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June 1, 2007

Opinion No. 07-86

City of Crossville Franchise Fee

QUESTION

Is the City of Crossville authorized to charge a franchise fee to a private company providing utility service in newly annexed territory, where that territory is in the service area of a utility district?

OPINION

Ordinarily, under Tenn. Code Ann. § 6-51-111(d), the private utility and the utility district must agree in writing to adjustments in the utility district's service area. If the private utility and the utility district cannot reach an agreement, the utility district's service area remains unchanged, and the private utility may not provide utility service within that area even though the area now falls within the city limits. Under these circumstances, the city may not authorize the private utility to provide service in the area and, therefore, may not charge the private utility a franchise fee with respect to that area. The fact that the private company may already have been providing service within the utility district's service area would probably not change the result under Tenn. Code Ann. § 6-51-111(d). In addition, federal law protects the rights of rural utilities that have obtained loans from the Farmers' Home Administration or its successor agencies. 7 U.S.C. § 1926(b). If this statute is applicable to the utility district, then it would also affect the rights of the city, the private utility, and the utility district with regard to utility service in the annexed territory.

ANALYSIS

This opinion concerns the authority of the City of Crossville to charge a franchise fee to a private company under the following circumstances. The Crossville City Charter authorizes the city to grant non-exclusive franchises of public utilities and public service to be furnished to the city. Crossville City Charter, Art. III, § 1(13). The Tennessee Regulatory Authority also has general supervisory authority over privately owned utilities, including their franchises. Tenn. Code Ann. §§ 65-4-105, -107 & -108. The City of Crossville recently annexed land in Cumberland County. The land was located in the service area of a utility district. But the owner of the land had obtained utility service from a private company even though the utility district was already providing service in the area. The private company was also providing service within the Crossville city limits. We assume the private company has been operating within the city limits under an agreement with the city, and that the question refers to the city's right to charge a franchise fee with respect to service

in the newly annexed territory. It is unclear from the request whether the private company began providing service to customers within the newly annexed territory before or after the annexation was completed. In either case, the relevant legal principals are as follows.

This issue is governed, first, by the city's rights with respect to utility services in newly annexed territory. Tenn. Code Ann. § 6-51-111 addresses adjustments to utility service in territory that a city has annexed. The statutes protect a public utility already providing service in the annexed territory. The statute provides in relevant part:

> (a) Upon adoption of an annexation ordinance or upon referendum approval of an annexation resolution as provided in this part, *an annexing municipality and any affected instrumentality of the state of Tennessee, including, but not limited to, a utility district . . . shall attempt to reach agreement in writing for allocation and conveyance to the annexing municipality of any or all public functions,* rights, duties, property, assets and liabilities of such state instrumentality that justice and reason may require in the circumstances. . . . *The annexing municipality, if and to the extent that it may choose, shall have the exclusive right to perform or provide municipal and utility functions and services in any territory that it annexes, notwithstanding § 7-82-301 or any other statute,* subject, however, to the provisions of this section with respect to electric cooperatives.
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> (b) Subject to such exclusive right, any such matters upon which the respective parties are not in agreement in writing within sixty (60) days after the operative date of such annexation shall be settled by arbitration with the laws of arbitration of the state of Tennessee effective at the time of submission to the arbitrators, and § 29-5-101(2) shall not apply to any arbitration arising under this part and § 6-51-301. The award so rendered shall be transmitted to the chancery court of the county in which the annexing municipality is situated, and thereupon shall be subject to review in accordance with §§ 29-5-113 — 29-5-115 and 29-5-118.
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> (c)(1) If the annexed territory is then being provided with a utility service by a state instrumentality that has outstanding bonds or other obligations payable from the revenues derived from the sale of such utility service, the agreement or arbitration award referred to in subsections (a) and (b) shall also provide that:
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> (A) The municipality will operate the utility property in such territory and account for the revenues therefrom in such manner as not to impair the obligations of contract with reference to such bonds or other obligations; or
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> (B) The municipality will assume the operation of the entire utility system of such state instrumentality and the payment of such bonds or other obligations in accordance with their terms.

> (2) Such agreement or arbitration award shall fully preserve and protect the contract rights vested in the holders of such outstanding bonds or other obligations.
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> (d)(1) Notwithstanding the provisions of any law to the contrary, *if a private individual or business entity provides utility service within the boundaries of a municipality under the terms of a privilege, franchise, license, or agreement granted or entered into by the municipality, and if the municipality annexes territory that includes the service area of a utility district, then such private individual or business entity and the utility district shall attempt to reach agreement in writing for allocation and conveyance to such private individual or business entity of any or all public functions, rights, duties, property, assets, and liabilities of such utility district that justice and reason may require in the circumstances. If an agreement is not reached, then notwithstanding the change of municipal boundaries,* ***the service area of the utility district shall remain unchanged, and such private individual or business entity shall not provide utility service in the service area of the utility district.***

(Emphasis added). Under subsection (e), the annexing city may also purchase a public utility system then providing service in the annexed territory.

In this situation, the city has annexed property that is within the service area of a public utility district. A privately owned utility has been providing service within the city limits under an agreement with the city. Under § 6-51-111(d), the private utility and the utility district must agree in writing to adjustments in the utility district's service area. If the private utility and the utility district cannot reach an agreement, the utility district's service area remains unchanged, and the private utility may not provide utility service within that area even though the area now falls within the city limits. Under these circumstances, the city may not authorize the private utility to provide service in the area and, therefore, may not charge the private utility a franchise fee with respect to that area.

The request indicates that the private utility may already have extended service to at least one customer in the service area of the utility district. The statute does not address the rights of the parties under those circumstances. Generally, once it furnishes services, a utility district is the sole public corporation authorized to furnish these services in its service area, subject to the annexation laws. Tenn. Code Ann. § 7-82-301(a)(1). Ordinarily, only the county mayor may change the exclusive service territory of a utility district after a public hearing. *Id.*; *see also Town of Rogersville ex rel. Rogersville Water Commission v. Mid-Hawkins County Utility District*, 122 S.W.3d 127 (Tenn. Ct. App. 2003), *p.t.a. denied* (2003). However, a utility district may forfeit its right to challenge the authority of other utilities to provide services within its service area by failing to assert its rights in a timely manner. *Whitehaven Utility District v. Ramsay*, 215 Tenn. 435, 387 S.W.2d 351 (1964). In that case, the Tennessee Supreme Court found that the equitable principle of *laches* barred a utility district from challenging the right of two other public utilities to provide service in the district's service area. The district had allowed the two utilities to construct facilities and provide

service for eight years before bringing the action. Whether the utility district in this situation has forfeited its exclusive right by allowing the private company to provide service within its service area would depend on all relevant facts and circumstances. Even if this were the case, under Tenn. Code Ann. § 6-51-111(d), the utility district would still retain exclusive rights in the rest of the annexed service area. Further, the effect of the forfeiture would be to prevent the utility district from challenging the service; it would not give the city any additional rights to authorize that service under Tenn. Code Ann. § 6-51-111(d). For this reason, the fact that the private company has already been providing service within the utility district's area would probably not change the result under this statute.

In addition, federal law protects the rights of rural utilities that have obtained loans from the Farmers' Home Administration or its successor agencies. 7 U.S.C. § 1926(b). This statute provides in relevant part:

> The service by or made available through any such association shall not be curtailed or limited by the inclusion of the area within the boundaries of any municipal corporation or other public body, *or by the granting of any private franchise for similar service within such area during the term of said loan*; nor shall the happening of such event be the basis of requiring such association to secure any franchise, license or permit as a condition to continuing to serve the area served by the association at the time of the occurrence of such event.

If this statute is applicable to the utility district, then it would also affect the rights of the city, the private utility, and the utility district with regard to utility service in the annexed territory. The statute is further discussed in *Town of Rogersville ex rel. Rogersville Water Commission v. Mid-Hawkins County Utility District*, 122 S.W.3d at 140-142.

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