, 1998).

¹¹ Application for Wholesale Water Service before the City of Greenup.

- Greenup amend its current plans for the Phase VI Project to include and show the proposed connections for South Shore.
- South Shore could not withdraw its application for water service unless the connections for service were not available by July 2000 and South Shore had acquired another source of supply.

The minutes of Greenup's City Council recorded South Shore's presentation and the City Council's response as follows:

Joe Hannah from South Shore Water Works presented an application to Mayor and council for wholesale water service. Water to the north side of Plum Fork Hill.

A motion was made by Neil Wright and seconded by Paul Judkins to accept the application for wholesale water service from South Shore Water Works subject to engineering approval from the Division of Water and funding of Phase 6 water line extension.

. . .

Motion Carried: 6-0.¹²

On March 17, 1999, Greenup formally applied to Rural Development for funding for the Phase VI Project. The Preliminary Engineering Report, which was included in the application and provided a detailed description of the project, specifically noted that the proposed project would provide for the physical interconnection of Greenup and

¹² See Greenup's Response to Commission Staff's First Set of Interrogatories and Requests for Production of Documents, Item 1.

South Shore's systems at the points set forth in South Shore's Application.¹³ The Final Engineering Report, which was issued on December 13, 2000, also contains this notation.¹⁴

Greenup eventually received funding from Rural Development and other governmental sources and the necessary regulatory approvals to construct the Phase VI Project. As of April 15, 2002, Greenup had completed all construction related to the proposed project.

As part of the Phase VI Project, Greenup made several changes to the original project design to provide for two interconnections with South Shore. Several miles of the proposed water main extension, originally designed as 4-inch water main, were increased to 6-inch water main to accommodate the expected demand. Greenup added additional water main to the project to reach the interconnection points. It also installed two 4-inch water meters and metering pits and several flush hydrants to serve South

¹³ The Greenup and South Shore water systems are physically separated along U.S. 23 by approximately 4.5 miles. The southern limits of the South Shore system being on U.S. 23 near Siloam the Greenup system northerly limits ending on Old U.S. 23 near Greys Branch. **The Phase 6 project will include two (2) separate connection points/4-inch master meters for the South Shore System. The connections will be provided at the north/south end of the proposed Phase 6 waterline on East Tyarts Road.**

Woolpert, Preliminary Engineering Report Phase 6 Water Line Extension Project (Feb. 26, 1999) at 8 (emphasis added). For a copy of this report, see Greenup's Response to Commission Staff's First Set of Interrogatories and Requests for Production of Documents, Item 4.

¹⁴ Woolpert, Final Engineering Report Phase 6 Water Line Extension Project (Dec. 13, 2000) at 6 - 7. For a copy of this report, see Greenup's Response to Commission Staff's First Set of Interrogatories and Requests for Production of Documents, Item 4.

Shore. These changes added approximately \$250,000 to the Phase VI Project's total cost.¹⁵

South Shore asserts that it implemented changes in its facilities at significant cost to accommodate the expected interconnection. In October 1998, it began construction of a reservoir at a higher elevation than originally planned and capable of handling Greenup's higher water pressures in expectation of the interconnection. Upon its completion in 2000, the total cost of this reservoir was \$90,450.¹⁶

Near the time of the Phase VI Project's completion, South Shore and Greenup entered discussions regarding a water user agreement. In November 2001, these discussions reached an impasse over the provisions of a minimum monthly bill for wholesale service. On November 28, 2001, South Shore tendered \$5,000 to Greenup as payment for all tapping fees related to the interconnection.¹⁷ Greenup refused to accept this payment.¹⁸ South Shore then filed its complaint with the Commission.

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. McClellan v. Louisville Water Co., Ky., 351 S.W.2d 197, 199 (1961). See also City of Mount Vernon v. Banks, Ky., 380 S.W.2d 268, 270 (1964) (In

¹⁵ Greenup's Response to South Shore's Interrogatories, Item 11.

¹⁶ Amended Complaint at ¶¶10-15.

¹⁷ Letter from Joe Hannah, President, South Shore Water Works Company, to Jimmy Doran, Mayor, city of Greenup, Kentucky (Nov. 28, 2001).

¹⁸ Letter from Vicky Hieneman, City Clerk, city of Greenup, Kentucky, to Joe Hannah, President, South Shore Water Works Company (Nov. 29, 2001).

the operation of a water plant a municipal corporation is not under the jurisdiction of the Public Service Commission.). The exception to this exemption occurs when a municipal utility contracts to provide utility service to a utility. Simpson County Water District v. City of Franklin, Ky., 872 S.W.2d 460, 463 (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.).

South Shore argues that a wholesale water service contract exists between it and Greenup based upon Greenup's acceptance of South Shore's application for wholesale water service. It further asserts that, as a result of this contract, the Commission possesses jurisdiction over Greenup's provision of wholesale service to South Shore and Greenup's refusal to provide such service. It requests that the Commission assert jurisdiction over the dispute and determine the appropriate minimum water usage and water rates to be assessed under the contract.

Contending that South Shore's application fails to contain the essential terms of an agreement for water service, Greenup denies the existence of any contract. It points to the discussions between the parties since August 2001 regarding the rate, minimum bill, deposit and term of agreement. It further notes that the parties have not reached any agreement on these terms. Greenup's argument, simply put, is [t]here is no document that sets forth the terms and conditions of service to SSWW [South Shore Water Works Company] that both parties have agreed to or have executed in the formality of a contract. Greenup's Motion to Dismiss at 2. In the absence of a contract,

Greenup argues, the Commission has no jurisdiction over the subject matter of the complaint and lacks any authority to grant the requested relief.

The principal issue before us, therefore, is whether Greenup's acceptance of South Shore's application created a contract for wholesale water service. If a contract exists, then the Commission has jurisdiction over Greenup's provision of such service and the rates and conditions attached to the provision of such service. If no contract exists, then we lack jurisdiction to hear South Shore's complaint.

Prior to deciding that issue, the Commission must first determine whether it has the authority to rule on the existence of a contract. Greenup argues that the Commission has no jurisdiction to decide questions of law or fact that do not relate to rates or service. The issue of whether a contract exists between the parties, Greenup argues, is a fact question unrelated to utility rates or service that must be resolved in a court of law. Contract interpretation, it argues, is not within the Commission's purview.

We disagree. An administrative agency generally may and must determine whether it has jurisdiction in a particular situation. 2 Am. Jur. 2d Administrative Law §277 (2002). Clearly the Commission has exclusive jurisdiction over utility rates and service. KRS 278.040(2). This jurisdiction extends to contracts between a city and a utility for utility service. Simpson County Water District, 872 S.W.2d at 463. The question of the existence of a contract is a question of the Commission's jurisdiction over the dispute and is thus within the Commission's power to address.

We now turn to the question of whether a contract exists between Greenup and South Shore. A contract requires a clear and definite offer and acceptance. In the present case, South Shore's application constitutes a clear and definite offer. It set forth

in sufficient detail the terms under which South Shore would take water service. It specified the location of the delivery points, meter size, the wholesale rate¹⁹ and the minimum bill.²⁰ It contained specific notice provisions for the modification of any rate or service provisions.

Likewise, Greenup's response to this offer was clear and definite. Greenup's City Council accepted the offer subject to obtaining funding for and regulatory approval of the Phase VI Project. It placed no other conditions or restrictions upon its acceptance of this offer.

We find no merit in Greenup's contention that no contract could be entered without the actions of Greenup's mayor. The resolution of Greenup's City Council, duly recorded, is sufficient action to constitute a binding acceptance. See Eugene McQuillin, The Law of Municipal Corporations §29.03 (3d. ed. 1999) (A proposition or offer made to the proper corporate authorities and an acceptance of the terms of it by ordinance, resolution or motion constitutes a contract. The ordinance or other official act accepting the terms of the proposition constitutes assent to the contract on the part of the corporation, as distinguished from a mere declaration of intention to enter into a contract.).

The parties' subsequent conduct further indicates that the parties had contracted for the provision of water service. Greenup amended its application to various funding

¹⁹ While it did not state a specific wholesale rate, it clearly stated that the rate would be in increments of 1,000 gallons and would not exceed any other wholesale rate. Application at ¶9.

²⁰ The Application provided that the monthly minimum bill would not exceed the rate for 1,000 gallons and could not be based upon the meter size or connection size.

agencies to specifically provide for the agreed interconnections. It further expended an additional \$250,000 of public funds to modify the Phase VI Project to make the interconnections. Similarly, South Shore expended over \$90,000 on facilities in contemplation of the interconnection.

We do not accept Greenup's contentions that the parties' discussions following Greenup's acceptance of South Shore's application demonstrated the lack of a contract. Based upon the record presented to us, it appears that the parties were negotiating modifications to the terms of their initial contract. Their failure to reach agreement on these modifications does not terminate the initial contract.

Having determined the existence of a contract for wholesale water service between South Shore and Greenup, we find that the contract rate for such service is the same rate that it currently assesses its other wholesale customers or, in the absence of another wholesale customer, the rate that Greenup currently assesses to its retail customers served through the Phase VI Project. Similarly, Greenup may assess a monthly minimum bill that is no greater than that assessed to any other wholesale customer or, in the absence of any other wholesale customer, that currently assessed to its retail customers served through the Phase VI Project.

The Commission notes that nothing within the initial contract prohibits or precludes Greenup from revising the rates or conditions of service set forth in the initial contract. Such revisions, however, require 90 days' notice to South Shore and must be filed with the Commission in accordance with KRS 278.180.²¹ To the extent that

²¹ The 90-day notice requirement may also be amended through the procedures set forth in KRS 278.180.

Greenup finds that the rates to which it agreed in 1998 no longer reflect the actual cost of service, it is encouraged to revise its rates to reflect existing costs.

IT IS THEREFORE ORDERED that:

1. Within 7 days of the date of this Order, Greenup shall begin providing wholesale water service to South Shore through the agreed interconnection points.

2. Greenup shall provide wholesale water service to South Shore at the same rate it currently assesses its other wholesale customers or, in the absence of another wholesale customer, the rate that Greenup currently assesses to its retail customers served through the Phase VI Project.

3. Greenup shall assess a monthly minimum bill that is no greater than that assessed to any other wholesale customer or, in the absence of any other wholesale customer, that currently assessed to its retail customers served through the Phase VI Project.

4. Within 20 days of the date of this Order, Greenup shall file tariff sheets with the Commission that set forth the rate at which it is providing wholesale water service to South Shore and all conditions of service that it imposes.

5. Upon its commencement of wholesale water service to South Shore, Greenup shall immediately advise the Commission in writing of this action.

Done at Frankfort, Kentucky, this 24th day of July, 2002.

By the Commission

ATTEST:

A handwritten signature in black ink, appearing to read "Thomas H. Dixon", written over a horizontal line.

Executive Director