THE UNIVERSITY of TENNESSEE
INSTITUTE for PUBLIC SERVICE
MUNICIPAL TECHNICAL ADVISORY SERVICE

MEMORANDUM

Date: September 3, 2012

To: Sharon Rollins, Technical Consulting Program Manager

From: Sid Hemsley, Legal Consultant

Subj: Can the Utility Board be given the authority to set water rates?

The City has the following question: Can the city's utility board be given the authority to set water rates? Under the facts, the City established the Board of Public Utilities under the Electric Power Plant Law of 1935. In 1941, the city transferred to the Board of Public Utilities the Water System, with "all of the powers, duties and responsibilities placed upon the Board of Waterworks and Sewer Commissioners by Public Acts 1933, Chapter 68." However, the Board of Public Utilities sets the electric rates, while the City Council sets the water rates.

The answer is no.

That answer derives from the Municipal Electric Plant Law of 1935, specifically Tenn. Code Ann., § 7-52-111 under which the city's electric utility is established, and two cases that interpret that statute. That statute provides that municipalities are authorized to turn over the operation of their water and sewer works to the electric utility board, but if it does so it must "keep separate accounts for the electric plant and each works, making due and proper allocation of all joint expenses, revenues and property valuations." At first glance that statute authorizes the utility board to have "jurisdiction over the water system's rate-making, the same as it has jurisdiction over electrical rate-making." In fact, I have previously issued that opinion. But in Tennessee Electric Power Co. v. Mayor and Aldermen of Fayetteville, 114 S.W.2d 811 (1938), the Tennessee Supreme Court declared that:

> It will be observed that in the above-quoted portion of section 13 [which is now Tenn. Code Ann. § 7-52-111] the Legislature, with regard to the management of sewerage and waterworks, did not confer jurisdiction upon the "board of public utilities," which it could have done. It did say that municipalities operating an

> electric plant under the act might do so. Such municipalities most likely were already vested with that power. The object of the Legislature was not to confer additional authority upon municipalities, but to require them to keep the revenue derived from their power plant separate from other revenue. The Legislature realized that a municipality, as a matter of convenience and economy, might confer upon the "board of public utilities," the operation or management of its sewerage and waterworks theretofore exercised by some other board or commission, and simply expressed its assent thereto upon condition that "it shall keep separate accounts for the electric plant and each works." *The Legislature, in our opinion, was legislating solely with regard to the electric plant**, and was not attempting in any manner to amend, modify or repeal any statutes pertaining to sewerage or waterworks. It did not empower municipalities to confer such jurisdiction on the "board of public utilities."*** In saying that municipalities "may" confer upon the board the "jurisdiction" over waterworks and sewerage works, the word *may* was used to indicate possibility not permission. As we say, he may live, or he may die, meaning that it is possible that he may live, or it is possible that he may die, not that we permit him to live, or that we permit him to die. Taking the Act of 1935 in its entirety, we readily concede that the construction we have given it accords with the legislative will. It is an elementary principle that if a statute is susceptible of two reasonable constructions, one that will sustain its constitutionality and one that will destroy the act, it is the duty of the court to adopt the construction which will preserve the law…[At 813-14] [Emphasis is mine.]

That language appears to stand for the proposition that any statute or statutes under which the water system was organized was preserved, that no jurisdiction to change those statutes was intended by the Electric Power Plant Law of 1935. Maury County Board of Public Utilities v. City of Columbia, 854 S.W.2d 890 (Tenn. Ct. App. 1993) supports that proposition. There the court separated the power to contract and the power to set rates under Tenn. Code Ann. § 7-35-401 et seq. The Columbia Board of Public Utility had entered into contracts with several municipalities to provide them water service, but subsequently argued that the contracts were invalid, they having been executed by the Public Utility Board rather than by the city's governing body, and that the contracts prevented the city from raising water rates. The city acknowledged that the Board of Public Utilities "has operated CWS [Columbia Water System] pursuant to city ordinance No. 51 and T.C.A. § 7-35-401 et seq., since the 1930's." But that statutory scheme, declared the court, "gives to the Board broad powers to operate CWS, including the power to contract." [At 891] But as the court, citing Tenn. Code Ann. § 7-35-412, concluded, that statute itself reserves some powers to the city's governing body:

> The board of waterworks and/or sewerage commissioners…has the power to take all steps and proceedings and to make and enter into all contracts and agreements necessary or incidental to the performance of its duties and the execution of its powers under this part, *subject only to limitations on matters requiring approval by the governing body of the city or town in question…"* [At 891] [Emphasis is mine]

Among those limitations on the Board of Public Utilities under that statute, said the court, was the power to set rates; that power rested in the city's governing body. Under Tenn. Code Ann. § 7-35-416, continued the court, the city even also has the power to contract for water services directly with other cities.

Title 18, Chapter 3 of the Columbia Municipal Code itself provides that:

> There is vested in the "Board of Public Utilities," all of the powers, duties and responsibilities placed upon the Board of Waterworks and Sewerage Commissioners by Pub. Acts 1933, Ch. 68 [now Tenn. Code Ann., Title 7, Chapter 35, Part 4] and the "Board of Public Utilities is hereby granted jurisdiction over the waterworks plant, distribution system, all real estate, or interest in real estate, all personal property, and all equipment and other things appertaining thereto; provided, however, that the funds received from the operation of the waterworks system shall at all times be kept separate and handled in the manner provided under said Pub. Acts 1933, Ch. 68, and provisions of the waterworks revenue bond ordinances. (1968 Code, § 13-1-1, modified). [Section 18-301]

Note that nothing is said in that grant of jurisdiction over the waterworks to the utility about the setting of rates, which, as Maury County Board of Public Utilities, above, pointed out, is controlled by Tenn. Code Ann. § 7-35-414, and which sets the rate-making power in the city's governing body. Indeed Section 18-302 of the Columbia Municipal Code, entitled "Rates, rules and regulations and definitions," provides that water rates are contained in Chapter 3.

I think that the City could probably remove its water system from under Tenn. Code Ann. § 7-35-401 et seq. However, that may not be so if the city has issued bonds predicated on the establishment and operation of the water system under that statute. In State ex rel. Barr v. Town of Selmer, 417 S.W.2d 532 (Tenn. 1967), the Selmer Board of Sewers and Waterworks Commissioners operated the water, sewer and gas system of the city. But the city's board of mayor and aldermen took over the operation of all three systems, after the gas system had issued bonds under the Revenue Bond Law. Bondholders protested the takeover, arguing that it was prohibited under the bond covenants. Those covenants provided, "That for the purpose

of assuring the efficient, impartial and nonpolitical operation of said system for the benefit of the municipality and the holders of the bonds from time to time outstanding, the complete and independent control and operation of the system shall be vested in the Board of Waterworks and Sewerage Commissioners of the municipality…. [At 533] The court agreed, holding that the bond covenants were a contract between the city and the bond holders, and that for as long as such bonds were outstanding the gas system was required to remain under the control of the Board of Waterworks and Sewerage Commissioners.