COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

PROPOSED ADJUSTMENT OF THE WHOLESALE WATER SERVICE RATES OF LEBANON WATER WORKS	)))	CASE NO. 2017-00417

RESPONSE TO MOTION FOR AN ORDER ESTABLISHING A PROCEDURAL SCHEDULE AND ASSIGNING BURDEN OF PROOF

Comes now Marion County Water District ("Marion District"), by counsel, pursuant to 807 KAR 5:001 Section 5(2) and other applicable law, and for its response to the Motion for an Order Establishing a Procedural Schedule and Assigning Burden of Proof filed by the Lebanon Water Works Company ("Company") on January 31, 2018, respectfully states as follows:

I. INTRODUCTION

Marion District agrees that a procedural schedule should be entered. The Company is proposing a 34% increase in its rate for the sale of potable water to Marion District, which appears to be excessive and unreasonable. Moreover, in a blatant attempt to dissuade Marion District from challenging the reasonableness of the proposed rate, the Company is also seeking sanction to impose the entirety of the cost of defending the proposed rate on Marion District. Both the amount of the rate request and the discriminatory intent evidenced in the effort to punish Marion District for challenging said increase are unlawful and should not be condoned.

Requesting the Commission to exercise its statutory jurisdiction under KRS 278.040 and KRS 278.200 hardly qualifies as what the Company labels "an extraordinary remedy."[1] The fact that the Company's rate for the sale of water to Marion District must be "fair, just and reasonable" is beyond doubt.[2] Likewise, it is undeniable that the Commission's jurisdiction over the Company's rate is "exclusive" in nature.[3] The Company's September 13, 2017 filing of the proposed tariff confirms that the rate which the Company charges to Marion District for the provision of water falls well within the ambit of the Commission's jurisdiction.[4]

The rate increase sought by the Company may have been approved by the City Council of the City of Lebanon, Kentucky ("Council"), but it may only become effective as applied to Marion District after Commission review. The term of the Master Agreement providing for an alternative method for approving rates was superseded and rendered void over twenty-five years ago by the Kentucky Supreme Court's decision in *Simpson County Water District v. City of Franklin*, which unambiguously affirmed that the Commission has sole and exclusive jurisdiction over the rate a municipal utility may charge to a water district.[5]

Adding insult to injury, the Company has now filed a motion asking the Commission to assign the burden of proof in this case to Marion District. The Company is either unaware that the Commission has already stated, by Order, that it is the Company that bears the burden of proof;[6]

---

[1] Company's Memorandum, p. 11.

[2] *See* KRS 278.030(1).

[3] *See* KRS 278.040(2).

[4] *See* Company's Letter to John Lyons (filed September 13, 2017).

[5] *See Simpson County Water District v. City of Franklin*, 872 S.W.2d 460 (Ky. 1994); *see also City of Greenup v. Public Service Comm'n*, 182 S.W.3d 535, 538 (Ky. App. 2005).

[6] *See* Order, Case No. 2017-00417, p. 4 (Nov. 13, 2017).

or the Company has simply chosen to disregard the Commission's Order. Regardless, the Company's motion lacks legal or factual support and must therefore be overruled.

II. ARGUMENT

The Company's motion boils down to one simple premise: If the Company's proposed rates are not found to be reasonable, then: (1) the rate Marion District pays would be lower than the rate paid by retail municipal customers in Lebanon; and (2) the existence of two rates would result in a material revision of the Master Agreement. Thus, the Company asserts that Marion District's effort to challenge the proposed rate increase equates to an effort to rewrite the Master Agreement, for which Marion District must bear the burden of proof. In addition to the flaws in the Company's logic, the Company's argument is simply incompatible with Kentucky law.

A. The Company's Logic is Flawed

The Company postulates that, if its proposed rate is not sustained, then Marion District will pay a lower rate than the rate paid by Lebanon's retail municipal customers. It is worth noting that the Company does not even suggest that the rate it is proposing could be too low – the motion concedes that any deviation from the proposed rate will be downward. This concession should be borne in mind as the case progresses. Apart from that side note, the Company's argument relies entirely upon a critical assumption that it cannot possibly sustain. Whether the Commission's review of the proposed rate increase results in one rate for Marion District and a separate rate for the citizens of Lebanon is a matter that ultimately and exclusively lies within the discretion of the Company and the Council.

Any Commission Order in this case regarding the rate that the Company may charge to Marion District would have no effect upon the rate that the Company may choose (with the Council's consent) to impose upon retail municipal customers. The Commission has no

jurisdiction over rates applicable to retail municipal customers,[7] and Marion District is not suggesting anything to the contrary. *Simpson County* makes it abundantly clear that the municipal exemption from Commission oversight does not apply to the sale of water by a municipal utility to a regulated water district.[8]

One would logically presume that the Company and Council would agree that retail municipal customers should also receive the benefit of a lower rate if the Commission finds that the proposed rate increase is excessive. However, if the Company and Council think differently and believe that a lower rate approved by the Commission following discovery, an evidentiary hearing and briefing should not also apply to retail municipal customers, it would be the conscious decision on the part of the Company and Council to not lower the retail municipal rate that prospectively creates the second rate. In fulfilling its statutory mandate under KRS 278.040 and KRS 278.200, the Commission is not in any way impairing the ability of the Company and Council to set whatever rate they deem appropriate for retail municipal customers. The Company's premise is flawed and, on that basis alone, its motion should be overruled.

B. The Company's Motion is Inconsistent with Kentucky Law

The Company's motion should also be denied due to its inconsistency with Kentucky law. For instance, the Company argues that Marion District is "seeking to modify the single, uniform rate" contemplated in the Master Agreement and asking the Commission to "replace it with a dual rate that would be favorable to Marion District."[9] Because of this, the Company alleges, the burden

[7] *See McClellan v. Louisville Water Co.*, 351 S.W.2d 197, 199 (Ky. 1961); *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.").

[8] *See Simpson County*. at 463 ("[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.").

[9] Company's Memorandum, pp. 11, 14.

of proof should be assigned to Marion District. This argument elevates form over substance and disregards the fundamental concerns with the Company's proposed rate that were expressed in the September 19, 2017 protest and request for Commission review. To be clear: Marion District wants only to be charged a rate that is fair, just and reasonable; nothing more, nothing less.[10] The Company's claim that the number of rates it charges is somehow more important than the reasonableness of the rate(s) it charges is a blatant attempt to shield its rate proposal from serious scrutiny, using a term from the Master Agreement that has been nullified by *Simpson County* as a shield. Each of the points the Company raises to support its argument that Marion District bears the burden of proof is quickly dispelled.

1. The Company is the Party Seeking Relief - Accordingly, it Bears the Burden of Proof

The Company claims that, in requesting the Commission to investigate the reasonableness of the proposed rate increase, Marion District "has sought a remedy not available to it in the Master Agreement."[11] What the Company fails to admit is that the Master Agreement's process for changing the rate it charges to Marion District was significantly nullified when the Kentucky Supreme Court decided *Simpson County*. The Court unequivocally held that "[t]he manifest purpose of the Public Service Commission is to require and insure fair and uniform rates, prevent unjust discrimination, and prevent ruinous competition."[12] The Commission has "exclusive" jurisdiction over the rate the Company charges to Marion District under KRS 278.040(2). As a

[10] The Commission's jurisdiction in this area is specifically intended to protect the customers of regulated water utilities from unfair practices by municipal utilities. *See Grayson Rural Electric Corp. v. City of Vanceburg*, 4 S.W.3d 526, 528 (Ky. 1999) ("[O]ur predecessor Court recognized that voting power gave residents of a city some means of protection against excessive rates or inadequate service of a utility owned by the city. However, customers outside the city have no such protection.") citing *Louisville Water Co. v. Public Service Comm'n.*, 318 S.W.2d 537, 539 (Ky. 1958).

[11] Company's Memorandum, pp. 12-13.

[12] *Simpson County*, at 464; citing *City of Olive Hill v. Public Service Comm'n*, 203 S.W.2d 68 (Ky. 1947).

matter of law, the language of the 1988 Master Agreement cannot trump the Kentucky Supreme Court's 1994 interpretation of KRS 278.040 and KRS 278.200, to the extent they are in conflict. As the Supreme Court said, "[t]he rates and service exception to a city's exemption from PSC regulatory jurisdiction is not avoidable by contract."[13]

Even the Company's own conduct confirms this.[14] Section 8 of the Master Agreement provides, "[w]ith respect to any future application for modification or its rates, the Company shall *present only to the City Council of Lebanon, Kentucky* the basis upon which such rate modification is sought" (emphasis added). However, the Company's September 13, 2017 filing with the Commission confirms that its rate could never become effective as applied to Marion District without first being reviewed and scrutinized by the Commission.[15] The Company cannot act contrary to the terms of the Master Agreement to comply with Kentucky law and then accuse Marion District of violating the same provision of the Master Agreement when it also complies with Kentucky law. The Company is the applicant in this case because it is proposing a new rate. Accordingly, it bears the burden of proof as a matter of law.[16]

2. The Company's Reliance Upon Commission Precedent is Misplaced

The Company also relies upon two prior Commission cases to suggest that Marion District must bear the burden of proof. Each of these cases is readily distinguishable. The Company first

---

[13] *Simpson County*, at 463.

[14] The Company alleges that having two rates for water would abolish a "material provision" of the Master Agreement. Elsewhere, however, it characterizes the single rate as a protection only benefitting Marion District, not the city's retail municipal customers. *Compare* Company Memorandum pp. 5, 17. The importance the Company places upon the single rate provisions therefore appears to be situational more than consistent.

[15] The two exclusive methods by which a change in rates may be imposed by a municipal utility upon a water district are set forth in a Commission Staff Opinion dated February 16, 2007. A copy of the Staff Opinion is attached hereto and incorporated herein by reference as Exhibit 1.

[16] *See Energy Regulatory Commission v. Kentucky Power Co.*, 605 S.W.2d 46, 50 (Ky. App. 1980) citing *Lee v. International Harvester Co.*, 373 S.W.2d 418 (Ky. 1963).

cites *East Clark Co. Water Dist. v. City of Winchester* ("*East Clark District*") for the proposition that a water district bears the burden of proof to challenge "a municipal utility's existing rate for wholesale service."[17] The procedural posture of the Commission's decision in *East Clark District* is strikingly different than this proceeding and, when the Commission's Order is read in its entirety, it is abundantly clear that the Company's reliance upon the case is misplaced.

In *East Clark District*, the Winchester municipal utility had proposed a rate increase, given notice of same to the Commission and the water district never filed a protest or otherwise objected to the proposed increase. In fact, the water district supported the proposed rate increase. As one would expect, the Commission allowed the rate increase to go into effect and only sometime later did the water district change its position and object to the new rate. Because the new rate was already in effect, the water district filed a complaint case – not a protest and request for Commission review – against the City of Winchester and its municipal utility board. Clearly, in the context of a complaint case, East Clark District bore the burden of proof because it was the complainant challenging a rate that already gone into effect. Indeed, the Commission specifically noted that East Clark District's delay in challenging the proposed rate increase was the cause of it having to bear the burden of proof:

> We note that WMU originally possessed the burden of proof to demonstrate the reasonableness of its rates when it filed its proposed rate in December 2004. At that time, East Clark District could have objected to the proposed rate and requested a Commission investigation. Such a request would have led to suspension of the proposed rate and a rate investigation. In such investigation, WMU would have had the burden to demonstrate that the proposed rate was reasonable and consistent with the terms of the water purchase agreement.[18]

---

[17] Company's Memorandum, p. 14 citing *East Clark County Water District v. City of Winchester, Acting By and Through Winchester Municipal Utilities Commission*, Order, Case No. 2005-00322 (Ky. P.S.C. Apr. 3, 2006).

[18] *Id.*, Order, p. 3.

In this case, Marion District filed a timely protest to the Company's proposed rates and the Commission appropriately initiated its own investigation into the reasonableness of the Company's proposed rates. Marion District is challenging the Company's *proposed* rate increase, not its *existing* rate. *East Clark District* therefore confirms that the Company, not Marion District, bears the burden of proof to demonstrate the reasonableness of its proposed rates in this proceeding.

Likewise, the Company's reliance upon the *City of Versailles* case is similarly misplaced.[19] In *City of Versailles*, the Commission suspended a proposed tariff filing whereby the municipal utility sought to unilaterally impose a minimum water purchase obligation upon a regulated water district. The Commission suspended the proposed tariff and ultimately found that the proposed revision was unreasonable. Again, it was the applicant, not the objecting party, that bore the burden of proof. The *City of Versailles* case simply does not support the Company's argument to shift the burden of proof in this case. Commission precedent affirms that the burden of proof in this case rests solely and exclusively upon the Company.

3. The Company's Reliance Upon "Public Policy" Fails to Reveal the Public Policy Upon Which it Relies

The Company's final argument is that reassigning the burden of proof to Marion District somehow satisfies vague notions of "sound public policy."[20] It bears emphasis that the burden of proof is assigned by the law, not by subjective ideas as to what constitutes "sound public policy" in any given circumstance. Thus, the Company's policy argument is void *ab initio*. Nevertheless,

[19] *See In the Matter of the Proposed Revision of the Rules Regarding the Provision of Wholesale Water Service by the City of Versailles to Northeast Woodford Water District*, Order, Case No. 2011-00419 (Ky. P.S.C. Aug. 12, 2014).

[20] Company's Memorandum, p. 15.

the only relevant public policy identified by the Company is the contractual opportunity that Marion District possesses under the Master Agreement to protest or object to the proposed rate before the Council prior to it being acted upon in a "public hearing."[21] In light of the Supreme Court's holding in *Simpson County*, the ability to present a challenge to the Council should be viewed for what it is – an opportunity to discuss a disagreement. It is no longer the venue in which the rate applicable to Marion District will be finally established.

Even if the Council's approval was relevant, the Company fails to describe the "public hearing" the Council conducted in this particular instance, however. Two readings of an ordinance that occurs in the context of regularly-scheduled Council meetings would hardly qualify as a public hearing on the reasonableness of the proposed rates. The Company asserts that the process spelled out in the Master Agreement "ensures that the Lebanon City Council rigorously investigates any proposed rate to determine that the proposed rate accurately reflects the cost of service."[22] Yet, there is nothing in the record which substantiates the claim that the Council gave any substantial unbiased, independent review to the Company's proposal. Certainly, there was some discussion between Marion District and the Company prior to the proposed rates being acted upon by the Council.[23] Marion District's concerns, however, were virtually ignored. "Public policy" provides no basis to ignore the law's placement of the burden of proof upon the Company.

C. The Company's Characterization of Marion District's Protest is Misleading

One final point merits a response. The Company seeks to emphasize the validity of its argument primarily by repeating it over and over again. Repetition does not equate to

---

[21] *Id.*, p. 15 (referring to Section 8 of the Master Agreement).

[22] *Id.*, p. 13.

[23] *See* Company's Memorandum, Testimony of Daren Thompson, Exhibit 16.

persuasiveness. The Company claims that, "[i]n requesting review of the single, uniform rate, Marion District *essentially requests* the modification of the Master Agreement...."[24] Arguments based upon loose characterizations of what an opposing party "essentially requests" are what logicians often refer to as "strawman arguments." They lack conviction and evidentiary support. The Company's fallaciousness is highlighted in succeeding sentences where it says Marion District: (1) has requested relief "under the guise of a rate investigation;" (2) tendered a protest that is "tantamount to a Complaint;" and (3) is "requesting the change in the long standing Master Agreement."[25] Perhaps the most entertaining of the Company's assertions is the statement: "Marion District requests that the Commission conduct its own review of the cost of service, substitute its own methods of analysis and procedures for those set forth in the Master Agreement, and then impose its findings upon the parties to the Master Agreement."[26] The Company's motion suggests that Marion District should be ashamed of itself for seeking to invoke the rights afforded by KRS 278.040 and KRS 278.200 to protect its own customers from what appears to be an unreasonable rate increase. However, that is exactly what the Supreme Court intended for water districts to do in situations such as this:

> The PSC acts as a quasi-judicial agency utilizing its authority to conduct hearings, render findings of fact and conclusions of law, and utilizing its expertise in the area and to the merits of rates and service issues. The rates and service exception effectively insures, throughout the Commonwealth, that any water district consumer/customer that has contracted and become dependent for its supply of water from a city utility is not subject to either excessive rates or inadequate service.[27]

[24] *See* Company's Memorandum, p. 15 (emphasis added).

[25] *Id.*

[26] *Id.*

[27] *Simpson County*, at 465.

III. CONCLUSION

The burden of proof to justify the proposed rate increase in this case falls upon the Company alone. Marion District is doing nothing other than availing itself of the rights granted to it by KRS 278.040 and KRS 278.200 and should not be punished for doing so. If Marion District failed to challenge what appears to be an unreasonable rate increase, it would be falling short of the obligations that it owes as a regulated utility and political subdivision of the Commonwealth of Kentucky to its own retail customers. For all the reasons set forth herein, Marion District respectfully requests the Commission to overrule the Company's motion. In so doing, Marion District respectfully requests the Commission to enter a procedural schedule as well.

This 7th day of February, 2018.

Respectfully submitted,

David S. Samford
L. Allyson Honaker
GOSS SAMFORD, PLLC
2365 Harrodsburg Road, Suite B-325
Lexington, Kentucky 40504
(859) 368-7740
david@gosssamfordlaw.com
allyson@gosssamfordlaw.com

and

Kaelin G. Reed
The Law Office of Mattingly & Nally-Martin, PLLC
P.O. Box 678
104 West Main Street
Lebanon, Kentucky 40033
(270) 692-1249
kaelin@mattinglylawoffices.com

Counsel for Marion County Water District

CERTIFICATE OF SERVICE

This is to certify that foregoing electronic filing is a true and accurate copy of the document being filed in paper medium; that the electronic filing was transmitted to the Commission on February 7, 2018; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding; and that a copy of the filing in paper medium is being hand delivered to the Commission on this the 7th day of February.

Counsel for Marion County Water District

Ernie Fletcher
Governor

Teresa J. Hill, Secretary
Environmental and Public
Protection Cabinet

Timothy J. LeDonne
Commissioner
Department of Public Protection

Commonwealth of Kentucky
Public Service Commission
211 Sower Blvd.
P.O. Box 615
Frankfort, Kentucky 40602-0615
Telephone: (502) 564-3940
Fax: (502) 564-3460
psc.ky.gov

Mark David Goss
Chairman

John W. Clay
Commissioner

February 16, 2007

Mr. Kevin Shaw
Grayson County Water District
P.O. Box 217
Leitchfield, Kentucky 42755

Dear Mr. Shaw:

Commission Staff acknowledges receipt of your letter of January 31, 2007 in which Grayson County Water District requests clarification of the procedures that a municipal utility must follow to adjust its wholesale water service rate to a public utility.

In your letter, you present the following facts:

> Grayson County Water District ("Grayson District"), a water district organized pursuant to KRS Chapter 74, currently purchases its water requirements from the city of Leitchfield, Kentucky ("Leitchfield"). On January 12, 2007, consultants for Grayson District and Leitchfield agreed upon a new wholesale water service rate. On January 22, 2007, Grayson District's Board of Commissioners accepted the agreed rate. Three days later Grayson District notified Leitchfield of its Board of Commissioners' action and requested that it be notified upon Leitchfield's filing of notice of the proposed rate adjustment with the Public Service Commission. On January 31, 2007, Leitchfield's legal counsel advised Grayson District that the Public Service Commission would be notified of the proposed rate adjustment by letter for "courtesy purposes." Leitchfield's City Clerk subsequently advised Grayson District that it would bill at the proposed rate for service provided on and after January 12, 2007.

You present the following question: What procedures must Leitchfield follow to place its proposed wholesale water service rate into effect?

In Simpson County Water District v. City of Franklin, 872 S.W.2d 460 (Ky.1994), the Kentucky Supreme Court held that the Public Service Commission has jurisdiction over contracts between municipal utilities and public utilities and that changes in any rate that a municipal utility assesses a public utility for wholesale utility service must be approved by the Public Service Commission. Pursuant to the Simpson County decision, the Public Service Commission in Administrative Case No. 351 directed that "[a]ny municipal utility wishing to change or revise a contract or rate for wholesale utility service to a public utility shall, no later than 30 days prior to the effective date of the revision, file with the Commission the revised contract and rate schedule." A copy of the Simpson County decision and the Public Service Commission's Order is enclosed.

A municipal utility has two methods for changing its rates for utility service to a public utility:

- Filing A New Rate Schedule. This method, which is governed by KRS 278.180 and Public Service Commission Regulations 807 KAR 5:001 and 807 KAR 5:011, is the easier and faster method for adjusting a rate. A municipal utility files a rate schedule which contains the new rate. (If the new rate is part of a new contract with a public utility, then the contract is filed.) The rate schedule must be filed with the Public Service Commission not less than 30 days before the proposed rate is scheduled to take effect. A copy of the form on which the proposed rate schedule should be filed is enclosed. **Any filing that does not use this form will be rejected.** When filing its rate schedule, a municipal utility must notify its public utility customers of the proposed rate change. This notice should be in writing and should generally conform to the requirements of Commission Regulation 807 KAR 5:001, Section 10(3). Proof of notice to the public utility should be submitted when the rate schedule is filed.

- Formal Application For Public Service Commission Approval. Public Service Commission Regulation 807 KAR 5:001 governs this filing. Under this method, the municipal utility makes a formal application to the Public Service Commission for approval of its proposed rates. The application must be filed with the Public Service Commission not less than 30 days before the proposed rates are to become effective. The application must include information about the municipal utility's past operations. Commission Regulation 807 KAR 5:001, Section 10, a copy of which is enclosed, identifies all required information. When it files its application for rate adjustment, a municipal utility shall notify its public utility customers of the proposed rate changes in the same manner as municipal utilities that file new rate schedules.

The Public Service Commission has 30 days from the filing of a rate schedule or an application for rate adjustment to suspend the rate for further review. See KRS 278.190. Where a municipal utility files a new rate schedule and the Public Service Commission suspends the proposed rate for further review, the municipal utility must provide the information which Commission Regulation 807 KAR 5:001, Section 10, requires.

If the proposed rate is suspended, it may not be placed into effect for five months. KRS 278.190(2). If the Public Service Commission has not approved the proposed rate within this five-month period, then the municipal utility may place the proposed rate into effect subject to refund. The Public Service Commission must rule on the proposed rate within ten months of the filing of the rate schedule or application. See KRS 278.190(3).

A municipal utility must comply with one of these procedures even when its wholesale customers have agreed to the proposed rate adjustment. Failure to follow these procedures will prevent the proposed rates from becoming effective. Please note that as of the date of this letter, Leitchfield has yet to file any revisions to its existing wholesale water service rate of $1.439 per 1,000 gallons. Until proper and timely notice of the proposed adjustment is given, Leitchfield may only assess the rate of $1.439 per 1,000 gallons.

This letter represents Commission Staff's interpretation of the law as applied to the facts presented. This opinion is advisory in nature and not binding on the Commission should the issues herein be formally presented for Commission resolution. Questions concerning this opinion should be directed to Gerald Wuetcher, Deputy General Counsel, at (502) 564-3940, Extension 259.

Sincerely,

Beth O'Donnell
Executive Director

Enclosures
cc: David B. Vickery, Esq.