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October 19, 2009

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Post Office Box 634  
Frankfort, Kentucky 40602-0634

R. Stephen McGinnis, Esq.  
McBrayer, McGinnis, Leslie and Kirkland, PLLC  
Post Office Box 280  
Greenup, Kentucky 41144-0280

Re: Case No. 2009-00247  
South Shores Water Works Co. v. City of Greenup

Gentlemen:

The enclosed memorandum has been filed in the record of the above-referenced case. Any comments regarding this memorandum's contents should be submitted to the Commission within five days of receipt of this letter. Any questions regarding this memorandum should be directed to Gerald Wuetcher, Executive Advisor, at (502) 564-3940, Extension 259.

Sincerely,

A handwritten signature in black ink, appearing to read "Jeff Derouen", with the words "on behalf of" written in smaller script below it.

Jeff Derouen  
Executive Director

gw  
Enclosure

**INTRA-AGENCY MEMORANDUM**  
**KENTUCKY PUBLIC SERVICE COMMISSION**

**TO:** Case File No. 2009-00247

**FROM:** Gerald Wuetcher <sup>GEW</sup>  
Executive Advisor

**DATE:** October 16, 2009

**RE:** Conference Call of October 14, 2009

On October 14, 2009, Commission Staff conducted a conference call in this case. Participating were:

R. Stephen McGinnis	-	City of Greenup
R. Benjamin Crittenden	-	South Shore Water Works Company
Gerald Wuetcher	-	Commission Staff

Commission Staff arranged for the conference call at the parties' joint request.

Beginning the conference call, Mr. Wuetcher stated that Commission Staff would prepare minutes of the conference for the case record, that a copy of these minutes would be provided to all parties, and that all parties would be given an opportunity to submit written comments upon those minutes.

Mr. McGinnis and Mr. Crittenden advised that negotiations between the parties are progressing. They noted three issues for which they needed clarification. These were: South Shore Water Works Company's ("South Shore") ability to pass through the cost of purchased water to its ratepayers; South Shore's right to contest an agreed wholesale rate, and restrictions upon the quantity of water provided.

As to the first issue, Mr. Wuetcher stated that the Commission was required to establish rates for South Shore that recovered the reasonable cost of purchased water. To the extent that the City of Greenup's ("Greenup") rate for purchased water exceeded South Shore's cost of producing its own water, South Shore would be required to demonstrate the reasonableness of its decision to purchase rather than produce water. In reviewing the reasonableness of such decision, the Commission would consider whether the construction of additional facilities by South Shore to produce water was necessary and how frequently these additional facilities would be needed to meet South Shore's demand. The Commission would likely compare South Shore's cost of producing the water including the cost of these new facilities with the cost of merely purchasing water from Greenup.

Mr. Wuetcher noted that, once Greenup established a rate for service and then subsequently adjusted that rate, South Shore could use the purchased water adjustment procedures set forth in 807 KAR 5:067. These procedures, however, could not be used to adjust South Shore's existing rate to reflect the additional source of supply.

Mr. Wuetcher stated that South Shore may contest an agreed rate. He noted that, as a result of the *Simpson County Water District v. City of Franklin* decision, Greenup is considered a public utility when providing utility service to a water district. KRS 278.030 permits public utilities to charge "fair, just, and reasonable rates" for service. Circumstances may change that render unreasonable a rate that was once considered reasonable. In such instances, the Commission may adjust an existing rate to make it reasonable under current conditions. A contract between a utility and a customer, moreover, does not bind the Commission. See *Board of Education v. William Dohrman, Inc.*, 620 S.W.2d328 (Ky.App. 1981). Mr. Wuetcher also noted that a rate on file with the Commission is presumed to be reasonable. If South Shore challenges the reasonableness of an existing rate, it will bear the burden of demonstrating to the Commission that the existing rate is unreasonable and requires modification.

As to quantity limitations, Mr. Wuetcher noted that quantity limitations were permissible, but could prove difficult to enforce. Shutting off service when a customer had exceeded its requirement is not very practical and may force unnecessary hardships on the customers of the wholesale customer. He suggested that parties consider penalty rates that would become effective when a purchaser has exceeded its contract volume or more than a certain percentage of its contract volume (e.g., 110 percent of contract volume). Such rates would provide a financial incentive to avoid exceeding contact volumes.

Finally, Mr. Wuetcher noted that Commission Staff has previously conducted wholesale rate studies for small municipal utilities. Such studies have served as the basis for an agreed rate between municipal utilities and their wholesale customers. Mr. Wuetcher suggested that the parties consider requesting such study if, in the future, it is unable to reach an agreement on a wholesale rate or desires an independent review of the rate outside of litigation.

The conference call then concluded.

cc: Parties of Record