MEMORANDUM
CONFIDENTIAL ATTORNEY-CLIENT WORK PRODUCT

TO: Susan F. Clark

FROM: Brittany Adams Long

DATE: September 18, 2019

RE: JEA's Potential Sale of Electric Utility; Authority of FPSC to Approve Agreement Allowing Two Utilities in Same Service Territory; Effect of City of Jacksonville Grant of Franchise on FPSC Territorial Authority.

Background

The City of Jacksonville (COJ), through the Jacksonville Charter, has authorized the Jacksonville Electric Authority (JEA) to own, manage, and operate a utilities system within and without the COJ. COJ Charter, § 21.01, *available at* https://library.municode.com/fl/jacksonville/codes. The JEA pays COJ a franchise fee of 3% of revenues of the electric system and the water and sewer system. *See* COJ Charter, § 21.07(l). Currently, this is an exclusive franchise for only JEA to service the area.

The JEA seeks to sell the electric utility through an Invitation To Negotiate (ITN), which will most likely result in ownership by a private entity (investor-owned utility) (for the purposes of this memorandum, the potential purchaser is called "Newco"). A unique feature of this transaction is that the JEA has entered into an agreement to buy power from two nuclear plants in Georgia (the "Georgia Plants"). The agreement requires the JEA to purchase a certain amount of power from the Georgia Plants for 20 years beginning when the plants are operational. It is our understanding that the JEA cannot transfer its obligations under the contract to a private entity without incurring tax consequences of approximately $800 million.[1]

Thus, the JEA seeks a unique structure to address this situation. The JEA would remain as the provider of the retail utility services solely for the delivery of power purchased from the Georgia Plants to current JEA customers. The JEA would sell the rest of its electric utility assets to a private entity that would be responsible for providing all additional power beyond that generated by the Georgia Plants needed to meet the demands of customers within the current JEA service territory. This service territory would become the service territory of Newco. Thus, there would be two entities responsible for providing service to customers in the territory: 1) JEA, who would have the limited obligation to serve electric customers up to the amount it is required to purchase from the Georgia Plants; and 2) Newco, who would have the obligation to serve the rest of the power needs of those same customers. Newco would own the transmission and distribution facilities to deliver power and would be responsible for all other aspects of providing utility service

[1] Likewise, the JEA cannot simply resell the power to a private entity without incurring the tax consequences.

to retail customers (billing, collections, maintenance, and operation of the system). To the extent JEA must deliver the services directly to customers, it is anticipated that as part of the agreement with Newco, JEA would use Newco's facilities and contract with Newco for the use of these facilities.

It is anticipated that COJ would grant a franchise to both JEA and Newco to allow them to provide service in the areas that are currently serviced by the JEA through an exclusive franchise. The new franchise would be exclusive to these two providers.

Issues

1) Whether the Florida Public Service Commission (FPSC) has authority to approve a territorial agreement that allows two electric utilities to serve the same territory in the specific situation described above.

2) Whether the City of Jacksonville's granting of franchises to both utilities has any effect on FPSC's authority over service territories.

Summary

1) There does not appear to be any authority that specifically prohibits the FPSC from allowing two electric utilities to operate in the same territory, although through case law, the FPSC has historically permitted only one utility to serve an area. The purpose of exclusivity is to avoid uneconomic duplication of services and higher electric costs to customers that would be the result of competition. The underlying concern is what is in the best interest of the public. It is likely that, although this situation is unconventional, the FPSC will analyze it as it typically analyzes territorial agreements and consider the policies and the best interest of the public. If it can be demonstrated that this situation is in the best interest of the public, based on the specific facts in the case, there appears to be no legal reason the FPSC could not approve the agreements. However, it is also likely that the FPSC will not want to create a precedent to change the traditional model (one retail electric utility serving a specific geographic territory), so the unique facts of this case will need to be highlighted and sufficient evidence presented to show why this transaction is needed for the best interest of the public.

2) FPSC maintains exclusive and superior authority over territorial areas, and a municipality, through a franchise agreement, cannot usurp the FPSC's authority to decide which utility serves a given territory. There is nothing unique in this case that would disrupt this authority.

Analysis

I. Law Relating to Public Utilities

Legal research revealed only two cases in which a Florida municipal electric company was sold to a public utility: *In re: Petition by Florida Power & Light Company (FPL) for authority to charge rates to former City of Vero Beach customers and for approval of FPL's accounting*

treatment for City of Vero Beach transaction, Final Order Number PSC-2018-0566-FOF-EU (Fla. P.S.C. 2018) and *In re: Joint Petition of Florida Power Corporation and Sebring Utilities for Approval of Certain Matters in Connection with the Sale of Assets by Sebring Utilities Commission to Florida Power Corporation*, Order Number PSC-1992-1468-FOF-EU (Fla. P.S.C. 1992).

In these cases, the FPSC did not specifically approve or rule on the sales agreement. In *Vero Beach*, the FPSC specifically acknowledged that it did "not have jurisdiction over, approval of the transfer of the City's electric utility assets to FPL [the private entity]." *Vero Beach*, at p. 4. The FPSC does, however, have jurisdiction over related items, such as termination or modification of territorial agreements, approval of any new territorial agreements, approval of rates for Newco, and approval of rate structure modifications if necessary for JEA.[2] §§ 366.04 & 366.05, Fla. Stat. Thus, the FPSC, consistent with these prior cases, should consider the traditional factors the FPSC and the Court considers in approving any territorial agreements and potential rate changes.

The unique situation here for the FPSC to consider is allowing two utility providers to operate in the same territory and to serve the same customers. Historically, since the FPSC has had regulatory jurisdiction over public utilities in Florida, this has not been permitted.[3] Instead, the FPSC approves territorial agreements (which approvals are reviewable by the Florida Supreme Court) in which the utilities agree which entity will serve customers in service areas or resolves disputes regarding which utility will serve a service area. §§ 366.04(2)(d)-(e), Fla. Stat.

The policy behind permitting only one utility in a territory is because the existence of two providers in one area results in a duplication of facilities and distribution systems. *Storey v. Mayo*, 217 So. 2d 304, 306 (Fla. 1968). Duplication of facilities increases the cost of service per customer because two separate systems are being supplied and maintained where one should be sufficient. *Id.* "The ultimate effect of this is that the rates charged in the affected area are necessarily higher, or, alternatively, the customers in some other part of the system must help bear the added cost." *Id.* This policy has been codified in the statutes, which provides the FPSC with "jurisdiction over the planning, development, and maintenance of a coordinated electric power grid throughout Florida to assure an adequate and reliable source of energy for operational and emergency purposes in Florida and the avoidance of further uneconomic duplication of generation, transmission, and distribution facilities." § 366.04(5), Fla. Stat.

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[2] The FPSC has different jurisdiction over "public utilities," which included private, investor-owned utilities and municipality-owned utilities and cooperatives. § 366.04, Fla. Stat. The FPSC fully regulates public utilities (§ 366.04(1), Fla. Stat.), but it does not specifically regulate municipal utilities. Instead, it can only regulate specific things related to municipal utilities, such as rate structure (§ 366.04(2)(b), Fla. Stat.); territorial agreements (§ 366.04(2)(d), Fla. Stat.); territorial disputes (§ 366.04(2)(e), Fla. Stat.); and reporting (§ 366.04(2)(f), Fla. Stat.).

[3] Prior to 1951, local governments, usually municipalities, regulated utilities by providing franchises to utilities to provide service within some or all of the municipality. *See Drawing the Lines: Statewide Territorial Boundaries for Public Utilities in Florida*, Richard C. Belleck & Martha Carter Brown, 19 Fla. St. U. Law Rev. 2, p. 409 (Fall 1991).

In considering whether to approve a territorial agreement, the FPSC rules identify consideration, at a minimum, of the following factors: 1) the reasonableness of the purchase price of any facilities being transferred; 2) the reasonable likelihood that the agreement, in and of itself, will not cause a decrease in the reliability of electrical service to the existing or future ratepayers of any utility party to the agreement; and 3) the reasonable likelihood that the agreement will eliminate potential uneconomic duplication of facilities. Fla. Admin. Code R. 25-6.0440(2).[4] The cases addressing both approvals of agreement and territorial disputes are very fact-specific.

The ultimate consideration, in both approving a territorial agreement (and modifications thereto) and resolving a dispute is what is best for the public interest. *See Gulf Coast Co-Op, Inc. v. Johnson*, 727 So. 2d 259, 264 (Fla. 1999). In short, "the Commission's charge in proceedings concerning territorial agreements is to approve those agreements which ensure the reliability of Florida's energy grid and to prevent needless uneconomic duplication of electric facilities so long as the agreement works 'no detriment to the public interest.'" *Ameristeel Corp. v. Clark*, 691 So. 2d 473, 478 (Fla. 1997). The FPSC and the Supreme Court also encourage settlement of territorial matters. *Id.*

Despite the history of setting territorial areas that include only one utility provider, there is no explicit provision in statute or rule that specifically states that there cannot be more than one utility in a service area. In fact, in *Gulf Coast Electric Cooperative, Inc. v. Johnson*, 727 So. 2d 259 (Fla. 1999), the Florida Supreme Court specifically held that "the PSC is not required as a matter of law to establish territorial boundaries in order to resolve a territorial dispute that does not involve service to a current or future identifiable customers." *Id.* at 264. In *Gulf Coast*, the Court explained that two utilities had comingled facilities and there were areas of the counties that were undeveloped. *Id.* at 261. There was not a present dispute about serving a particular customer, but *Gulf Coast* sought territorial boundaries for future service. *Id.*

The FPSC concluded that there was no assurance that a territorial boundary was going to be the most effective way of providing service. It noted that because facilities were comingled, a line on the ground would not cure future or past duplication and instead would eliminate flexibility to determine who was in the best economic position to serve future customers. Instead, the FPSC would exercise its jurisdiction on a case-by-case basis. *Id.*

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[4] Rule 25-6.044(1) sets out items to be included in an application for approval of a territorial agreement which includes: a map and description of the area covered by the agreement; terms and conditions of the agreement; number and class of customers transferred; assurance that affected customers have been contacted and differences in rates explained; and information on acceptance of agreement "i.e. the number in favor of and those opposed to the transfer." Following the example of FPL/City of Vero Beach (COVB) filing, these application requirements should not apply in this case. Similar to FPL/COVB's filing for a termination of their agreement, JEA and Newco should file for a modification to existing territorial agreements to add Newco as a party to the agreement, thus avoiding these application requirements. The FPL/COVB petition did not address "reasonableness of purchase price" – only reliability of electric service going forward and the potential for uneconomic duplication. The purchase price was discussed in the companion filing requesting approval to charge FPL's existing rates and an acquisition adjustment to previous COVB customers.

The Supreme Court noted that this case was different from prior cases as there was not a current dispute over customers. *Id.* at 263. The Court noted that "there is no explicit authority for the PSC to impose territorial boundaries." *Id.* Instead, that authority came from the statutory provisions that permitted the FPSC to approved territorial agreements and resolve disputes. *Id.* The Court ultimately held that the FPSC was not required as a matter of law to establish territorial boundaries in this case. In doing so, it explained that "the public interest is the ultimate measuring stick to guide the PSC in its decisions." *Id.* at 264. The Court considered all of the factors and agreed that the PSC's determination that the parties should establish guidelines for resolving future service disputes was "a better solution in this case." *Id.* at 265.

Although it does not directly address the issue in this case, *Gulf Coast* highlights several important points. First, there is no explicit authority requiring the FPSC to set territorial boundaries. Next, the FPSC has the authority to consider the best solution for the situation. Finally, the best interest of the public is paramount. In short, this case stands for the proposition that the FPSC is not constrained to one way of resolving disputes or considering the interests of the public.

The two cases in which a private entity purchased assets from a municipality are very fact-specific. However, there are a few things that are important to take away from these cases. First and foremost, in both cases, the emphasis is on what is in the best interest of the public.

In *Sebring*, the utility was facing severe financial troubles, which was going to result in a huge increase in customer bills without a sale to a private entity. *Sebring*, at p. 2. In *Vero Beach*, although there was not a financial issue, there had been years of litigation between many parties involving the City's provision of utilities. There was extreme dissatisfaction of many customers and many attempts to rectify the concerns through attempted legislation and litigation. *Vero Beach*, pp. 6-7. Although the FPSC did not decide whether to approve the actual sale in these cases, the above factors were considered in what rates could be approved and whether to approve the territorial agreements. The overriding consideration was the public interest. In these cases, the existing structure was found to be detrimental in some way and the change in the best interest of the public.

II. Proposed Structure Between JEA and Newco

As in *Gulf Coast*, this case is different than any case that has come before it. There is nothing in the statute that prohibits the structure suggested. In fact, the Commission's jurisdiction is limited to what it can review and it does not include the sale of the assets. The FPSC, however, does review other related issues, such as the territorial agreement and rates, and it has broad authority to ascertain what is in the public's best interest. Any territorial agreement cannot be to the detriment of the public.[5] Any changes, new agreements, and rates will have to be in the best interest of the public.

[5] *Utilities Commission of City of New Smyrna Beach v. Florida Public Service Commission*, 469 So. 2d 731 (Fla. 1985).

The entire policy behind having territorial areas that are served by only one entity is to protect the public from uneconomic duplication of facilities, higher costs, and discriminatory costs (when some customers are paying for usage by other customers). In this case, the intent of the structure is to not violate any of these underlying policies. There will not be any competition for customers as it will be expressly explained as to how the customers will receive power—in part from the JEA up to a specified limit, and then from Newco. There will not be any duplication of facilities as Newco will purchase all assets and be responsible for all administrative tasks. To the extent the JEA will directly provide some utility service, it will utilize Newco's facilities and this should be explicitly explained in the agreement. Because there is no competition or duplication of facilities, there should not be increased costs. To the extent there is any concern about future competition, this concern could be alleviated by a provision in the agreement that states once the agreement with the Georgia Plants is terminated, Newco will serve all customers exclusively.

Although the *Sebring* and *Vero Beach* cases are very fact specific, both cases considered both the public's interest in maintaining the utility services as they existed and the service after the sale based on all of the information presented. It is likely the FPSC would approach this case in the same way. Essentially, the FPSC may compare the current system and provision of services to see if the suggested changes will be better or more advantageous to the public. The FPSC could go beyond looking at the factors in the rule for approving territorial agreements and may consider other factors such as additional conservation programs, the customers' preferences, and any problems facing the current provision of services.

There are several things the FPSC could consider in this structure that may be unique here and would not be an issue when only one provider is present in a service area. For example, the FPSC may have concerns about customer confusion. It would likely not be in the best interest for the customer to receive two bills or bills with charges from two companies that may be different. It is my understanding that this has been considered and only one bill would be provided by Newco with a surcharge for JEA's charges. This may alleviate that concern.

Another consideration is whether there will be different rates and how these would be explained. JEA and Newco will want to ensure that there are not any discriminatory charges.[6]

Finally, it is expected that the FPSC will want to ensure the case does not set a precedent of allowing multiple utilities to serve one service area. This concern can be alleviated by an explanation of why this situation is unique (because of the lengthy contract with the Georgia Plants, which could result in a huge tax consequence, which will ultimately be passed on the customers in their bill, if transferred to a private entity). In *Sebring*, the FPSC stated that it did not usually approve some of the things that it approved, but stated "unique problems require unique solutions" and "we uncategorically state that this decision has no precedential value." *Sebring*, at p.11. The FPSC could make specific similar clarifications in its order as to the unique situation here.

[6] A surcharge may be considered part of the "rate structure," over which the FPSC has jurisdiction for municipal utilities. § 366.04(2)(b), Fla. Stat.; *Polk Cnty. v. Fla. Pub. Serv. Comm'n*, 460 So. 2d 370, 372 (Fla. 1984).

In considering whether a territorial agreement can include the type of structure listed above and not simply a division of territories, the definition of a territorial agreement is "a written agreement between two or more electric utilities which identifies the geographical areas to be served by each electric utility party to the agreement, the terms and conditions pertaining to implementation of the agreement, and any other terms and conditions pertinent to the agreement." Fla. Admin. Code R. 25-6.0439(1). Here, the agreement would include the areas served by each party: each party would serve the same geographical areas. It would also include the specific terms and conditions of that service: the JEA will provide service up to the limit of the power it is contracted to receive from the Georgia Plants and Newco will provide everything else. The agreement will consider other pertinent terms, such as how exactly this will function and how the customers should be provided will clear and simple information about the service.

III. Impact of Franchise Agreements

It is anticipated that the COJ will be in agreement with the modifications and will issue two franchises: one to the JEA (or modify the one they already have) and one to Newco. These franchises will be exclusive to only these two entities.

While the FPSC has authority over territorial agreements, COJ has jurisdiction over specific franchises that it authorizes and for which it receives payment. The FPSC's jurisdiction is "exclusive and superior to that of all other boards, agencies, political subdivisions, municipalities, towns, villages, or counties, and in case of conflict therewith, all lawful acts, orders, rules, and regulations of the commission shall in each instance prevail." § 366.04(1), Fla. Stat. "A franchise agreement between a local government and an electric utility cannot override a territorial order." *In re: Petition for modification of territorial order based on changed legal description emanating from Article III, Section 2(c) of the Florida Constitution by the Town of Indian River Shores*, Order Number PSC-16-0427-PAA-EU, p. *13 (Fla. P.S.C.).

The Florida Supreme Court recently discussed the interplay between a local franchise to a utility and the FPSC's Jurisdiction. *See Bd. of Cnty. Comm'nrs Indian River Cnty. v. Graham*, 191 So. 3d 890 (Fla. 2016). In *Graham*, the County had a franchise agreement with the City granting it the exclusive right to use City property to construct, maintain, and operate an electric system in certain parts of the County. *Id.* at 892. The franchise agreement was expiring and the County indicated that it would not renew the agreement. *Id.* Prior to the execution of the franchise agreement, the FPSC had issued territorial orders approving the City's service area (with later amendments). *Id.* The City and the County both sought declaratory statements as to their rights at expiration of the agreements, and the FPSC ordered that the City had the right and the obligation to continue to provide electric retail service as described in the territorial agreement upon expiration of the franchise agreement. *Id.* at 893.

The County appealed, arguing in part that the declaration exceeded the FPSC's authority by interpreting the franchise agreement. The Court disagreed, noting that the FPSC's order specifically stated that it was not interpreting the franchise agreement and acknowledging that the declaration was "at odds with the County's position that the territorial order become void with respect to the franchise area when the Franchise Agreement expires." *Id.* at 895. The Court found, however, that the FPSC's order did not address any dispute that might arise as a result of the

franchise agreement, such as franchise fees, access to property, or territorial disputes. *Id.* The order simply declared that the City must continue to serve pursuant to the FPSC's territorial orders. *Id.*

The Court also rejected the County's contention that the declaration granted property rights to the City. *Id.* at 896. The Court explained that while it was a well-established principle that a franchise agreement was an enforceable contract governing the use of property, a local government franchisor did not get to decide which utility provider served a given area. *Id.* Moreover, the FPSC's order did not prevent the County from requiring the utility to pay a fee for use of government property because the FPSC's declaration was limited to the City's obligations under its territorial agreements, which is within the FPSC's exclusive and superior jurisdiction. *Id.*

In general, a franchise agreement and a territorial agreement are separate issues. The FPSC's order approving a territorial agreement is the ultimate authority as to who can provide the service in the service area. The franchise agreement provides the duties of the municipality granting the franchise and the utility using governmental property. The FPSC can require compliance with the territorial agreement regardless of the franchise agreement, but the franchise agreement dictates the contract terms as to what happens at termination of the franchise agreement in other respects.

Here, if the COJ is in agreement and intends to grant franchises to both parties, there should not be any concerns. The franchise agreements (or prospective agreements) may be considered by the FSPC as giving local authority for both utilities to serve the area. Here, the franchise agreements could include a provision that the franchise terminates for the JEA when it is no longer under contract to provide electricity from the Georgia Plants, and Newco will be the exclusive franchisee at that point.

Conclusion

There is no statute, rule, or case that prohibits the proposed JEA/Newco territorial structure although it is unique. The FPSC's consideration will be very fact-specific and will ultimately consider the best interests of the public. Evidence should be directed to all aspects of the proposed structure and how it will impact customers with a comparison of how the current structure will impact customers in the future if it is not changed. A franchise to both entities does not impact the FPSC's authority to determine who serves a specific territory. The FPSC has the exclusive and superior authority to decide territorial services areas, but the FPSC does not have any involvement in the franchise agreement's terms and rights.