1374.

UTILITIES—MUNICIPALLY OWNED—MUNICIPALITY ACTS IN PROPRIETARY CAPACITY—AUTHORITY: FIX RATE SCHEDULES, OPERATE, COVER COSTS, REPAIRS, ENLARGEMENTS, EXTENSIONS, PAY INTEREST, CREATE SINKING FUND, PAY DEBTS, NOTES OR BONDS—ELECTRIC PLANT—COUNCIL OR LEGISLATIVE AUTHORITY —WATERWORKS—LIMITATIONS AS TO PROFITS—RATE MUST NOT BE EXCESSIVE, UNREASONABLE OR DISCRIMINATORY—SECTIONS 3959, 5625-13a, G. C.

SYLLABUS:

1. In the ownership and operation of municipally owned utilities, a municipality acts in its proprietary capacity.

2. A municipality, in the operation of its municpally owned utility and the fixing of schedules of rates to be charged for the furnishing of the product and service of the utility to its inhabitants should fix those rates and operate the utility so that it will at least be self-supporting, that is to say, so that the receipts from the operation of the utility will at least be sufficient to cover operating costs, repairs, necessary enlargements and extensions, the payment of interest on any loans that may have been made for the construction of the utility or that may be made for enlargements or extensions and sufficient for the creation of a sinking fund for the liquidation of such debts or the payment of serial notes or bonds that may have been given for such debts, as the case may be.

3. Rates to be charged for the product and service of a municipally owned electric plant may be lawfully fixed by the council or other legislative authority of the municipality so that by the collection thereof the operation of the plant will show a fair and reasonable profit to the municipality after cost of operation and reasonable depreciation and amortization are taken care of.

4. In the absence of statutory limitation upon such action, courts will not prohibit a municipality from making a fair and reasonable profit in the operation of its publicly owned utility.

5. Unless restricted by statute as to the use to which balances accruing from the operation of a municipally owned utility may be put, as in the case of waterworks in Section 3959, General Code, a municipality may transfer such balances if any, to other funds of the municipality by authority of Section 5625-13a, General Code, and thereafter use the funds for purposes within the purview of the fund to which they have been transferred.

6. Whether or not utility rates for the product or service of a municipally owned utility are to be fixed so that a profit will accrue to the municipality from the operation of the utility is a matter within the sound

discretion of the council or other legislative authority as the rate making body for the municipality limited only by the fact that such rates must not be excessive, unreasonable or discriminatory.

7. Municipal authorities, if they determine to make a profit from the operation of a municipally owned utility, should bear in mind that municipal ownership implies the furnishing of the product or service of the utility at the lowest cost possible consistent with efficiency, service, quality of the commodity and the preservation of the plant, and profits should not be used to create manifest preferences or discrimination among taxpayers.

COLUMBUS, OHIO, November 2, 1939.

Bureau of Inspection and Supervision of Public Offices, Columbus, Ohio.

GENTLEMEN: You have submitted for my consideration and opinion certain correspondence and data relating to the operation of a municipally owned electric plant in the city of ..... It appears from this data that a surplus has accumulated over a period of years from the operation of this plant and an ordinance proposing the reduction of rates by reason thereof has been submitted to council. With respect thereto, the auditor of the city has requested from you an expression as to the advisability of reducing the rates under the circumstances. With respect thereto he states in his letter to you:

> "* * * an ordinance has been presented to reduce the rates in the City of ..... to the extent of $8,000.00 annually and from the attached statement you will note that the average gross profit in the three years that the present rates have been in effect has been $19,000.00. You will also note that the table showing equipment costs and depreciation show that $16,000.00 per year is required for depreciation, leaving a net profit of $3,000.00.
>
> The surplus now in the Electric Light Plant is $25,000.00 and on making a rough estimate of the amount necessary to meet depreciation to date the surplus should be approximately $65,000.00.
>
> We would appreciate it if you would favor us with your opinion, first, regarding the setting up of a depreciation account and second, as to the advisability of a reduction in the electric rates under present financial conditions."

The specific questions submitted by you to me for my opinion, are as follows:

> "May a municipally owned electric light plant be operated at a profit greater than sufficient to cover all the purposes

enumerated in section 3959 G. C., and in sufficient amount to at least equal a cash reserve for depreciation?

If the answer to the above question should be in the negative, due to the arbitrary method and rates employed in computing depreciation on such plants, would it be your opinion that council of the city in question is justified in reducing the electric rates in view of the fact that a cash surplus exists in the electric light fund in the amount of $25,000?"

You refer to an opinion of a former Attorney General found in the reported Opinions of the Attorney General for 1933, page 417, as follows:

> "Inasmuch as waterworks, gas and electric light plants have the same classification, all opinions relative to waterworks will also apply to light plants."

With respect to the above quotation, it should be observed that the statement of the Attorney General quoted above should be read in view of the facts upon which it was predicated and the question presented and then under consideration. An examination of the opinion in which it appears discloses that the question under consideration was the duties and powers of a board of trustees of public affairs in a village in the construction of an electric plant in the village. The then Attorney General, after quoting from a 1927 opinion which dealt with the powers of a board of trustees of public affairs in a village with respect to the construction of municipal waterworks plants, followed this quotation with the observation quoted above. This statement of the Attorney General should not be considered as applying to all situations.

It should also be noted that Section 3959, General Code, which is mentioned in your inquiry has no application whatever to funds or surpluses derived from the operation of municipal electric plants. It specifically relates to waterworks and cannot by any course of reasoning be made to apply to anything else. No similar statutory provision exists which relates to the funds or surpluses accruing from the operation of electric plants or those of any utility except waterworks. Said Section 3959, General Code, reads as follows:

> "After paying the expenses of conducting and managing the water works, any surplus therefrom may be applied to the repairs, enlargement or extension of the works or of the reservoirs, the payment of the interest of any loan made for their construction or for the creation of a sinking fund for the liquidation of the debt. The amount authorized to be levied and assessed for water works purposes shall be applied by the council to the creation of the sinking fund for the payment of the indebtedness

incurred for the construction and extension of water works and for no other purpose whatever."

Before further discussing the subject of your inquiry it should also be noted with respect to the second branch thereof that it would not be proper, in my opinion, for me, as Attorney General, to express any opinion as to whether or not the council of the city in question is "justified" in reducing electric rates under existing circumstances. The entire matter of fixing utility rates for municipally owned utilities and of controlling receipts and surpluses arising from the operation of such utilities with the exception of municipal waterworks, is left to the sound discretion of the legislative branch of local government in the municipality which owns and operates them.

The state may, no doubt, in the exercise of its sovereign police power, regulate the rates which a municipality may charge for the products of its utilities furnished to its inhabitants, but in this state it has not done so, nor has it delegated that power to any subordinate agency. The supervision and regulation of utilities owned or operated by a municipality, are specifically exempted from the jurisdiction of the Ohio Public Utilities Commission by Section 614-2a of the General Code, and are not reposed by statute in any administrative board, commission or agency. Of course, the courts in the exercise of judicial power, and limited only by the terms of the Federal Constitution, particularly the due process provisions of the Fourteenth Amendment may, in a proper action review the action of a municipal council in fixing utility rates, and will, if the rates are unreasonable or discriminatory, enjoin their collection. Butler v. Karb, 96 O. S., 472; Shirk v. Lancaster, 313 Pa. 158, 169 A. 557. Practically the only limitation upon the fixing of such rates is that they must be reasonable, not excessive, and non-discriminatory. The determination of what is a reasonable rate presents considerable difficulty, involving as it does the determination of a proper rate base, as well as the determination of the limits of a fair and reasonable profit. I do not wish to be understood as attempting in this opinion to state what constitutes a proper rate base for the fixing of utility rates. Suffice it to say that by the weight of authority the determination of facts and values upon which a proper rate base for the fixing of municipal utility rates rests, should be made in the same manner as though a private corporation were involved. Shirk v. Lancaster, supra. And it is stated on good authority that "the same rules as to reasonableness of rates apply as in the case of private corporations owning a public utility and furnishing service to the municipality and its inhabitants." McQuillin on Municipal Corporations, 2d Ed., Sec. 1948. Citing Logansport v. Public Utility Company, 202 Ind., 523; Holton Creamery v. Brown, 137 Kans., 418.

The above statement should perhaps not be taken as being applicable to all the rules by which the reasonableness of rates is measured. While

there is a dearth of authority on the subject, and in fact I have found no case wherein the question has been discussed at any considerable length, there is some doubt whether the courts would uphold the making of as great a profit by municipally owned utilities as that permitted a privately owned one. It might be noted at this point, that Judge Day, in the course of his opinion in the case of City of Niles v. Ice Corporation, 133 O. S., 169, stated on page 183:

> "Where, however, the rates charged are excessive, a municipality is amenable to the same laws governing rates as a private corporation would be when engaged in a public utility business. But we need not here dwell on this point, since no complaint is made that the rate or charge is excessive."

The question of excessive rates or excessive profits for either a municipally owned utility or a privately owned one was not involved in that case, but it throws some light on the question of whether or not any profit may be made by a municipally owned utility in the absence of statutory regulation, which is the primary question involved in your inquiry.

It is well settled by the great weight of authority that publicly owned utilities may make a profit. The same authorities all hold that the profit must not be an unreasonable profit. Nowhere will be found any definite rules as to what constitutes an unreasonable profit.

The earlier cases which involved the question of power of municipal ownership of utilities based the justification for that power largely on the motive of securing for the inhabitants of a municipality satisfactory service at a fair, uniform rate. In Pond on Public Utilities, 4th Ed. Section 865, it is said:

> "Naturally the purpose and chief motive of the privately owned municipal public utility is to secure the largest possible return on its investment, while the motive of the municipality in furnishing such service by its own plant is not primarily selfish or mercenary beyond the point of making the business self-sustaining: its chief object being rather to furnish efficient comprehensive service to its inhabitants at cost. That the municipality has the power and that it is its duty to provide public utility service itself, when it is not furnished satisfactorily by private enterprise at reasonable rates is the consensus of opinion in our courts generally."

The observation of the author in the text quoted above with respect to the primary purpose of the establishment and operation of municipally owned utilities and the motive which justified the extension of power to establish and operate those utilities did not deter the author from stating

in a later section, 868, that the determination of rates was a matter largely within the discretion of the municipal authorities. In this section the author states:

> "As the policy of municipal ownership is a legislative and not a judicial question the rate which a municipality may charge for public utility service and the disposition of the proceeds (in the absence of statute) so long as they are used for municipal purposes, rests largely in the discretion of the municipal authorities, whose judgment in such matters will not be set aside by the courts unless unreasonable or ultra vires."

In the support of the text there is cited the case of Travaillie v. Sioux Falls, 59 S. D., 396, 240 N. W., 336, and a number of other cases.

In this state municipalities derive their power to acquire and operate public utilities for the purposes of supplying the product and service thereof to the municipality or its inhabitants, not from the Legislature, but direct from the Constitution of Ohio, Article XII, Section 4. In the operation of a public utility, a municipality acts not in a governmental capacity as an arm or agency of the sovereignity of the State, but in a proprietary or business capacity. In its proprietary capacity it occupies the same "posture" as that occupied by a private corporation engaged in business. Travellers Insurance Company v. Village of Wadsworth, 109 O. S., 440; Butler v. Karb, supra; City of Niles v. Ice Corporation, 43 C. J., 420, Section 551.

While some few courts in other states have held otherwise, it is well settled by the great weight of authority in this state and elsewhere, as stated above, that in the absence of statutory restriction, municipally owned utilities may be operated so that a reasonable profit will accrue therefrom and, of course, that fact may be taken into consideration in the determination of proper rates .

McQuillin on Municipal Corporations, 2d Ed. Sec. 1948;
Ruling Case Law, Vol. 27, p. 1438;
67 Corpus Juris, Sec. 784, p. 1236;
Farnum on Water Rights, Sec. 145, p. 162;
City of Niles v. Ice Corporation, supra;
Twitchell v. City of Spokane, 55 Wash., 86;
Preston v. Water Commissioners, 117 Mich., 589;
Wagner v. City of Rock Island, 146 Ill., 139;
Shirk v. Lancaster, 313 Pa., 158;
Culver v. Jersey City, 45 N. J. L., 256.

Since the decision of the case of Niles v. Ice Corporation, supra, de-

cided by the Supreme Court of Ohio in 1938, the question of the right of a municipal corporation to make a reasonable profit from the operation of municipally owned electric plants is no longer an open one. In the course of the opinion in that case, Judge Day, after stating the contention of the appellants that a municipal corporation is not permitted to charge for the product of its electric plant a rate in excess of the cost of furnishing the service or product, says:

> "This contention proceeds on the theory that a municipality has no right to charge for its utility service or product a rate in excess of cost, i. e., that it has no right to make a profit. Nevertheless, we are not referred to any statute or constitutional provision denying this right. In the absence of such prohibition, a municipality, no less than a private corporation engaged in the operation of a public utility, is entitled to a fair profit."

The holding of the court in the Niles case as stated in the syllabus is as follows:

> "1. The provisions of Section 5625-13a, General Code, relate to the transfer of funds of a political subdivision, whether tax-derived or not, and include, in their authorization to transfer funds derived from the maintenance and operation of an electric light and power system, but do not apply to waterworks funds by reason of the provisions of Section 3959, General Code. (Paragraph 2 of the syllabus in the case of City of Lakewood v. Rees, 132 Ohio St., 399, modified in part.)
>
> 2. A patron, purchasing electric energy from a municipally owned electric light and power plant or system, occupies, with respect to the purchase price, the same position as if the purchase were made from a private corporation engaged in the same business. The patron loses all interest in the control over the purchase price after it is paid, and it becomes the exclusive property of the municipality, with the right to use, transfer or divert it to any uses and purposes authorized by law.
>
> 3. Section 5625-13a, General Code, permitting political subdivisions to transfer 'any public funds under its supervision' to another fund, does not release municipal corporations from the limitations upon their taxing power, imposed by the Constitution."

Even in jurisdictions where the trust fund theory as to receipts and balances accruing from the operation of publicly owned utilities prevails, which is not the case in Ohio (Niles v. Ice Corporation, supra) municipalities are permitted to make a profit from the operation of those utilities. See Shirk v. Lancaster, supra.

In view of the foregoing discussion and the authorities cited, it is my conclusion:

1. In the ownership and operation of municipally owned utilities, a municipality acts in its proprietary capacity.

2. A municipality, in the operation of its municipally owned utility and the fixing of schedules of rates to be charged for the furnishing of the product and service of the utility to its inhabitants should fix those rates and operate the utility so that it will at least be self-supporting, that is to say, so that the receipts from the operation of the utility will at least be sufficient to cover operating costs, repairs, necessary enlargements and extensions, the payment of interest on any loans that may have been made for the construction of the utility or that may be made for enlargements or extensions and sufficient for the creation of a sinking fund for the liquidation of such debts or the payment of serial notes or bonds that may have been given for such debts, as the case may be.

3. Rates to be charged for the product and service of a municipally owned electric plant may be lawfully fixed by the council or other legislative authority of the municipality so that by the collection thereof the the operation of the plant will show a fair and reasonable profit to the municipality after cost of operation and reasonable depreciation and amortization are taken care of.

4. In the absence of statutory limitation upon such action, courts will not prohibit a municipality from making a fair and reasonable profit in the operation of its publicly owned utility.

5. Unless restricted by statute as to the use to which balances accruing from the operation of a municipally owned utility may be put, as in the case of waterworks in Section 3959, General Code, a municipality may transfer such balances, if any, to other funds of the municipality by authority of Section 5625-13a, General Code, and thereafter use the funds for purposes within the purview of the fund to which they have been transferred.

6. Whether or not utility rates for the product or service of a municipally owned utility are to be fixed so that a profit will accrue to the municipality from the operation of the utility is a matter within the sound discretion of the council or other legislative authority as the rate-making body for the municipality, limited only by the fact that such rates must not be excessive, unreasonable or discriminatory.

7. Municipal authorities, if they determine to make a profit from the operation of a municipally owned utility, should bear in mind that municipal ownership implies the furnishing of the product or service of the utility at the lowest cost possible consistent with efficiency, service, quality of the commodity and the preservation of the plant, and profits

should not be used to create manifest preferences or discrimination among taxpayers.

Respectfully,
THOMAS J. HERBERT,
Attorney General.

1375.

CONTRACT—COOPERATIVE, STATE WITH VILLAGE OF BARNESVILLE, BELMONT COUNTY, IMPROVEMENT S. H. 295, ALONG MAIN SREET FROM BALTIMORE AND OHIO RAILROAD AT ARCH STREET, APPROXIMATELY 0.628 MILE.

COLUMBUS, OHIO, November 2, 1939.

HON. ROBERT S. BEIGHTLER, *Director, Department of Highways, Columbus, Ohio.*

DEAR SIR: You have submitted a cooperative contract between the Director of Highways and the Village of Barnesville, covering the following improvement:

> Being all of that portion of the Barnesville-Bellaire Road State Highway No. 295, as extended over and along Main Street in the Village of Barnesville, Ohio, from the Baltimore and Ohio railroad at Arch Street, southeast, then northeast, for a distance of approximately 0.628 mile, to Station 33 plus 17 and there terminate.

Finding said contract proper as to form and legality, I have accordingly endorsed my approval thereon, and return the same herewith.

Respectfully,
THOMAS J. HERBERT,
Attorney General.

1376.

MINIMUM WAGE—FOOD AND LODGING BUSINESS—DIRECTOR, DEPARTMENT INDUSTRIAL RELATIONS—NO AUTHORITY UNDER MINIMUM FAIR WAGE STANDARDS TO MODIFY DIFFERENTIALS IN RATES ESTABLISHED BY WAGE BOARD—SUCH MODIFICATION DEPARTURE FROM BASIC MINIMUM RATES—SECTIONS 154-45d TO 154-45t, G. C.

SYLLABUS:

The Director of the Department of Industrial Relations had no authority under the provisions of the Minimum Fair Wage Standards to