



office memorandum

DATE: July 14, 2017

TO: Honorable Mayor and Councilmembers

THROUGH: Jeff Bryant, City Attorney
FROM: Kathryn L. Walker, Assistant City Attorney III

RE: Franchise Agreements

During a Council Conference on July 11, 2017 regarding the proposed renewal of the Oklahoma Gas and Electric (OG&E) franchise, Staff was asked to provide additional information regarding franchises in general and the impact of this specific franchise on the provision of electricity in Norman. The purpose of this memorandum is to provide the requested information to inform Council's discussion of the topic during the next Study Session scheduled for July 18, 2017.

Franchises: The Basics

A franchise is a right or privilege conferred by law to one or more parties to do some act which cannot be exercised by private individuals at their mere will and pleasure.¹ A franchise allows the holder a right to occupy or burden the streets or public grounds.² A franchise is required before a utility can use the streets, alleys or public grounds to construct and operate its utility.³ More than one franchise can be granted for the same use and purpose.⁴

In *City of Okmulgee v. Okmulgee Gas Co.*,⁵ the Oklahoma Supreme Court detailed the history of franchises in Oklahoma. When the framers were developing the Oklahoma Constitution, they had for their consideration the Constitutions of 45 states and the construction by the courts in those states of those constitutions.⁶ Some delegates to the convention were from the Indian Territory and some were from the Oklahoma Territory.⁷ Each territory dealt with utility franchises differently.⁸ In the Oklahoma Territory, municipalities had the power to grant charters for up to twenty one years in duration.⁹ Municipalities in Indian Territory were empowered to contract, through its mayor and council, with any person or company to construct and operate water and gas systems, as well as to construct

¹ *State of California v. Central Pac. R. Co.*, 127 U.S. 1 (1888); *Oklahoma Gas & Electric Company v. Wilson & Company*, 288 P. 316 (1930).

² *Overholser v. Oklahoma Interurban Traction Co.*, 119 P. 127 (Okla. 1911).

³ *Bartlesville Elec. Light & Power Co. v. Bartlesville Interurban Ry. Co.*, 109 P. 228 (Okla. 1910).

⁴ OKLA. CONST. XVIII, §7.

⁵ *City of Okmulgee v. Okmulgee Gas Co.*, 282 P. 640 (Okla. 1929).

⁶ *Id.* at 644.

⁷ *Id.*

⁸ *Id.*

⁹ *Id.*

street railroads.¹⁰ Some states had laws in place to grant exclusive privileges and franchises, and others had laws that granted a perpetual franchise while reserving in the legislature the right to alter, amend, annul, revoke, or repeal any charter of corporations or franchises when the legislature determined it to be injurious to the citizenry.¹¹ Other states had laws that granted limited franchises for a set number of years.¹² After reviewing the history, the Court said that “[F]rom the historical events and conditions existing about the time the framers of the Constitution assembled and prepared and submitted to the people for their ratification the Constitution, they had in mind the reservation of power in our Constitution by the people to themselves. They also had in mind that the surest way of securing franchises satisfactory to the people was for the people to vote such franchises”.¹³

Ultimately, the adopted provision in the Oklahoma Constitution reserves the decision of granting a franchise to the voters. It says:

No municipal corporation shall ever grant, extend, or renew a franchise, without the approval of a majority of the qualified electors residing within its corporate limits, who shall vote thereon at a general or special election; and the legislative body of any such corporation may submit any such matter for approval or disapproval to such electors at any general municipal election, or call a special election for such purpose at any time upon thirty days' notice; and no franchise shall be granted, extended, or renewed for a longer term than twenty-five years.¹⁴

The qualified voters of a municipal corporation can also bring the issue of granting a franchise forward for a vote through the initiative process. An initiative is an electoral process by which a percentage of voters can propose legislation and compel a vote by the electorate.¹⁵ It is one of the few methods of direct democracy in an otherwise representative system.¹⁶ If a petition, signed by a number of qualified voters equal to twenty-five percent (25%) of the total number cast at the most recent general municipal election, is presented to the City, demanding that a franchise be granted, extended or renewed, a special election must be called.¹⁷ The right of the voters to authorize a franchise cannot be taken away by the Legislature.¹⁸

Franchised Utilities in Norman

There are a number of utilities operating in Norman. Companies providing telephone service are granted statewide access to public rights of way by the Oklahoma Constitution.¹⁹ As new technologies have developed, the Oklahoma Attorney General has

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

¹³ *Id.* at 645.

¹⁴ OKLA. CONST. XVIII, § 5(a).

¹⁵ BLACK'S LAW DICTIONARY 788 (7th ed. 1999).

¹⁶ *Id.*

¹⁷ OKLA. CONST. XVIII, §5(b).

¹⁸ *City of Okmulgee v. Okmulgee Gas Company*, 282 P. 640 (Okla. 1929).

¹⁹ OKLA. CONST. IX, §2.

opined that telephone companies don't need a separate municipal franchise to provide additional services, like video programming, over its telephone lines.²⁰ Thus, the only municipal franchises currently in place are with OG&E, Oklahoma Electric Cooperative (OEC), and Oklahoma Natural Gas (ONG). Although there are two electric providers in Norman, their territories do not overlap.

Oklahoma Natural Gas Franchise: The ONG franchise was first granted by the voters in 1949. The franchise was renewed in the 1970's and again most recently in 1999. During the late 1990's, the State Legislature was considering deregulating utilities. At the time, the City was considering the possibility of buying out the natural gas facilities and becoming a natural gas provider in Norman. Ultimately, Ordinance No. O-9899-22 granting a franchise to ONG was submitted to the voters and approved. ONG pays a franchise fee to the City equal to three percent (3%) of its Gross Receipts received from the distribution of natural gas in Norman. The franchise agreement allows the City the option to purchase all of the gas facilities, including office buildings, distribution system, machinery, real and personal property, etc. owned by ONG during certain defined time periods and provides for payment of fair market value. The agreement will expire March 2, 2024.

Oklahoma Electric Cooperative: The current OEC franchise was granted by the voters in 1996. Rural cooperatives have historically been treated differently by the Legislature than investor-owned electric utilities. Congress adopted the Rural Electrification Act (7 U.S.C. §901, et. seq.) in 1936 to provide low cost funds to expand access to electricity because of the high cost of serving rural areas.²¹ Oklahoma enacted the Rural Electric Cooperative Act (18 Okla. Stat. §437) in 1939.²² The Legislature established a separate tax structure acknowledging the differences between rural electric cooperatives that are member owned versus corporations that are investor owned.²³

Typically, rural cooperatives were operating in unincorporated areas so there was no municipal franchise to be granted. As cities annexed more and more property, they were including areas where rural cooperatives were already operating. As a result, in those situations where previously unincorporated areas were then annexed into a city, rural cooperatives were empowered by the Legislature to construct, maintain and operate electric transmission and distribution lines along, upon, under and across all public thoroughfares and upon all publically owned lands without obtaining the consent, franchise, license, permit or other authorization of the City.²⁴

Prior to the current franchise, OEC operated in Norman under an agreement that provided for an amount to be remitted to the City equal to two percent (2%) of the gross receipts from the sale of electricity in Norman, plus payment of City sales tax of three percent (3%) for a total of five percent (5%) on the sale of electricity in Norman. In 1990,

²⁰ 2006 OK AG 15, §14.

²¹ *Branch Trucking Co. v. State, ex. rel. Okla. Tax Com'n*, 801 P.2d 686 (Okla. 1990).

²² *Id.*

²³ 18 Okla Stat. §437 et. seq.; 68 Okla. Stat. §1214.

²⁴ 18 Okla. Stat. §437.2 (k).

however, the Oklahoma Supreme Court ruled that rural electric cooperatives were exempt from collecting sales tax on the sale of electricity.²⁵ Since OEC could no longer collect sales tax, the OEC franchise agreement adopted in 1996 included a franchise fee of five percent (5%).

State law allows electric cooperatives to opt out of price regulation by the Oklahoma Corporation Commission.²⁶ OEC has opted out of regulation by the Oklahoma Corporation Commission but the Commission retains jurisdiction in specific situations, including issues related to certified territories established under the Retail Electric Supplier Certified Territory Act.²⁷

Oklahoma Gas & Electric: The first OG&E franchise was granted by Norman voters in 1923. The most recent franchise was approved in 1993 and will expire in 2018. Unlike electric cooperatives, investor owned utilities are not exempt from sales tax. In addition to remitting sales taxes, OG&E collects and remits a franchise fee that is equal to three percent (3%) of its gross revenues from the sale of electricity in Norman. Provisions of the franchise agreement require OG&E to defend and indemnify the City against all liability caused by the negligence of OG&E. Rates must be approved by the Oklahoma Corporation Commission. OG&E provides free electricity for the City's operation of traffic signal lights and buildings operated for municipal purposes, provided it does not exceed one-half of one percent (0.5%) of the kilowatt hours sold by OG&E to Norman customers during the preceding fiscal year. This operates as a credit on the City's billings. During the last fiscal year, the City essentially received free electricity for 10 out of 12 months. The value of this was \$534,045.90. The franchise fee remitted to the City for the last fiscal year was \$2,808,327.47.

As discussed last Tuesday, OG&E has requested that the City put the question of renewing the franchise before the voters in November. This would require Council approval of an ordinance setting forth the terms of the franchise and calling the election during Second and Final Reading on August 22, 2017. OG&E will bear the cost of the election. OG&E has asked that the substantive terms of the franchise agreement remain the same.

Public utilities like OG&E fall under the jurisdiction of the Oklahoma Corporation Commission (OCC). The OCC was created by the Oklahoma Constitution to supervise, regulate and control all transportation and transmission companies doing business in Oklahoma.²⁸ The goal of OCC is to insure adequate service, prevent unfair charges to the public, and to protect utilities from unreasonable demands.²⁹ The OCC regulates any changes in rates, the sale or disposal of jurisdictional facilities (utility assets), extension of distribution lines, maintenance of plant, equipment and facilities, meter installations and replacement, utility resource plans, and numerous other operational issues.³⁰

²⁵ *Branch Trucking Co.* at 689, 690.

²⁶ 17 Okla. Stat. §158.27.

²⁷ *Id.*

²⁸ OKLA. CONST. Art. 9, §18.

²⁹ OKLA. ADMIN. CODE §165:35 *et seq.* (2017).

³⁰ *Id.*

Consequences of Failing to Renew a Franchise

During the discussion last week, Council asked that Staff address any consequences of failing to renew a franchise. The Court addressed the expiration of a franchise granted to a water and electric provider in *Incorporated Town of Pittsburg v. Cochrane*.³¹ It said that, if, after a franchise ends, the utility continues to provide, and the municipality accepts, the service, an implied contract of indefinite duration arises.³² The utility would function as a “quasi public utility” and would be subject to the terms of the former franchise and other applicable rules.³³ Similarly, the City would not be absolved of its duties by termination of the franchise.³⁴ However, an implied contract of indefinite duration can be terminated by either party after giving reasonable notice.³⁵

Could another electric provider serve Norman?

Oklahoma law does not currently allow for competitive choice by customers for energy suppliers. Current law favors a territorial approach to electric service. In 1971, the Legislature passed the Retail Electric Supplier Certified Territory Act.³⁶ This act fixed boundaries of certified territories and prohibited retail electric suppliers, which includes both investor owned corporations and cooperative corporations, from furnishing electric services in the certified territory of another.³⁷ In 2009, the Legislature passed the Retail Electric Consumer Cost Reduction, Safety and Service Efficiency Act which similarly divided unincorporated areas into territories and provided for only one supplier to avoid duplication of electrical distribution facilities and minimize unnecessary use of the public rights-of-way.³⁸

Thus, in order for another electric provider to serve those areas of Norman currently served by OG&E, OG&E would have to cease providing electric service in Norman.

Could the City operate an electric utility?

Cities in Oklahoma are empowered to engage in any business or enterprise that may be engaged in by a person, firm or corporation by virtue of a franchise.³⁹ A number of towns have an electric utility. Edmond is the largest municipality in Oklahoma with its own electric utility. In the early 1900’s, while installing its water and sewage systems, the City constructed its own electric plant and infrastructure to provide electricity to its citizens. The distribution and transmission systems were added to as the town grew. In 1982, because of the rising wholesale electric rates, Edmond joined the Oklahoma Municipal

³¹ 159 P.2d 534 (Okla. 1945).

³² *Id.* at 538.

³³ *Id.*

³⁴ *Iowa City v. Iowa City Light & Power Co.*, 90 F. 2d. 679 (8th Cir. 1937).

³⁵ *Id.*

³⁶ 17 Okla. Stat. §158.21 *et seq.*

³⁷ 17 Okla. Stat. §158.24.

³⁸ 17 Okla. Stat. §158.41 *et seq.*

³⁹ 11 Okla. Stat. §22-104.

Power Authority (OMPA).⁴⁰ There are three general components of an electrical grid power system – generation, transmission, and distribution. OMPA generates the power and Edmond transmits it through 6,300 distribution transformers and nine substations, and then distributes the electricity through approximately 35,000 electric meters.⁴¹ Their service territory covers 90 square miles and includes approximately 617 miles of overhead and 657 miles of underground electric lines.

OMPA is a municipal joint-action agency created by statute as a result of advocacy by the Municipal Electric System of Oklahoma to provide adequate, reliable, and affordable electrical power supply to the municipally owned electric systems. OMPA owns generating plants in four states.⁴² OMPA currently has power sales contracts with 42 towns and cities in Oklahoma and reported serving 115,280 customers in 2015. If Norman were to create its own utility and join the OMPA, it would have to acquire transmission and distribution facilities as well as the staff to support them. All electric utility rates would be subject to the provision in Norman's charter requiring voter approval. Currently, there is a moratorium in place that restricts the City from using eminent domain to acquire such facilities.⁴³ Under current law, the moratorium will remain in place until electric restructuring enabling legislation is enacted and consumer choice of retail electric energy suppliers is implemented.⁴⁴

Conclusion

Franchise agreements are scheduled for additional discussion during the Council Study Session on July 18, 2017. Staff will be available to answer any additional questions at that time.

⁴⁰ Source: <http://www.edmondok.com/227/Company-History>

⁴¹ Source: <http://www.edmondok.com/1240/Energy-Portfolio>

⁴² *Id.*

⁴³ 11 Okla. Stat. §21-222.

⁴⁴ *Id.*