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May 18, 2004

VIA HAND DELIVERY

Ms Deborah Taylor Tate, Chairman
TENNESSEE REGULATORY AUTHORITY
460 James Robertson Parkway
Nashville, Tennessee 37243

Re: ***Petition of Tennessee Wastewater Systems, Inc. to Amend its Certificate of Convenience and Necessity*, Docket No. 03-00329**

Dear Chairman Tate:

Enclosed for filing in the above-referenced docket are the original and thirteen copies of the Memorandum of Law by the City of Pigeon Forge, Tennessee.

Should you have any questions with respect to this filing, please do not hesitate to contact me at the number shown above. Thank you in advance for your assistance with this matter.

Yours truly,

G. Scott Thomas

G Scott Thomas

GST/rk
Enclosure

cc. Jim Gass, Esq. (w/enclosure)
Ms. Sharla Dillon (w/enclosure)

IN THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

IN RE:	)	
	)	
PETITION OF ON-SITE SYSTEMS, INC. TO	)	**Docket No. 03-00329**
AMEND ITS CERTIFICATE OF	)	
CONVENIENCE AND NECESSITY	)	

MEMORANDUM OF LAW BY THE CITY OF PIGEON FORGE

Issue Presented

On May 10, 2004, the Hearing Officer in this case, Randal L. Gilliam, issued a Notice of Filing and Status Conference in this docket.[1] In the Notice of Filing and Status Conference, Mr. Gilliam requested a Memorandum of Law on the following issue:

> Whether the grant of a Certificate of Convenience and Necessity to a public utility (as defined by Tenn. Code Ann. § 65-4-101) providing wastewater treatment services in an identified service area operates to exclude other public utilities or non-utilities (as defined by Tenn. Code Ann. § 65-4-101) from providing wastewater treatment services in the identified service area.

The City of Pigeon Forge is a non-utility under T.C.A. § 65-4-101 and its discussion is thus limited accordingly.

Discussion

1. A certificate of public convenience and necessity in favor of Tennessee Wastewater Systems cannot exclude the City of Pigeon Forge from providing wastewater service within an annexed portion of the identified service area.

1 This docket has been consolidated with Docket No 04-00045

All parties to this action agree that it is well-settled law that within its boundaries a municipality has the power to provide utility services itself, or choose which parties will provide utility services, regardless of whether a public utility has a certificate of convenience and necessity in the area to be served "Municipalities in Tennessee have the right to grant exclusive franchises for public utilities and public services, regardless of the form of the municipal government." City of South Fulton v. Hickman-Fulton Counties Rural Elec. Coop., 976 S.W.2d 86, 89 (Tenn. 1998). As to sewer systems specifically, "the establishment and maintenance of a sewer system by city is ordinarily regarded as an exercise of its police power." Campbell v. City of Knoxville, 505 S.W.2d 710, 711 (Tenn. 1974) and Patterson v. City of Chattanooga, 241 S.W.2d 291, 294 (Tenn. 1951) (citing McQuillan, Municipal Corporations, Sec. 1545). See also, Zirkle v. City of Kingston, 396 S.W.2d 356, 360 (Tenn. 1965) (setting forth several Tennessee Code provisions applicable to a municipality's power to maintain and operate a sewer system). Under the Tennessee annexation statutes, when a municipality chooses to provide "utility water service" within its municipal boundaries, and all or part of such area is included within the scope of a certificate of convenience and necessity, the municipality may exercise its powers of eminent domain with regard to any existing sewer "facilities." See, T.C.A. § 6-51-301(a)(1)-(2). The Tennessee Court of Appeals, though not directly holding such, has assumed that the term "utility water service" includes sewer service within the scope of the § 301. Lynnwood Utility Corp. v. City of Franklin, No. 89-360-II, 1990 WL 38358, at *3 (Tenn. Ct. App. Apr. 6, 1990) (copy attached)[2]

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[2] In the Lynwood case, the Tennessee Court of Appeals decided an action brought by a public utility holding a certificate to provide sewer services in a portion of an area that had been annexed by the City of Franklin The plaintiff had installed and was operating a sewer system for a large, new subdivision, but had no pipes in the ground, had not constructed any plant, had no equipment of any kind, and had not made any physical addition of any kind in the remainder of the annexed area Nevertheless, the plaintiff sued claiming that it deserved compensation solely because it held a certificate and was now deprived of providing sewer service to part of the annexed area The Court of Appeals

2. A certificate of public convenience and necessity from the Tennessee Regulatory Authority may exclude the City of Pigeon Forge from providing service within the identified service area prior to annexation of portions of that service area by the City.

There is a substantial risk that if Tennessee Wastewater Systems receives the certificate of convenience and necessity at issue, the City of Pigeon Forge would be excluded from providing service within the identified service area outside of its city limits. Under Tenn. Code Ann. § 6-51-301(a)(1), "no municipality may render utility water service to be consumed in any area outside its municipal boundaries when all of such area is included within the scope of a certificate or certificates of convenience and necessity . . . in favor of any person, firm or corporation authorized to render such utility water service." For purposes of this memorandum, we may assume that the term "utility water service" includes sewer service within the scope of the § 301(a). See, Lynnwood Utility Corp., 1990 WL 38358, at *3.

A decision of the Tennessee Court of Appeals indirectly addresses whether a municipality is excluded under T.C.A. § 6-51-301(a)(1) from providing utility water service to an area outside of its boundaries. See, Westland Drive Service Co. v. Citizens & Southern Realty Investors, 558 S.W.2d 439 (Tenn. Ct. App. 1977). In this case, the Knoxville Utilities Board ("KUB") began to provide water services in 1972 to an apartment complex, Timbers West, constructed immediately adjacent to and outside of the Knoxville corporate limits. Westland had earlier obtained a certificate of convenience and necessity from the Tennessee Public Service Commission ("Commission") granting Westland an exclusive franchise to provide services throughout its certified area, which included the

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held that the certificate did not qualify as "facilities" under T C A § 6-51-301(a)(2) and that plaintiff's compensation therefore did not exceed zero In dicta, the court noted that a certificate holder possesses an intangible right to provide

site of the apartment complex. After KUB began providing water services to Timbers West, Westland filed a complaint before the Commission in 1973. The Commission simply reaffirmed that Westland had an exclusive franchise. However, because the Commission had no jurisdiction over KUB and Timbers West, the Commission's order instructed Westland to "proceed in a court of equity to insure that its franchise area is not infringed upon by KUB . ."

In 1975, Westland brought a lawsuit seeking to enjoin KUB from furnishing water to the apartment complex pursuant to T.C.A. § 6-51-301(a)(1) (then, § 6-319). The Chancellor dismissed the lawsuit in favor of KUB, apparently because "it would be inequitable and unjust to require Timbers West to disconnect from KUB's service and hook on to Westland's facilities." The Court of Appeals affirmed the dismissal, but solely on the grounds that the language in the first sentence of § 6-51-301 did not come into effect until April 5, 1974 – nearly two years after KUB began providing water service to Timbers West. Therefore, prior to the enactment of the provision, "it was not a violation of the Tennessee statutes for KUB to serve Timbers West." Because the 1974 amendment could not apply retroactively, it "would have no effect on KUB and Timbers West's valid 1972 agreement."

The clear implication of this decision is that, from 1974 forward, the language in the above-quoted first sentence of T.C.A. § 6-51-301(a) excludes a municipality from providing sewer service to an area outside its municipal boundaries when such area is already within the scope of a certificate of convenience or necessity.

Although the Tennessee Regulatory Authority ("Authority") itself cannot prohibit a municipality from serving in an certificated area, the Authority must be mindful in considering

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sewer services, which might have value in the context of the eminent domain laws, but that the certificate holder is only entitled to damages that may not exceed the replacement cost of the facilities under §301(a)(2)

whether to grant a certificate that T.C A. § 6-51-301 may exclude a municipality from providing sewer service in the certificated area outside the municipal boundaries. The Authority's actions in granting broad, "blanket" certificates can have significant consequences for a municipality when it seeks to expand municipal sewer service in anticipation of urban growth and subsequent annexation. The Authority clearly possesses the discretion to consider these potential issues when deliberating on a certificate application. See, T.C.A. § 65-4-201 (stating that a certificate is based on considerations of future public convenience and necessity).

There is a possible exception to the prohibition in the first sentence of T.C.A. § 6-51-301 when a municipality has established sewer service outside of its boundaries in an urban growth area that is then *later* included within a scope of a certificate's area. Such an exception is consistent with the Authority's certification statutes. Under T.C.A. § 65-4-201, a public utility cannot establish service in a territory already receiving that utility service without a certificate; *provided that* the a public utility need not obtain a certificate for an extension in territory where it has already lawfully commenced operations or into territory contiguous to its existing utility system. Likewise, a municipality, which has at least the same rights as a public utility, should be able to expand its utility service in areas outside its boundaries where it has already lawfully commenced operations.

This interpretation of the prohibition in § 6-51-301 is much more consistent with several other Tennessee statutes and case law that allow a municipality to extend its water service outside of its borders, irrespective of a certificate of convenience or necessity. The Tennessee Supreme Court "has on numerous occasions approved the rule above announced, that a city may own and operate such [sewer systems] beyond its corporate limits." Patterson, 241 S W.2d 291, 294 (citing prior decisions). Under T.C.A. § 6-54-109, it is not unlawful for a municipal corporation chartered to

supply water to acquire franchises or property of any similar corporation in such city or town and in the territory adjacent to the same. Under Tennessee's Revenue Bond Law, a municipality may operate and maintain any public works for the use and benefit of persons located outside the territorial boundaries of such municipality. T.C.A. § 7-34-104(a)(2). According to T.C.A. § 7-35-401(a), every incorporated city is authorized to operate and maintain within and/or without the corporate limits of such city a waterworks system and/or sewerage system.

Moreover, under the Authority's own certificate of convenience and necessity statutes, a municipality is not required to obtain a certificate for any project or development, and a municipality may determine that the provisions of the certificate statutes do not apply where a municipality, by resolution or ordinance, declares that a public necessity requires competition within that municipality. T.C.A. §§ 65-4-202, 207(a). The Revenue Bond Law is in accordance, stating that it is not necessary for any municipality to obtain a certificate of convenience or necessity in order to extend, maintain or operate any public works. T.C. A. § 7-34-106.

Some Tennessee statutes are more consistent with the prohibitory language in the first sentence of § 6-51-301(a), however. For example, even though T.C.A. § 7-51-401(a) states that each municipality is authorized to extend sewage collection and treatment services beyond its boundaries to customers desiring such service, § 7-51-401(c) states that no such municipality shall extend its services into sections of roads or streets already occupied by other public agencies rendering the same service, so long as such other public agency continues to render such service. See, Whitehaven Utility District v. Ramsay, 384 S.W.2d 351 (Tenn. 1964); Tenn. AG Opinion No. 01-125 (8/7/01).

Conclusions

It is well-settled (and agreed upon by all parties hereto) that a municipality has absolute

power to provide utility service within an area that it has annexed. There is a significant risk, however, that a municipality may be excluded from extending its utility services into an urban growth area slated to be annexed in the future if a public utility holds a certificate that covers the urban growth area. This issue is within the Authority's discretion to consider when deliberating on a certificate application, and the Authority should exercise such discretion in the current action.

Dated this 18 day of May, 2004.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that the above and foregoing Memorandum has been served upon the following persons on this 18 day of May, 2004 by U.S. Mail, postage prepaid:

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1990 WL 38358
118 P.U R.4th 288
(Cite as: 1990 WL 38358 (Tenn.Ct.App.))

SEE COURT OF APPEALS RULES 11 AND 12

Court of Appeals of Tennessee, Middle Section at Nashville.

LYNNWOOD UTILITY COMPANY,
Plaintiff-Appellant.
v.
THE CITY OF FRANKLIN, TENNESSEE,
Defendant-Appellee.

April 6, 1990.

Appeal No. 89-360-II, Williamson Equity, Appealed from the Chancery Court for Williamson County, Henry Denmark Bell, Chancellor.

Harris A Gilbert, J. Graham Matherne, Wyatt, Tarrant, Combs, Gilbert & Milom, Nashville, for plaintiff-appellant.

William L. Baggett, Jr., Farris, Warfield & Kanaday, Nashville, Charles W. Burson, Attorney General and Reporter, John Knox Walkup, Solicitor General, Michael W. Catalano, Deputy Attorney General, Nashville, for defendant-appellee.

OPINION

LEWIS, Judge.

*1 Plaintiff Lynnwood Utility Company (Lynnwood) filed its complaint against defendant, The City of Franklin, Tennessee (Franklin), in which Lynnwood sought compensation from Franklin for Franklin's alleged taking of Lynnwood's right to serve an area in North Williamson County, Tennessee, with utility **sewer** service. Franklin had annexed the area in question subsequent to the Tennessee Public Service Commission (PSC) granting Lynnwood a "Certificate of Convenience and Necessity" to provide utility **sewer** service to the area in question.

Following the filing of Franklin's answer, Lynnwood moved for partial summary judgment pursuant to Tenn.Code Ann. § 6-51-301, *et seq* Thereafter, Franklin moved for summary judgment on the grounds (1) that Lynnwood was not entitled to rely on Tenn Code Ann. § 6-51-101, *et seq*, (2) that even if Tenn Code Ann. § 6-51-101, *et seq.* were applicable, Lynnwood's damages under Tenn.Code Ann § 6-51-101 would be zero, (3) that Franklin had complied with Tenn.Code Ann. § 65-4-207 and therefore no legal dispute existed between Franklin and Lynnwood, (4) that Lynnwood had no constitutional taking claim, and (5) that public policy considerations dictate that Franklin be permitted to serve the disputed area without payment of compensation to Lynnwood.

The trial court thereafter took the matter under advisement and, on 29 December 1988, entered an order overruling Lynnwood's motion for partial summary judgment and sustaining Franklin's motion for summary judgment on grounds (1), (2) and (3)

Lynnwood filed a petition to rehear the 29 December 1988 order and moved the trial court to reach the constitutional issues which it had raised in its pleadings and which had arisen because of the nature of Franklin's motion for summary judgment In conjunction with its petition to rehear, Lynnwood also moved that the Tennessee Attorney General be made party defendant in order to fully bring before the court the issues concerning the constitutionality of Tenn.Code Ann. § 6-51-301

On 7 July 1989, the trial court denied all of Lynnwood's motions. Lynnwood has properly perfected its appeal.

The facts pertinent to our inquiry are as follows.

Lynnwood is a privately-owned **sewer** utility company and subject to the rules of the PSC. Tenn Code Ann. § 65-4-101.

In June 1976, Lynnwood applied for and was

granted a Certificate of Public Convenience and Necessity to serve the Cottonwood Development and Drainage Basin of the Lynnwood Branch in northern Williamson County. Since the issuance of its Certificate, Lynnwood has been operating in its designated service district, providing **sewer** service to a large residential development, as well as other customers within its designated service area. Lynnwood had not extended its system to certain undeveloped areas of its designated service district, but had never refused to do so. Lynnwood has never been requested to provide **sewer** service to these undeveloped areas.

In 1986, Lynnwood petitioned the PSC for an increase in its rates and tap fees. During the hearing on its petition, Lynnwood stated that no new customers were expected in its existing service area. It also developed that Lynnwood did not have any excess capacity in its **sewer** treatment facilities In order to serve other customers, additional capacity would have been needed.

***2** In the Summer of 1986, Harlon East Properties (Harlon), a Raleigh, North Carolina based land development Company, commenced negotiations with owners of property in northern Williamson County The property was undeveloped and a large portion of the property was in Lynnwood's utility service district. The property was open farmland owned by three different owners, and only a few persons resided on the property. No part of the property Harlon wished to purchase contained **sewer** mains, pumping stations, treatment stations, **sewer** lines, or any other type of **sewer** equipment.

Harlon planned to develop this property into a residential development to be known as Fieldstone Farms. A portion of Fieldstone Farms is within Lynnwood's service area.

On 28 October 1986, a referendum election regarding whether the land in question would be annexed by Franklin was passed and 1147 acres were annexed into Franklin.

On 12 November 1986, Lynnwood wrote Harlon requesting a meeting to discuss Lynnwood's providing **sewer** services to that portion of Fieldstone Farms located within Lynnwood's designated service area. A copy of the correspondence was sent to Franklin

On 25 November 1986, Harlon wrote the Mayor of Franklin confirming that the area containing Fieldstone Farms was annexed and acknowledging that Harlon and Franklin had reached a "tentative agreement" that Franklin would provide water and **sewer** services to the annexed area. Harlon requested that Franklin exercise its right to provide water and **sewer** service to the annexed area and also requested Franklin to attempt to reach an agreement with Lynnwood regarding Franklin's providing **sewer** service to Fieldstone Farms.

On 8 December 1986, the Water Committee of the Franklin Board of Mayor and Aldermen unanimously recommended that Franklin provide **sewer** service to the entire newly annexed area.

On 9 December 1986, the Mayor and Board of Aldermen unanimously approved the Water Committee's recommendation with a proviso that Lynnwood be notified of Franklin's intention The 9 December minutes of the Board do not reflect an election by Franklin to exercise exclusive rights to service the annexed area.

On 14 April 1987, the Franklin Board of Mayor and Aldermen passed a resolution declaring its intention to serve the annexed area and confirming the right of Lynnwood to compete for service pursuant to Tenn.Code Ann. § 65-4-207.

Lynnwood's first issue is:

Does T.C.A § 6-51-301 provide a right of compensation for a private **sewer** water utility company's right to serve an area when that utility company holds a Certificate of Convenience and Necessity from the Tennessee Public Service Commission where the utility has operated a **sewer** plant in part of the area for many years, and then an adjoining municipality annexes part of the undeveloped area?"

A. Does T C.A. § 6-51-301 apply only to a purified water utility company and not to a **sewer** water utility company

B. Does T C.A. § 6-51-301 apply only where there have been physical improvements laid into the ground by the **sewer** water company, or does the statute apply to the right to serve the service area lost by the utility when part of its overall service

area is appropriated by the municipality through annexation?

***3** For the purposes of this opinion we assume, without holding, that the term "utility water service" in the statute includes **sewer** service and that the **sewer** service provided by Lynnwood comes within the statute

With that assumption in place, we must determine if Lynnwood, under the undisputed facts, suffered damages as a result of Franklin's election to provide **sewer** service to that portion of the annexed area in which Lynnwood held a Certificate of Convenience and Necessity

The trial court, in granting Franklin's motion for summary judgment, determined that even if Tenn.Code Ann § 6-51-301 did apply to a **sewer** utility provider such as Lynnwood, summary judgment was still appropriate since the amount of damages to which Lynnwood would be entitled would not exceed zero under Tenn.Code Ann. § 6-51-301(a)(2) which provides:

Such proceeding [to determine damages] shall be conducted according to the laws of **eminent domain** , Title 29, Ch. 16, and shall include a determination of actual damages, incidental damages, and incidental benefits, as provided for therein, but in no event shall the amounts so determined exceed the replacement cost of the facilities.

Lynnwood concedes that it has no pipes in the ground, that it had constructed no plant, that it has no equipment of any kind, nor has it made any physical addition of any kind in that portion of the area annexed in which it holds a Certificate of Convenience and Necessity. Lynnwood had not constructed its treatment plant so that it has an over capacity as a result of not being able to serve the annexed area.

Lynnwood only has a Certificate of Convenience and Necessity issued by the PSC and has never provided **sewer** services to the annexed area.

Lynnwood contends that the issue is what is meant by the term "facilities" as used in Tenn.Code Ann § 6-51-301(a)(2) Lynnwood argues that its Certificate of Convenience and Necessity is included within the term "facilities." We respectfully disagree.

We are of the opinion that the term "facilities" as used in Tenn Code Ann. § 6-51-301(a)(2) means physical facilities, not a right to construct physical facilities and not a right to serve an area. We reiterate that Lynnwood has no physical facilities of any kind in or on the annexed area. Further, it cannot be argued that there has been damage to Lynnwood's physical facilities located outside the annexed area. Lynnwood admitted in the hearing before the PSC that its treatment facilities were not presently built to serve excess customers. In other words, Lynnwood has not constructed its physical facilities in anticipation of serving a larger area.

Our search has not revealed any Tennessee authority, and Lynnwood has not cited any Tennessee Authority, to support its argument that its Certificate of Convenience and Necessity, *i e.,* its right to serve the annexed area, is a "facility" which is compensable under the statute

Lynnwood relies on *Hartford Electric Light Co. v. Federal Power Comm'n.,* 131 F.2d 953 (2nd Cir 1942), and *Mississippi Power and Light Co. v. City of Clarksdale,* 288 So 2d 9 (Miss 1973). We are of the opinion that these cases are inapposite to the facts in the case before us.

***4** In *Hartford,* the court found that the plaintiff company's contracts, accounts, memoranda, papers and other records utilized in connection with sales constituted facilities for the purposes of the Federal Power Act, 16 U.S C. § 791(a), *et seq.* Here, none of these items are at issue. Franklin has not attempted to assume operating any of Lynnwood's existing facilities, nor has it attempted to acquire any of Lynnwood's accounts, papers, contracts, etc.

In *Mississippi Power and Light Co.,* the statute did not give the municipality the absolute first right to serve upon annexation. The Mississippi statute contained a "grandfather" provision that favored the original service providers. The court therefore deemed the grandfather franchise a "valuable right." We have no such provision in Tenn Code Ann. § 6-51-301.

A Certificate of Convenience and Necessity is not a facility. However, even if we could find that the Certificate of Convenience and Necessity is

included in the term "facilities," Lynnwood has, under the facts and circumstances of this case, damages which do not exceed zero.

When an area is annexed in which an individual or corporation has a Certificate of Convenience and Necessity and the "municipality chooses to render a utility or water services," the holder of the Certificate is entitled to damages but these damages may not "exceed the replacement cost of the facilities." Tenn.Code Ann. § 6-51-301(a)(2). Lynnwood possesses nothing in the annexed area except the Certificate of Convenience and Necessity, *i.e.*, an intangible "right" to provide **sewer** services. As argued by Franklin, payment of the "replacement costs" of items to be transferred makes no sense in the context of an intangible right to provide **sewer** service

While an intangible right to provide **sewer** services might have some value in the context of the "law of **eminent domain**," Tenn.Code Ann. § 29-16-101, *et seq*, damages under Tenn.Code Ann. § 6-51-301(a)(2) are limited to "replacement costs." There is no replacement cost as contemplated by Tenn.Code Ann. § 6-51-301(a)(2) for an intangible right to provide **sewer** services.

The Chancellor properly granted summary judgment on the ground that the damages Lynnwood suffered did not exceed zero.

In view of our holding under this issue, we deem it unnecessary to address other issues raised by Lynnwood and, therefore, pretermit them.

The judgment of the Chancellor is affirmed with costs assessed to Lynnwood and the cause remanded to the trial court for the collection of costs and any further necessary proceedings.

TODD, P.J , and CANTRELL, J., concur.

1990 WL 38358, 118 P U R.4th 288, 1990 WL 38358 (Tenn.Ct.App.)

END OF DOCUMENT