

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeem G. Kelly.

Kentucky Utilities Company

Docket No. EL04-117-000

ORDER DENYING REQUEST FOR DECLARATORY ORDER

(Issued October 8, 2004)

1. Kentucky Utilities Company (Kentucky) filed a petition for a declaratory order, requesting that the Commission take jurisdiction over a contract dispute pending in a federal district court. Kentucky contests the terms and conditions of a wholesale electricity contract that is on file here. For the reasons stated below, we will deny Kentucky's petition for a declaratory order and allow the matter to be decided in federal court. This order benefits customers by having the dispute settled in the most appropriate venue.

Background

2. Kentucky and Owensboro Municipal Utilities (Owensboro) are parties to a longstanding wholesale electricity contract that includes rates, terms, and conditions of service for certain wholesale sales of electric energy in interstate commerce. Under the contract, according to Kentucky, Owensboro sells excess supply from a particular generating station to Kentucky, Kentucky dispatches that station, and in turn Kentucky sells backup energy to Owensboro at a rate that reflects the "incremental energy cost" of Kentucky's system.¹ Owensboro agreed to pay a 20 percent reserve requirement and Kentucky agreed, in return, to charge Owensboro only the incremental energy cost for backup energy. Kentucky further agreed that if its reserves were inadequate, Kentucky would purchase the promised energy and would charge Owensboro only the actual cost of such purchased energy, excluding any demand charge.

¹ The contract also requires Kentucky to sell backup energy to Owensboro during periods of forced outages, unit derates, and scheduled maintenance when Owensboro cannot supply its customers from its own resources.

3. Earlier this year, Owensboro filed suit against Kentucky in the Commonwealth of Kentucky's Daviess Circuit Court.² Kentucky subsequently removed the case to the U.S. District Court for the Western District of Kentucky, Owensboro Division. Concurrently, Kentucky filed the instant petition for a declaratory order.

4. In its petition, Kentucky states that Owensboro asked the Daviess Circuit Court to impose a reserve margin on Kentucky although Kentucky claims there is no such requirement under the contract, and requests that the Commission so declare. Kentucky acknowledges that the contract mentions reserve requirements, but argues that this does not support Owensboro's position.

5. Kentucky next states, and requests that the Commission find, that the contract requires that if Kentucky purchases energy in order to provide backup energy to Owensboro, the rate Kentucky charges Owensboro for that energy must reflect the actual cost to Kentucky, excluding any demand charge, plus seven percent for transmission losses. Kentucky also asserts that Owensboro has not paid bills that are due.

6. As a jurisdictional matter, Kentucky argues first that the Commission has exclusive jurisdiction, and alternatively that the Commission has primary jurisdiction. Kentucky's basis for claiming exclusive jurisdiction is that "the heart of the matter goes to setting rates and ensuring that utility practices are just and reasonable and not unduly discriminatory." Kentucky maintains that the facts of the case satisfy the three-part test that the Commission set forth in *Arkansas Louisiana Gas Co. v. Hall*, 7 FERC ¶ 61,175 at 61,332, *reh'g denied*, 8 FERC ¶ 61,031 (1979) (*Arkla*).

Notice of Filings and Responsive Pleadings

7. Notice of Kentucky's filing was published in the *Federal Register*, 69 Fed. Reg. 45,703 (2004) with interventions or protests due on or before August 12, 2004. Owensboro filed a motion to intervene and protest. Kentucky then filed an answer, after which Owensboro filed an answer to Kentucky's answer.

8. In general, Owensboro contends that the issues are contract interpretation and enforcement matters, not an attempt to modify a filed rate. It argues, therefore, that the Commission's jurisdiction is not exclusive but is concurrent with that of the court.

9. Owensboro states that Kentucky's first argument is a red herring; that Owensboro raised the reserve issue merely to explain how the pricing provisions for backup energy should be understood and applied within the context of the contract as a whole.

² A copy of the complaint is attached to Kentucky's petition at Appendix A.

Owensboro acknowledges that the contract does not specify a particular percentage level of reserves that Kentucky must maintain and states that it does not seek to apply or enforce any such specific reserve obligation on Kentucky, either as such an obligation would relate to Owensboro or otherwise.

10. As for backup energy, Owensboro states that many sellers no longer use two-part rates with a separately stated demand charge, and that Kentucky wants to pass through the entire purchase price, including demand and energy charges. Instead, Owensboro argues, when Kentucky is required to go to the market to purchase power in order to honor its backup energy obligation to Owensboro, Kentucky should absorb the costs that are charged by third-party sellers to recover their fixed costs, passing through only the incremental energy charges. “The crux of [Owensboro’s] position is that the Contract requires [Kentucky] to exclude the demand charge (or fixed cost) component of power that is purchased at market prices, *i.e.*, the portion of the price in excess of the ‘incremental energy cost,’ regardless of whether that demand charge is separately stated.” Owensboro requests that the Commission set the matter for hearing and initiate alternative dispute resolution procedures.

11. Owensboro asserts that it has paid in full for the backup energy services provided by Kentucky, and that Kentucky’s demand for more money arises from Kentucky’s flawed interpretation of the contract.

12. As for jurisdiction, Owensboro provides a lengthy analysis of the jurisdictional question and argues that the Commission has concurrent jurisdiction and should defer to the court, as the case is a controversy over contract interpretation.

Discussion

13. Pursuant to Rule 214 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2004), the timely, unopposed motion to intervene serves to make Owensboro a party to this proceeding. Rule 213(a)(2) of the Commission’s Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2004), prohibits an answer to a protest and an answer to an answer unless otherwise ordered by the decisional authority. We are not persuaded to accept Kentucky’s Answer or Owensboro’s Answer to Kentucky’s Answer and will, therefore, reject them.

14. The instant case is a contract interpretation dispute. We use a three-part test for deciding whether to assert primary jurisdiction, which is set forth in *Arkla*, *supra* P 6:

(1) whether the Commission possesses some special expertise which makes the case peculiarly appropriate for Commission decision; (2) whether there is a need for uniformity of interpretation of the type of question raised in the dispute; and, (3) whether the case is important in relation to the regulatory responsibilities of the Commission.³

15. Based on the application of the *Arkla* factors, we find that the contract dispute between Kentucky and Owensboro does not warrant assertion of the Commission's primary jurisdiction. We find that we do not possess special expertise beyond that of a federal district court in this matter. Construing the contract's provisions and inquiring into the parties' intent is a straightforward matter of contract interpretation that is better left to the district court. There is also no need for uniform interpretation of the contract language at issue here. This is merely a contract dispute between two parties over the appropriate compensation for backup energy services. Finally, while this is a matter of significance to the parties, it is not important in relation to the regulatory responsibilities of the Commission.

16. We are satisfied that analysis of each *Arkla* factor leads to the conclusion that the dispute does not require assertion of the Commission's primary jurisdiction. The dispute involves a matter of contract interpretation that is best left to the district court. Therefore, we will deny Kentucky's petition for declaratory order.

The Commission orders:

Kentucky's petition for declaratory order is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.

³ *Arkla*, 8 FERC ¶ 61,031 at 61,332.