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DOE/CS/20289-18

STUDY OF THE IMPACTS OF REGULATIONS AFFECTING THE ACCEPTANCE OF INTEGRATED COMMUNITY ENERGY SYSTEMS

PRELIMINARY BACKGROUND REPORT

Public Utility, Energy Facility Siting and Municipal Franchising Regulatory Programs in Kentucky

MASTER

DUANE A. FEURER
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KEVIN J. RIELLEY

January, 1980

WORK PERFORMED UNDER DOE CONTRACT NO.

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UNITED STATES DEPARTMENT OF ENERGY

Division of Buildings and Community Systems
under Contract No. DE-AC02-78CS20289

ABSTRACT

This report is one of a series of preliminary reports describing the laws and regulatory programs of the United States and each of the 50 states affecting the siting and operation of energy generating facilities likely to be used in Integrated Community Energy Systems (ICES). Public utility regulatory statutes, energy facility siting programs, and municipal franchising authority are examined to identify how they may impact on the ability of an organization, whether or not it be a regulated utility, to construct and operate an ICES.

This report describes laws and regulatory programs in Kentucky. Subsequent reports will (1) describe public utility rate regulatory procedures and practices as they might affect an ICES, (2) analyze each of the aforementioned regulatory programs to identify impediments to the development of ICES and (3) recommend potential changes in legislation and regulatory practices and procedures to overcome such impediments.

CHAPTER 1

INTRODUCTION

One response to current concerns about the adequacy of the nation's energy supplies is to make more efficient use of existing energy sources. The United States Department of Energy (DOE) has funded research, development and demonstration programs to determine the feasibility of applying proven cogeneration technologies in decentralized energy systems, known as Integrated Community Energy Systems (ICES), to provide heating, cooling and electrical services to entire "communities" in an energy conserving and economic manner.

The relevant "community" which will be appropriate for ICES development will typically consist of a combination of current energy "wasters" -- i.e., installations with large energy conversion facilities which now exhaust usable amounts of waste heat or mechanical energy -- and current energy users -- i.e., commercial or residential structures which currently obtain electricity and gas from a traditional central utility and convert part of it on customer premises to space heating and cooling purposes.

In most current applications, energy conversion facilities burn fuels such as coal, oil or natural gas to produce a single energy stream, such as process steam or electricity, for various industrial processes or for sale to other parties. However, the technology exists to produce more than one energy stream from most energy conversion processes so that the input of a given amount of fuel could lead to the production and use of far more usable energy than is presently produced. This technology is the foundation of the ICES concept. Current examples of the technology can be found on university campuses, industrial or hospital complexes and other developments where a central power plant provides not only electricity but also thermal energy to the relevant community.

It is generally assumed by DOE that ICES will be designed to produce sufficient thermal energy to meet all the demands of the relevant community. With a given level of thermal energy output, an ICES generation facility will be capable of producing a level of electricity which may or may not coincide with the demand for electricity in the community at that time. Thus, an ICES will also be interconnected with the existing electric utility grid. Through an interconnection, the ICES will be able to purchase electricity when its community's need for electricity exceeds the amount can be produced from the level of operations needed to meet the community's thermal needs. In addition, when operations to meet thermal needs result in generation of more electricity than necessary for the ICES community, the ICES will be able to sell excess electricity through the interconnection with the grid.

ICES may take a variety of forms, from a single owner-user such as massive industrial complex or university campus where all energy generated is used by the owner without sales to other customers, to a large residential community in which a central power plant produces heat and electricity which is sold at retail to residents of the community. Since successful operation of an ICES presupposes that the ICES will be able to use or sell all energy produced, it can be anticipated that all ICES will at some point seek to sell energy to customers or to the electric utility grid from which the electricity will be sold to customers. By their very nature ICES are likely to be public utilities under the laws of many, or even all, states.

The Chicago law firm of Ross, Hardies, O'Keefe, Babcock & Parsons has undertaken a contract with the Department of Energy to identify impediments to the implementation of the ICES concept found in existing institutional structures established to regulate the construction and operation of traditional public utilities which would normally be the suppliers to a community of the type of energy produced by an ICES.

These structures have been developed in light of policy decisions which have determined that the most effective means of providing utility services to the public is by means of regulated monopolies serving areas large enough to permit economies of scale while avoiding wasteful duplication of production and delivery facilities. These existing institutional structures have led to an energy delivery system characterized by the construction and operation of large central power plants, in many cases some distance from the principal population centers being served.

In contrast, effective implementation of ICES depends to some extent upon the concept of small scale operations supplying a limited market in an area which may already be served by one or more traditional suppliers of similar utility services. ICES may in many instances involve both existing regulated utilities and a variety of non-utility energy producers and consumers who have not traditionally been subject to public utility type regulation. It will also require a variety of non-traditional relationships between existing regulated utilities and non-regulated energy producers and consumers.

Ross, Hardies, O'Keefe, Babcock & Parsons is being assisted in this study by Deloitte Haskins & Sells, independent public accountants, Hittman Associates, Inc., engineering consultants, and Professor Edmund Kitch, Professor of Law at the University of Chicago Law School.

The purpose of this report is to generally describe the existing programs of public utility regulation, energy facility siting and municipal franchising likely to relate to the development and operation of an ICES, and the construction of ICES facilities in Kentucky. Attention is given to the problems of the entry of an ICES into a market for energy which has traditionally been characterized by a form of regulated monopoly where only one utility has been auth-implementation of the ICES concept and a series of recommendations for responding to those impediments. orized to serve a given area and to the necessary relationships between the ICES and the existing utility. In many jurisdictions legal issues similar to those likely to arise in the implementation of the ICES concept have not previously been faced. Thus, this report cannot give definitive guidance as to what will in fact be the response of existing institutions when faced with the issues arising from efforts at ICES implementation. Rather, this report is descriptive of present institutional frameworks as reflected in the public record.

Further reports are being prepared describing the determination and apportionment of relevant costs of service, rates of return and rate structures for the sale and purchase of energy by an ICES. Impediments presented by existing institutional mechanisms to development of ICES will be identified and analyzed. In addition to identifying the existing institutional mechanisms and the problems they present to implementation of ICES, future reports will suggest possible modifications of existing statutes, regulations and regulatory practices to minimize impediments to ICES.

This report is one of a series of preliminary reports covering the laws of all 50 states and the federal government. In addition to the reports on individual states, Ross, Hardies, O'Keefe, Babcock & Parsons is preparing a summary report which will provide a national overview of the existing regulatory mechanisms and impediments to effective implementation of the ICES concept and a series of recommendations for responding to those impediments.

CHAPTER 2

REGULATION OF PUBLIC UTILITIES IN KENTUCKY

I. PUBLIC AGENCIES WHICH REGULATE PUBLIC UTILITIES

Until April 1, 1979, the Public Service Commission had been vested with "exclusive jurisdiction over the regulation of rates and service of utilities."1/ As of that date, two new agencies, the Energy Regulatory Commission (ERC) and the Utility Regulatory Commission (URC), have replaced the Public Service Commission. The ERC consists of three full-time members appointed by the governor for four year terms and is responsible for enforcing the provisions of the Kentucky Statutes relating to electric and gas utilities. The three-member URC is responsible for enforcing the provisions relating to non-energy utilities such as telephone, sewer and water utilities.

The statutes vest all regulatory authority over public utilities in either the ERC or the URC. Local governments retain only the power to grant local franchises. However, it should be noted, that any utility owned or operated by a political subdivision of the state is exempt from regulation. Thus, local government has complete authority over utilities which are self-owned.

II. JURISDICTION OF THE ERC AND URC

The ERC has jurisdiction over any "energy utility" which is defined to include any person or corporation, except a city, which owns, controls, operates or manages any facility used in connection with:

(a) The generation, production, transmission or distribution of electricity to or for the public, for compensation, for light, heat, power or other uses;

(b) The production, manufacture, storage, distribution, sale or furnishing of natural or manufactured gas, or a mixture of same, to or for the public for compensation, for light, heat, power or other uses; or

(c) The transporting or conveying of gas, crude oil or other fluid substance by pipeline to or for the public for compensation. . . .2/

The statute does not specifically discuss heating, cooling or steam producing plants.

The URC regulates non-energy facilities which are not relevant to the discussion.3/

"Person" as defined in the statute includes natural persons, partnerships, corporations, and two or more persons having a joint or common interest.4/ "Corporation" includes private, quasi-public and public corporations, and all boards, agencies and instrumentalities thereof, associations, joint-stock companies and business trusts.5/

Before any of the aforementioned utilities become subject to regulation, the statute requires that there must be some type of sale or the receipt of compensation for services produced, transported or distributed "to or for the public." No reported cases have been found interpreting the phrase "to or for the public." An attorney for the Commission has stated, however, that the ERC would probably be without jurisdiction over a geneating installation producing energy for self-consumption or for sale to a limited number of patrons under contract.6/ Under the statutory requirement that service be "to or for the public," any production, generation or storage of energy for private use would be exempt from regulation. The question of the production, generation or storage of energy for the use of tenants is not treated in the statute and has not been resolved by the courts.

By specific statutory provision, municipally-owned utilities are exempt from regulation by the ERC and URC.7/ Although the Kentucky statutes provide that the ERC and URC shall have exclusive jurisdiction over the regulation of rates of utilities, nothing in the statute is intended to limit or restrict the police jurisdiction, contract rights or powers of cities or political subdivisions.8/

Municipal utilities are the only companies specifically exempted from regulatory control. Cooperative associations meeting the "to or for the public, for compensation" requirement must adhere to all rules and regulations imposed and enforced by the ERC and URC.

III. POWERS OF THE ERC AND URC

The powers of the ERC over energy utilities and the URC over non-energy utilities, as specifically enumerated in the statutes, include the power to regulate rates,9/ to control the issuance of securities,10/ to prescribe a system of accounts,11/

to approve agreements or arrangements with other utilities,[12/] to authorize the construction or siting of new plants or the expansion of existing plants,[13/] to allow or compel a utility to make reasonable extensions to new customers,[14/] to issue certificates of convenience and necessity[15/] and to establish and regulate standards for utility services.[16/]

Kentucky statutes also authorize the ERC and URC to "regulate utilities and enforce the provisions of this chapter."[17/] In so doing the ERC and URC may adopt reasonable regulations to implement the provisions of the statute.[18/] An attorney with the ERC has stated that it is the ERC's belief that the two clauses permit it to exert powers not specifically enumerated in the statutes.[19/] Judicial interpretations appear to uphold this belief.

In Public Service Commission v. City of Southgate,[20/] the Kentucky court acknowledged that certain "jurisdiction is implied necessarily from the statutory powers of the Commission to regulate the service of utilities." In this case, the court upheld the jurisdiction of the Public Service Commission to pass upon the sales of utility systems despite the absence of explicit statutory authority. Citing favorably a discussion of public utilities and services in a widely used treatise,[21/] the court also recognized "that a public utility subject to the jurisdiction of the Public Service Commission cannot discontinue operation without approval of the Commission."[22/]

Based on the authority of the ERC and URC to regulate public utilities[23/] and the broad interpretation the courts have attached to that clause,[24/] a member of the staff of the ERC has suggested that the ERC may assert jurisdiction over mergers, consolidations, sales or leases of property, transfers of franchises or property, abandonment of service, and initiation of service.[25/]

IV. AUTHORITY TO ASSIGN RIGHTS TO PROVIDE SERVICE IN A GIVEN AREA

A. Generally

Under the old statutes certificates of convenience and necessity, issued by the Public Service Commission, were required to construct or operate any "public utility" as defined in the statute. The present statutory provisions state that "no person, partnership, public or private corporation or combination thereof shall begin the construction of any plant, equipment, property or facility for furnishing to the public any of the services enumerated in the statute . . . until such person has obtained from the appropriate commission a certificate that public convenience and necessity require such construction."[26/] The only exception to this requirement applies to "retail electric suppliers for service connections to electric-consuming facilities located within its certified territory and ordinary extensions of existing systems in the usual course of business . . . ."27/ Extensions into areas not specifically assigned to a supplier are not allowed. "Retail electric supplier" is defined to include any person, firm, corporation, association or cooperative corporation, excluding municipal corporations, engaged in the furnishing of retail electric service.28/

B. Competition

According to an attorney with the ERC, Kentucky follows a monopoly policy with respect to utility suppliers. Pursuant to this policy, no electric, gas or telephone company has ever been allowed to provide duplicate service in the same area already served by another utility.29/ This policy follows from a legislative declaration that:

> [I]n order to encourage the orderly development of retail electric service, to avoid wasteful duplication of distribution facilities, to avoid unnecessary encumbering of the landscapes of the Commonwealth of Kentucky, to prevent the waste of materials and natural resources, for the public convenience and necessity and to minimize disputes between retail electric suppliers which may result in inconvenience, diminished efficiency and higher costs in serving the consumer, the state be divided into geographical areas, establishing the areas within which each retail electric supplier is to provide the retail electric service as provided in KRS 278.016 to 278.020 and, except as otherwise provided, no retail electric supplier shall furnish retail electric service in the certified territory of another retail electric supplier.30/

Accordingly, the Public Service Commission, in 1972, established boundaries around existing suppliers within which each retail electric supplier was given the exclusive right to furnish retail electric service to all electric-consuming facilities.[31/] To further insure the state's policy on monopoly of supply, the legislature has declared that, "no retail electric suppliers shall furnish, make available, render or extend retail electric service to any electric-consuming facility to which service is being lawfully furnished by another retail electric supplier . . . ."[32/]

However, new suppliers may be authorized to replace an existing supplier if the ERC finds that the existing utility is not rendering or does not propose to render adequate service.[33/] Accordingly, the ERC will consider whether there is a substantial inadequacy of existing service and whether there will be any wasteful duplication resulting from the construction of a new system.[34/]

Because the state is divided into designated areas, there is little occasion for service area disputes. Should a dispute occur, however, the ERC is empowered to resolve the disagreement.[35/]

C. Procedure

Any party seeking a certificate of public convenience and necessity must file an application with the appropriate commission.[36/] The required contents of each application are specified in the Kentucky Administrative Regulations.[37/]

After the application is filed, a hearing is held with all interested parties.[38/] If the application is for the construction of a new electric transmission line of 400 kilovolts or more, the ERC is required to give public notice of the hearing.[39/]

D. Criteria

Other than a general declaration that the appropriate commission shall issue a certificate only upon a finding that the public convenience and necessity will thereby be served, the legislature has not established any particular factors to be considered when reviewing the certificate applications of most utilities. Specific criteria have only been outlined for dividing service areas between electric suppliers.

Service areas partitioned by lines set up substantially equidistant from the distribution lines of suppliers serving the state as of June 16, 1972, were established by the Public Service Commission.[40/] Any party aggrieved by the partitions could have sought to have the territorial designations revised. In such cases, the ERC was to be guided by the following conditions as they existed on June 16, 1972:

(a) The proximity of existing distribution lines to such certified territory.

(b) Which supplier was first furnishing retail electric service, and the age of existing facilities in the area.

(c) The adequacy and dependability of existing distribution lines to provide dependable, high quality retail electric service at reasonable costs.

(d) The elimination and prevention of duplication of electric lines and facilities supplying such territory. In its determination of such protest, the Commission hearing shall be de novo; and neither supplier shall bear the burden of proof.41/

V. APPEALS OF ERC AND URC DECISIONS

Any party to a proceeding before the ERC or the URC may petition for a rehearing on any of the matters determined.42/ The rehearing is optional, however, and a party may appeal directly to the Franklin Circuit Court.43/ An appeal may also be taken from a final decision on rehearing or from a denial of a request for a rehearing.44/ The appeal to Franklin Circuit Court must be made within twenty days after being served with the ERC's or the URC's final decision. The appeal takes the form of an action against the ERC or the URC to vacate or set aside an order on the grounds that it is unlawful or unreasonable.45/

The appeal is based on the transcript compiled at the initial decisionmaking level. New evidence will not be heard by the court.46/ If newly discovered evidence that will materially affect the case is offered, the court may remand the case for rehearing by the ERC or the URC.47/

After a judgment by the circuit court, either party is entitled to seek review by the Court of Appeals. This appeal must be taken in accordance with the Rules of Civil Procedure and the appeal will proceed in the same manner as other civil cases. The decision of the Court of Appeals is final and may not be subsequently reviewed.

FOOTNOTES

1. Ky. Rev. Stat. §278.040 (1972).
2. *Id*. §278.010(4) (Supp. 1978).
3. *Id*. §278.010(5).
4. *Id*. §278.010(2).
5. *Id*. §278.010(1).
6. Mr. Bill Sawyer, Attorney for the ERC, Telephone conversation, August 7, 1978.
7. Ky. Rev. Stat. §278.010(3) (Supp. 1978).
8. *Id*. §278.040(2).
9. *Id*. §278.040(2).
10. *Id*. §278.300.
11. *Id*. §278.220.
12. *Id*. §278.018(6).
13. *Id*. §§278.017-278.025.
14. *Id*. §§278.018, 278.280.
15. *Id*. §278.020.
16. *Id*. §§278.018(3), 278.280(1).
17. *Id*. §278.040(1).
18. *Id*. §278.040(3).
19. Mr. Bill Sawyer, Attorney for the ERC, Telephone conversation, August 7, 1978.

20. *Public Service Comm'n. v. City of Southgate*, 268 S.W. 2d 19 (Ky. 1954) (citing Ky. Rev. Stat. §278.040.)

21. 43 Am. Jur. 2d Public Utilities and Services §78.

22. *Ibid*.

23. Ky. Rev. Stat. §278.040 (Supp. 1978).

24. *Public Service Comm'n. v. City of Southgate*, 268 S.W. 2d 19 (Ky. 1954).

25. Mr. Bill Sawyer, Attorney for the Kentucky Public Service Commission, Telephone conversation, August 7, 1978.

26. Ky. Rev. Stat. §278.020(1) (Supp. 1978).

27. *Ibid*.

28. *Id*. §278.010(6).

29. Mr. Bill Sawyer, Attorney for the ERC, Telephone conversation, August 7, 1978.

30. Ky. Rev. Stat. §278.016 (Supp. 1978).

31. *Id*. §278.018(1).

32. *Id*. §278.018(4).

33. *Id*. §278.018(3).

34. *Kentucky Utilities Co. v. Public Service Comm'n.*, 252 S.W.2d 885 (Ky. 1952) (case involving the application of the East Kentucky Rural Electric Cooperative Corporation for a certificate of convenience and necessity authorizing construction of a steam generating plant and associated transmission lines for the purpose of supplying electric energy to consumers already being served by the Kentucky Utilities Company.

35. Ky. Rev. Stat. §278.018(2) (Supp. 1978).

36. *Id*. §278.020(1).

37. 807 Ky. Admin. Reg. 1:010(8)(9).

38. Ky. Rev. Stat. §278.020(1) (Supp. 1978).

39. *Id*. §278.027.

40. _Id_. §278.017(1).

41. _Id_. §278.017(3).

42. _Id_. §278.400.

43. _Id_. §278.410(1).

44. _Ibid_.

45. _Ibid_.

46. _Id_. §278.440 (1972).

47. _Ibid_.

CHAPTER 3

SITING OF ENERGY FACILITIES IN KENTUCKY

I. PUBLIC AGENCIES WHICH ADMINISTER SITING LAWS

A. State Agencies

1. Public Service Commission and Energy Regulatory Commission

As noted in Chapter 2, effective April 1, 1979, new legislation replaced the Public Service Commission with a new three-member Energy Regulatory Commission (ERC) with jurisdiction over electric and natural gas utilities, and a three-member Utility Regulatory Commission with control over telephone, sewer and water utilities. The Energy Regulatory Commission thus succeeded to the jurisdiction of the former Kentucky Public Service Commission to enforce certain energy facility siting provisions of the Kentucky statutes.[1/] The provisions require a company to obtain a certificate of environmental compatibility before beginning "the construction of any facility to be used for the generation of electricity to or for the public for compensation . . . ." The ERC's jurisdiction preempts local regulations with respect to public utilities under the ERC's control, but does not preempt the permitting authority of the Department of Natural Resources and Environmental Protection.

2. Department of Natural Resources and Environmental Protection

The only state agency apart from the ERC concerned with energy facility siting is the Department of Natural

Resources and Environmental Protection ("Department"). The Department administers extensive permitting requirements for the construction and operation of any facility affecting the environment.2/ Details concerning the individual permits (e.g., air, water, steam, solid waste) are found in Chapters 151 and 224 of the Kentucky statutes. Because the Department has such extensive permitting requirements, officials are considering implementing a coordinated permitting procedure for energy facility siting to be administered by the Office of Program and Policy Analysis.3/

B. Local Government

Chapter 100 of the Kentucky Revised Statutes deals with local planning and zoning.4/ The chapter allows cities and counties independently or jointly to form planning units. The planning commission of each unit is authorized to prepare comprehensive plans to be used as a guide for cities in establishing zoning regulations.5/ Any city or county which is a member of a planning unit may then adopt zoning regulations "to promote the public health, safety, morals and general welfare of the planning unit."6/

Once all components of a comprehensive plan are prepared and adopted, local jurisdictions have the power to adopt an "official map."7/ Any person desiring to construct, or in any way alter, facilities which would change the "official map" must receive a permit from the city or county.8/

However, public utilities operating under the jurisdiction of the ERC, i.e., those holding themselves out as serving the general public (see Chapter 2), are exempt from the local permitting procedure. Such utilities are not required to obtain permits from the local planning unit approving the location or relocation of any of their service facilities.[9/]

II. SCOPE OF SITING JURISDICTION OF COMMISSION

The Kentucky statutes provide that "no person, partnership, public or private corporation or combination thereof shall begin the construction of any facility to be used for the generation of electricity to or for the public for compensation without having first obtained from the [ERC] a certificate of environmental compatibility."[10/] "Facility" is defined broadly as "all property, means and instrumentalities owned, operated, leased, licensed, used, furnished or supplied for, by, or in connection with the business of any utility."[11/] It is, therefore, likely that the facilities used in all phases of electric utility service, i.e., generation, transmission, distribution and storage, are subject to siting regulation.

Cities are expressly exempted from the ERC's jurisdiction.[12/]

While parties are precluded from "beginning any construction" without first obtaining the proper certification, neither the legislature nor the courts have defined the term "construction." Arguably, all construction conduct, including the initial preparation for new construction and the replacement or extension of existing facilities, falls within the scope of the ERC's siting jurisdiction.

There are no minimum limits on the size of facilities subject to the siting provisions. A grandfather clause, however, exempts those "facilities for which an application for a certificate of convenience and necessity has been filed with, or granted by, the public service commission prior to June 21, 1974."[13/]

The ERC's jurisdiction is co-extensive with the permitting authority of the Department. Although the siting statute does not specify whether the ERC's powers are preemptory of, or concurrent with the Department's permitting authority, spokesmen for the ERC and the Department have stated that jurisdiction is concurrent.[14/]

In addition to issuing separate permits for air, water, and solid waste pollution, the Department participates in the ERC's certification of facilities by submitting a report to the ERC of any recommendations or objections it has to the proposed facility.[15/] Presumably, these views are considered by the ERC but there is no statutory duty to comply with such recommendations, nor any standards for following or overriding the recommendations set out in the statutes.

The ERC's rules and regulations are primarily procedural in nature and do not further delineate the ERC's jurisdiction.[16/] Because the siting statute did not become effective until June 17, 1978, there have also been no reported judicial decisions under the statute.

III. CERTIFICATION PROCESS

A. Statement of Environmental Compatibility

Prior to applying for a certificate of environmental compatibility from the ERC, an applicant must submit to the Department (or any local pollution control district exercising concurrent jurisdiction) a statement of environmental compatiblity concerning the proposed site.[17/] Such statement must contain, at a minimum, the following information:

(a) A complete description of the proposed project;

(b) Comments on the effects of air pollutants from the proposed facility on public health and welfare, the effects of the proposed facility on the waters of the Commonwealth, the treatment, handling and disposal of solid waste from the proposed facility, noise pollution, if any, and other adverse environmental effects which cannot be avoided. [18/]

The Department is required to prepare recommendations concerning the proposal within 60 days of receiving the applicant's statement of environmental compatibility.[19/]

B. Application for Certification

The applicant also submits an application directly to the ERC, in accordance with requirements set forth in the Kentucky Administrative Regulations.[20/] The application is not required to include alternative site proposals, and the applicant is not required to publish copies of the application nor give public notice.

C. ERC Duties

Upon receiving a report from the Department (or the local pollution control district) containing recommendations on the proposed facility, the ERC is required to hold a public hearing open to all interested parties.[21/] As previously noted, however, there is no statutory duty to follow the recommendations of the other departments.

There is no requirement that the ERC prepare a written report of its decision, nor is there a time limit within which it must render a decision.

For a discussion of procedures involved in appealing ERC decisions to the court, see Chapter 2, Part V.

IV. CERTIFICATION STANDARDS

In granting or denying the application for a certificate of environmental compatibility, the ERC is required to consider community needs, industrial development, consumer requirements, and the economics of the facility. All of these factors are to be balanced against any adverse environmental factors.[22/] No additional criteria have been established either by statute or by administrative regulations.

The statute envisions that these standards will be applied generally to the certification of all facilities by the ERC. A recent order of the Public Service Commission, predecessor of the ERC, granting certification does not discuss the criteria.[23/] Rather, the Public Service Commission merely found that the Department had "reviewed the Applicant's Environmental Impact Statement and . . . has no objection to the issuing of a Certificate of Environmental Compatibility for the said generating units."[24/] Thus, although the statute does not specify any particular weight to be given to the recommendations of other agencies, this case does suggest that the ERC is likely to attach significance to reports submitted by the Department of Natural Resources and Environmental Protection. It is unclear what standard will be followed by the ERC in overriding the negative recommendation of the Department.

FOOTNOTES

1. Ky. Rev. Stat. Ann. §278.025 (Bobbs-Merrill Supp. 1978).

2. Mr. Frank Wermeling, Attorney for the Department of Natural Resources and Environmental Protection, Telephone conversation, August 10, 1978.

3. Ibid.

4. Ky. Rev. Stat. Ann. §§100.113-100.123 (Bobbs-Merrill 1971 and Bobbs-Merrill Supp. 1978).

5. Id. §100.183 (Bobbs-Merrill 1971).

6. Id. §100.201.

7. Id. §100.293.

8. Id. §100.303.

9. Id. §100.324.

10. Id. §278.025(1)(Bobbs-Merrill Supp. 1978).

11. Id. §278.010(11).

12. Id. §278.010(3).

13. Id. §278.025(1).

14. Mr. Bill Sawyer, Counsel for the ERC, Telephone conversation, August 7, 1978; Mr. Frank Wermeling, Counsel for the Department of Natural Resources and Environmental Protection, Telephone conversation, August 10, 1978.

15. Ky. Rev. Stat. Ann. §278.025(4)(Bobbs-Merrill Supp. 1978).

16. Id. §13.081(Bobbs-Merrill Supp. 1971).

17. Id. §278.025(2)(Bobbs-Merrill Supp. 1978).

18. Id. §§278.025(3).

19. Id. §278.025(4).

20. 807 Ky. Admin. Regs. 1:010(1972).

21. Ky. Rev. Stat. Ann. §278.025(5)(Bobbs-Merrill Supp. 1978).

22. Id. §278.025(6).

23. In Re Ky. Utils. Co., Hearing before the Kentucky Public Service Commission, Case No. 6920(1977).

24. Id.

CHAPTER 4

LAW GOVERNING FRANCHISES IN KENTUCKY

I. AUTHORITY TO GRANT FRANCHISES

The Constitution of Kentucky, enacted in 1891, authorizes municipalities to grant franchises, except with respect to a utility which had a charter from the legislature that already contained rights comparable to franchise rights, and the utility had undertaken activities pursuant to those rights in good faith, prior to 1891.[1/] The purpose of the constitutional provisions is to prevent the legislature from authorizing the indiscriminate use of the streets of cities by public utilities, without the approval and control of the cities.[2/] The two provisions of the Constitution are as follows:

> §163. Public Utilities must obtain franchise to use streets. -- No street railway, gas, water, steam heating, telephone, or electric light company, within a city or town, shall be permitted or authorized to construct its tracks, lay its pipes or mains, or erect its poles, posts or other apparatus along, over, under or across the streets, alleys or public grounds of a city or town, without the consent of the proper legislative bodies or boards of such city or town being first obtained; but when charters have been heretofore granted conferring such rights, and work has in good faith been begun thereunder, the provisions of this section shall not apply.
>
> §164. Term of franchises -- Advertisement and bids. -- No county, city, town, taxing district or other municipality shall be authorized or permitted to grant any franchise or privilege, or make any contract in reference thereto, for a term exceeding twenty years. Before granting such franchise or privilege for a term of years,

> such municipality shall first, after due advertisement, receive bids therefor publicly, and award the same to the highest and best bidder; but it shall have the right to reject any or all bids. This section shall not apply to a trunk railway. 3/

Statutes enacted to establish specific procedures for granting franchise by cities of various classes are discussed in Part II, below.

The final clause of Section 163 of the Constitution, quoted above, exempting from municipal franchising authority the exercise of rights granted by charter prior to adoption of the Constitution, applies even where those rights have been assigned or the original company has been mêrged into a new company after adoption of the Constitution. Those pre-existing rights are perpetual and cannot be abridged or revoked by a municipality. In 1972, the Kentucky Attorney General issued an opinion outlining at length the relevant case law, and finding that the Western Kentucky Gas Company and South Central Bell Telephone Company had perpetual rights to furnish respectively gas and telephone services in the City of Shelbyville, and that those rights were not subject to local franchising authority.4/ South Central Bell was a successor to a company which had, in turn, purchased all the rights, privileges and franchises from another company which had consolidated with yet another company which had been chartered in 1886 to construct, maintain and operate telephone lines within Kentucky, together with all rights "as are usually enjoyed by such corporations."

Western Kentucky Gas Company had similarly succeeded to a perpetual grant by the legislature which was made prior to adoption of the 1891 Constitution.

Where no right was granted by charter prior to the Constitution of 1891, the franchising provisions are binding upon the municipality, upon any person or company exercising rights subject to the franchising requirements, and upon the legislature. In City of Nicholasville v. Blue Grass Rural Electric Coop. Corp.,[5/] the court held invalid a statute purporting to authorize a rural electric co-op to construct facilities along streets without the consent of the city that had recently annexed the area. Hilliard v. George G. Fetter Lighting & Heating Co.,[6/] held an ordinance permitting the local department of public works to issue annual licenses to corporations desiring to transmit electricity or heat invalid for failing to comply with the franchising procedures. Town of Hodgenville v. Gainesboro Tel. Co.,[7/] held that a public utility operating within a municipality without a franchise is a mere licensee.

The franchise requirements have been construed to apply to activities involving use of public streets beyond those activities specified in the Constitution. In Ray v. City of Owensboro,[8/] the city enacted an ordinance requiring a franchise for the operation of an ambulance within the city. The plaintiff argued that an ambulance was not a proper subject for a franchise because Section 163 of the

Kentucky Constitution specifies only street railways, gas, water, steam heating, telephone or electric light companies. The court found that

> the purpose of the section was to give the city control of the streets, alleys and public grounds and to make it possible for the city to provide the services of these utilities to its inhabitants. Therefore, the right granted is not . . . restricted to those utilities enumerated, but applies to all utilities and services which might today be proper subjects for control when the original content and purpose of the act is considered.

In City of Owensboro v. Top Vision Cable Co.,[9/] the court held that cable television was subject to the franchise requirements.

The franchise requirements, however, do not apply to activities on private property.[10/]

The above-quoted Constitutional provisions are self-executing, and apply to all municipalities regardless of other enabling statutes or ordinances.[11/] However, a few statutes have been enacted clarifying or granting additional powers to cities of various classes in connection with franchises. A city of the second-class is authorized, among other things, to:

> [1] Compel gas and electric companies and all persons using, controlling, or managing electric light wires for any purpose to change and relocate poles, electric wires, conduits for electric wires, gas mains and pipes, place those above the surface of the ground below it, change the method of conveying light and generally to do things conducive to the safety and comfort of the inhabitants of the city in the premises;

[2] Regulate the manner in which electric light, telephone and telegraph wires are placed underground and the use of all such wires and connections therewith. 12/

A third-class city is authorized as follows:

(1) The legislative body of any city of the third class may, by ordinance, grant the right of way in streets, alleys and public grounds of the city to any railway, street railway, gas, water, steam heating, telephone or electric light or power company for a term not exceeding twenty (20) years. Before granting such privilege, the city shall, after advertising by publication . . . receive bids publicly, and award the privilege to the highest and best bidder, having the right to reject any and all bids.

(2) The city shall reserve the right to regulate and control the tracks, pipes and wires of such companies, and the public ways in which they are laid or constructed, and shall reserve the right to require any such company to conform to any changed grades of the streets and public grounds, . . . or mode of construction or operation, to suit public convenience, to raise or lower its pipes, or to take down its wires to raise or lower its pipes, or to take down its wires and lay them underground, as the public good requires.

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(4) All such grants shall expire and become voidable, at the option of the city, although a consideration has been paid unless a bona fide organization has taken place and business has been commenced and prosecuted under the grant in good faith within one (1) year from the date of the grant. The legislative body may impose other conditions and terms in addition to and not inconsistent with those enumerated in this section 13/

A fourth-class city is authorized to:

. . . grant right of ways over the public streets or public grounds of the city to any utility company, on such conditions as seem proper, shall have a supervising control over the use of same 14/

The different classes of cities represent primarily differences in size.[15/] Louisville is the only first class city.[16/]

Where a municipality annexes territory, a company already operating in the area annexed will normally have the right to continue:

> Any utility providing electric service in any area annexed, subsequent to June 16, 1960, by any municipality shall have the dominant right to continue to provide electric service in said area to consumers then being served and to new consumers located nearer to its facilities than to the facilities of any other utility as all those facilities were located immediately prior to annexation. [17/]

However, if the company is to use public streets and ways, it must still obtain a franchise; the quoted provision merely provides a right to obtain the franchise.[18/]

II. PROCEDURES FOR GRANTING FRANCHISES

A. Granting Franchises

The Kentucky Constitution and the Kentucky statutes outline certain procedural steps to be followed when granting a franchise. Section 164 of the Constitution, quoted in Part I, above, requires the municipality to receive bids publicly after due advertisement.[19/] In the case of second-class cities, by statute, the advertisement is required to be made in one or more newspapers in the city.[20/] The courts have not set any absolute guidelines regarding the "due advertisement" requirement. In *Garthright v. H. M. Byllesby & Co.*,[21/] the court held a two week notice sufficient, and in Bowling Green v. Davis,[22/] a six day notice was held to be sufficient to insure competitive bidding. It is important, however, that the advertisement state, with accuracy, the type of franchises to be given. In Princeton v. Princeton Elec. Light & Power Co.[23/] for example, the court held a fifteen year franchise invalid because the city had advertised only for bids on a franchise with a ten year duration.

The franchise is granted by the adoption of an ordinance. The procedures for adopting an ordinance vary depending on the size of the city. In a first, second, third or fourth class city under a city manager form of government (first class cities are not permitted to adopt a commission form of government[24/] every ordinance "granting any franchisee the right to use or occupy the streets, highways, bridges, or public places of the city . . . shall, after its introduction and before its adoption, remain on file at least one (1) week for public inspection in the completed form in which it shall be put upon its final passage."[25/] The statute further provides that no such ordinance is effective until 10 days after its passage, except in the case of emergencies, when the public health or safety requires that the ordinance take immediate effect. A unanimous vote of the board of commissioners must declare such an emergency.[26/] The declaration of an emergency is not conclusive and will not be upheld if done to abridge the right of referendum.[27/]

If, within the ten day period, a petition signed by electors totalling 25% of the total number of votes cast for both candidates for mayor in the last election is presented, protesting the ordinance, the ordinance is suspended and must be reconsidered by the board of commissioners. If the ordinance is not repealed, it is to be submitted to the voters of the whole city, and if a majority of the voters agree to pass the ordinance, it will become effective when the result is officially declared; otherwise, it shall fail. 28/

Fifth and sixth class cities (which may only adopt a commission form of government 29/ use somewhat different procedures for granting a franchise. An ordinance by such cities granting a franchise cannot be passed by the city council within five days after its introduction, nor at other than a regular meeting. Each ordinance must be signed by the chairman, attested by the clerk and published. The ordinance will be in force from and after publication. 30/ A councilman having an interest in the matter may not vote. 31/

In addition to the above procedures, the Kentucky statutes provide that:

> No utility shall apply for or obtain any franchise, license, or permit from any city or other governmental agency until it has obtained from the Commission . . . a certificate of convenience and necessity showing that there is a demand and need for the service sought to be rendered. 32/

The Commission's requirements for certificates of convenience and necessity are discussed in Chapter 2 above.

B. Renewing Franchises

At least eighteen months prior to the expiration of a franchise, the city must provide for

> the sale of a new franchise to the highest and best bidder on terms that are fair and reasonable to the city, to the purchaser of the franchise and to the patrons of the utility. The terms shall specify the quality of the service to be rendered and, in cities of the first class, the price that shall be charged for the service. 33/

Unless the bidder already owns (in a city other than a first-class city) a plant and equipment which is adequate to render the service required under the franchise, he must provide a deposit of 5% of the fair estimated cost of the plant. This deposit is forfeited if the bid is accepted and the bidder fails, within thirty days after the confirmation of the sale, to pay his bid price and post a sufficient bond of one-fourth of the fair, estimated cost of the plant. The bond is forfeited if the bidder fails within a reasonable time, to establish a plant and begin service in accordance with the terms of the sale. 34/ No specific provision is made for the disposition of existing facilities.

The renewal procedures do not apply in the following circumstances:

> If there is no public necessity for the kind of public utility in operation and if the city desires to discontinue entirely the kind of service in question, or if, in the case of cities other than those of the first class, the city

> owns or desires to own and operate a municipal plant to render the required service this section shall not apply. 35/

Thus, if a city (other than one of the first class) desires to own and operate a municipal plant to render the service, it need not offer to renew the franchise upon its expiration. 36/

III. CRITERIA FOR GRANTING FRANCHISES

The only criteria for granting franchises are that the constitutional and statutory procedures and requirements be followed. The Constitutional requirement that the franchise be sold to the highest and best bidder has been held to permit the municipality to reject what appears on its face to be the highest and best bid, and to accept a lower bid, if in so doing the municipality exercises sound discretion. 37/ For example, the franchise may be sold to the second highest bidder where the highest bidder is insolvent and lacks experience in producing or furnishing the services. 38/ However, the municipality may not arbitrarily or corruptly reject all bids. 39/

Reasonable requirements may be imposed by a municipality as conditions for granting a franchise. In Peoples Gas Co. v. Barbourville, 40/ the court upheld, as reasonable conditions, provisions in an ordinance offering the sale of a gas franchise, that specified that a continuous basic pipeline must be used, and specified the rates and amount of security to be given by the operator of the gas plant. In Mount Vernon Telephone Co. v. City of Mount Vernon, 41/

the city's "telephone franchise ordinance" prohibiting the erection, construction or maintenance of poles, lines or wires upon certain streets was sustained. The utility company had objected that the subject streets had been designated by the Commissioner of Highways as part of the primary system, that the utility had procured from the Department of Highways a permit authorizing the utility to construct the lines and poles, that indemnity had been provided against any damages to the streets, that it was necessary to erect poles and lines on these streets to provide reasonably adequate telephone service, and that the poles would be constructed and maintained under the rules of the Department of Highways so that there would be no obstruction of streets or interference with travel and use. The court held that under present day conditions of crowded business streets, the ordinance was not arbitrary, capricious, oppressive or unreasonable.[42/]

Judicial decisions have established that any franchise adopted in violation of prescribed procedures is void. Thus, where a city granted a franchise to a telephone company but failed to adhere to a procedural requirement that an ordinance be held over five days from the time it was introduced before its passage, the court declared the franchise invalid.[47/]

At the expiration or termination of a franchise, the franchisee may be required to remove its facilities, but is given a reasonable time in which to do so. 48/ However, another case held that ERC must approve all abandonments of service by jurisdictional utilities. (See Chapter 2). No reported decisions have discussed or resolved this inconsistency. If a company begins operations and cannot prove that it has obtained a franchise, a municipality may institute proceedings to compel the company to remove its poles, wires and equipment from the city streets. 49/

B. Exclusivity

First class cities are expressly prohibited from granting exclusive franchises under a section of the statutes providing procedures for the renewal of franchises. 50/ Otherwise, the statutes do not directly address the question of exclusivity. Another statute, however, provides:

> No municipality, in which there is located in existing electric water or gas public utility plant or facility shall construct or cause to be constructed any similar utility plant or any similar public utility facility duplicating such existing plant or facility or to obtain or acquire any similar public utility plant or facility other than by the purchase of the existing plant or facility or by the acquisition of such existing plant or facility by the exercising of eminent domain. 51/

Thus, an existing plant may effectively serve to exclude a municipality from constructing a new similar plant.

The Kentucky Attorney General has issued an opinion that exclusive franchises may be granted if in the public interest. 52/ The question of the validity of an exclusive franchise has, however, not been litigated in

Kentucky. In Truesdale v. City of Newport,[53/] an exclusive 20 year gas franchise had been awarded, but the grounds given for challenging the franchise in court did not include its exclusivity. (Rather, the plaintiff claimed that the Constitutional 20 year limit was violated because the ordinance granting the franchise made the contract effective as of a date two years later).

Although the Kentucky Attorney General is of the opinion that exclusive franchises may be permitted, and there have been no judicial decisions inconsistent with that view, some decisions indicate that franchises will be construed not to grant exclusive franchises in the absence of clear language to the contrary. Willis v. Davis,[54/] for example, held that where notice of bids published by the county for the granting of a franchise omitted to mention that an exclusive franchise would be awarded, the exclusive franchise granted was void for lack of due advertisement. City of Princeton v. Princeton Electric Light & Power Co.,[55/] held a franchise for the exclusive right to manufacture and sell electric light and power void, reasoning that the city had only the right to authorize the use of public ways, not to authorize actual operations. Thus, although exclusive franchises might be granted, they will not readily be construed to be exclusive.

C. Other Characteristics.

There is no requirement that municipalities impose a franchise tax, although they may do so. The state has imposed a tax on all tangible and intangible property, including franchises, and has authorized local governments to impose similar taxes.56/

FOOTNOTES

1. Ky. Const. §163.

2. Kentucky Utilities Co. v. Board of Comm'rs., 254 Ky. 527 S.W. 2d 1024, 1027 (1933).

3. Ky. Const. §§163, 164.

4. Op. Att'y Gen. 72-274 (1972). See, Louisville v. Cumberland Tel. & T. Co., 224 U.S. 649 (1912); Southern Bell Telephone Co. v. City of Commonwealth, 266 S.W. 2d 308 (Ky. 1954); Feichter v. City of Corbin, 71 S.W. 2d 423 (Ky. 1934).

5. 514 S.W.2d 414 (Ky. App. 1974).

6. 105 S.W. 115 (Ky. 1909).

7. 237 Ky. 419 35 S.W.2d 888 (1931).

8. 415 S.W.2d 77 (Ky. 1967).

9. 487 S.W.2d 283 (Ky. 1972), cert. denied, 411 U.S. 948 (1973).

10. Tri State Ferry Co. v. Birney, 31 S.W.2d 932 (Ky. 1930).

11. Irvine Toll Bridge Co. v. Estill County, 275 S.W. 634 (Ky. 1925); Merchants' Police & District Tel. Co. v. Citizens' Tel. Co., 93 S.W. 642 (Ky. 1906).

12. Ky. Rev. Stat. §96.050 (1971).

13. Id. §96.060.

14. Id. §96.070.

15. See Id. §86.010.

16. Id. §81.010 (Supp. 1978).

17. Id. §96.538 (1971).

18. City of Nicholsville v. Blue Grass Rural Electric Co-op Corp., 514 S.W.2d 414 (Ky. 1974).

19. Ky. Const. §164.

20. Ky. Rev. Stat. §84.270 (1971).

21. 154 Ky. 106, 157 S.W. 45 (1913).

22. 313 Ky. 203, 230 S.W.2d 909 (1950).

23. 166 Ky. 730, 179 S.W. 1074 (1915).

24. Ky. Rev. Stat. §89.010 (1971).

25. Id. §§89.230 (1971), 89.590 (Supp. 1978).

26. Ibid.

27. Kentucky Utilities v. Ginsberg, 255 Ky. 148, 72 S.W. 2d 738 (1934).

28. Ky. Rev. Stat. §§89.240, 89.600 (1971).

29. Id. §89.390 (Supp. 1978).

30. Id. §§87.050, 88.060 (1971).

31. Springfield v. Haydon, 216, Ky. 483, 288 S.W. 337 (1926).

32. Ky. Rev. Stat. §278.020(3)(Supp. 1978).

33. Id. §96.010 (1971).

34. Id. §96.020.

35. Id. §96.010.

36. Mormarc Utilities Corp. v. Salyersville, 323 S.W.2d 568 (Ky. 1959).

37. Basket v. Davis, 311 Ky. 13 223 S.W.2d 168 (1949).

38. Hatcher v. Kentucky & West Virginia Power Co., 280 Ky. 583 133 S.W.2d 910 (1939).

39. See, Norris v. Kentucky State Tel. Co., 235 Ky. 234 30 S.W.2d 960 (1930).

40. 291 Ky. 805, 165 S.W.2d 567 (1942).

41. 313 Ky. 93, 230 S.W.2d 451 (1950).

42. Id.

43. Petroleum Exploration v. Joseph Greenspon's Sons Iron & Steel Co., 52 F.2d 944 (6th Cir. 1931).

44. 97 S.W. 770 (Ky. 1906).

45. Ky. Const. §3.

46. 313 Ky. 203, 230 S.W.2d 909 (1950).

47. Rough River Telephone Co. v. Cumberland Telephone & Telegraph Co., 84 S.W. 517 (Ky. 1905).

48. Kentucky Utilities Co. v. Bd. of Commissioners, 254 Ky. 527, 71 S.W.2d 1024 (1933).

49. Rockport Coal Co. v. Tilford, 300 S.W. 898 (Ky. 1927).

50. Ky. Rev. Stat. §96.030 (1971). See, discussion at Part II.B., above.

51. Id. §96.045.

52. Op. Atty. Gen. 70-565 (1970).

53. 90 S.W. 589 (Ky. 1906).

54. 534 S.W.2d 255 (Ky. 1976).

55. 179 S.W. 1074 (Ky. 1915).

56. Ky. Rev. Stat. §136.120.

57. Public Services Commission v. City of Southgate, etc., 268 S.W.2d 19, 21 (Ky. 1954); 43 AM. Jr. 621, §78.