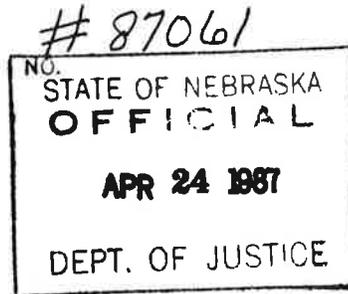


DEPARTMENT OF JUSTICE

STATE OF NEBRASKA

TELEPHONE 402/471-2682 • STATE CAPITOL • LINCOLN, NEBRASKA 68509



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DATE: April 21, 1987

RE: Constitutionality of LB 663 - Due Process  
Requirements Regarding Natural Gas Rate-Making by  
Nebraska Municipalities

REQUESTED BY: Senator David Landis  
Nebraska State Legislature

WRITTEN BY: Robert M. Spire  
Attorney General

L. Jay Bartel  
Assistant Attorney General

You have requested our opinion regarding the constitutionality of LB 663. Generally, LB 663 proposes to amend Nebraska statutory provisions relating to the establishment of natural gas rates by municipalities. Your question concerns to what extent procedural due process safeguards are constitutionally required with regard to a municipality enacting an ordinance making or changing rates of a gas supplier operating as a public utility.

The general rule regarding the application of the due process requirements of notice and hearing in the context of public utility rate determination proceedings is stated in 73B C.J.S. Public Utilities §44 (1983) as follows:

The nature of a rate determination proceeding before a public service commission depends on constitutional and statutory provisions, which may determine whether notice and hearing are necessary before tariffs become effective. Where the nature of proceedings is judicial or quasi-judicial in character, notice and hearing are necessary, and hearings not in accordance with constitutional and statutory provisions contravene procedural due process. However, it has been held that where tariff procedures are described and characterized as being legislative in nature, a due process hearing is not necessary. (Footnotes omitted).

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The Nebraska Supreme Court has adopted the view that the act of a public body in determining a rate for a public utility constitutes action in a legislative, as opposed to a judicial, capacity. City of Scottsbluff v. United Tel. Co. of the West, 171 Neb. 229, 106 N.W.2d 12 (1960); Yellow Cab Co. v. Nebraska State Railway Commission, 176 Neb. 711, 127 N.W.2d 211 (1964). Specifically, with regard to the actions of a municipality in the context of determining gas rates within the city, the court has stated:

A municipal corporation in fixing rates to be charged by a public utility acts in a legislative rather than a judicial capacity. (Citations omitted). By statute, the Legislature has delegated to municipalities the authority to regulate, determine, and fix rates. This power being legislative in nature, it cannot be assumed by the courts and this court cannot usurp the functions of a rate-making body.

Kansas-Nebraska Natural Gas Co., Inc. v. City of Sidney, 186 Neb. 168, 170, 181 N.W.2d 682, 683 (1970). See also Kansas-Nebraska Natural Gas Co. v. City of St. Edward, 167 Neb. 15, 91 N.W.2d 69 (1958). See generally 64 Am.Jur.2d Public Utilities §89 (1972).

The mere characterization of rate setting as a legislative function, however, is not in and of itself sufficient to determine the necessity to provide notice and hearing comporting with full procedural due process requirements to utilities regarding rate determinations. It is well-established that public utilities are entitled to a just and reasonable compensation or a fair return on property used for public service. Kansas-Nebraska Natural Gas Co. v. City of Sidney, supra. Rates fixed by government authorities which are not sufficient to yield a fair return to a public utility are deemed unjust, unreasonable, and confiscatory. American Toll Bridge Co. v. Railroad Commission of California, 307 U.S. 486 (1938). Enforcement of such confiscatory rates deprives the utility of its property in violation of constitutional guarantees safeguarding private property against taking for a public use and due process of law. West v. Chesapeake and Potomac Tel. Co., 295 U.S. 662 (1934); U.S. Const., amend. 5 and amend. 14; Neb. Const., art. I, sec. 3, and Art. I, sec. 21; See generally 64 Am.Jur.2d Public Utilities §134 (1972).

Based on the property right implications associated with public utility rate-making, courts have recognized the need for procedural due process safeguards in the rate-making process. In essence, the right to procedural due process in this context requires providing the utility with adequate notice and an opportunity to be heard, consistent with the essentials of a fair

trial. Railroad Commission of California v. Pacific Gas and Electric Company, 302 U.S. 388 (1937); Ohio Bell Tel. Co. v. Public Utilities Commission, 301 U.S. 292 (1937); Morgan v. United States, 298 U.S. 468 (1936).

While it is clear that a public utility is entitled to notice and an opportunity to be heard at a trial-type hearing in the course of the rate setting process, there is authority to support the proposition that such hearing need not be provided at the legislative or administrative level if provision is made for a trial de novo before a court in which evidence may be offered and a full opportunity provided to address the propriety of rates established as a result of the legislative process. Mayfield Gas Co. v. Public Service Commission, 259 S.W.2d 8 (Ky. 1953); See Jordan v. American Eagle Fire Ins. Co., 169 F.2d 281 (D.C. Cir. 1948); See also Ohio Bell Tel. Co. v. Public Utilities Commission, supra. In Jordan v. American Eagle Fire Ins. Co., supra, the court, after citing a number of cases dealing with due process requirements in the public utility rate setting process, summarized these decisions as follows:

Rate-making procedures differ. Sometimes they are state or local tasks and sometimes federal tasks, and the functions of particular courts differ according to the place of the court in the procedure involved. . . . [T]he state legislature may prescribe a procedure in which the initial order is upon legislative or wholly administrative consideration and the full hearing is afforded in a court action. If the court proceeding includes the full right to present evidence, to meet issues, and to explore the evidence and conclusions of the legislative or administrative agent, due process of law exists. . . . However, if the state procedure consists of administrative consideration without hearing, and court consideration merely by way of review of the determination below without new evidence or exploration by cross-examination, a federal court will set aside the final order as without due process. In modern times, most states, like the federal government, provide for a full hearing in the course of the administrative consideration, thus making that proceeding quasi-judicial. In such instances the addition of a judicial review of the record, findings and conclusions made below, constitutes a combination of actions which satisfies the requirements of due process.

Reversing the lower court's determination that a full due process hearing was necessary at the legislative or administrative level, the court in Jordan stated:

The District Court rightly held that in rate-making proceedings, such as this, a full hearing in the judicial sense is required. We think it was in error in holding that that hearing must in all cases be afforded in the administrative or legislative process. As we see it, the modern custom of placing that hearing in that part of the procedure is a matter of desirability by reason of expertise, and not a matter of constitutional necessity.

Id. at 290-91.

Based on the foregoing, the Legislature has two options to consider with respect to satisfying procedural due process requirements regarding the establishment of natural gas rates by municipalities. One alternative would be to provide, by statute, for a complete, trial-type hearing before the municipal rate setting body. The other alternative, under the holding in Jordan v. American Eagle Fire Ins. Co., supra, would be to provide procedural due process in the form of a trial de novo in court following action by the municipal body.

An examination of LB 663 reveals that the bill appears to follow the second course of action, permitting a gas supplier to institute a court action in the event a municipality does not grant a requested rate increase. LB 663, §5(3). In view of Nebraska case law characterizing the rate setting process as legislative in nature, we cannot say that such a procedure, on its face, would be held unconstitutional as a denial of procedural due process. The right of a gas supplier to a trial de novo before a court under LB 663 provides the gas supplier with the entire panoply of rights accorded in a judicial proceeding, in the event the supplier is dissatisfied with the action taken by the municipal body in the rate setting process. The provision of a trial-type hearing at the judicial level, as opposed to the administrative or legislative level, has been held sufficient to satisfy due process requirements.

While there is authority to support such a procedure, it should be noted that the modern trend of practice appears to provide, by statute, for a hearing before the rate setting agency, either state public service commission or municipal rate setting body, including the essential elements of a trial-type hearing. E.g., Arkansas Public Service Commission v. Continental Tel. Co., 262 Ark. 821, 561 S.W.2d 645 (1978); City of Los Angeles v. Public Utilities Commission, 15 Cal. 3d 680, 542 P.2d

1371, 125 Cal. Rptr. 779 (1975); Glen Oaks Utilities, Inc. v. City of Houston, 161 Tex. 417, 340 S.W.2d 783 (1960). Generally, while rate-making has traditionally been labeled a "legislative" activity, these cases recognize the rate-making process actually partakes of a proceeding which is quasi-judicial in nature, involving the determination of factual findings relating to the individual company's operations, rate base, and required rate of return on investment. Arkansas Public Service Commission v. Continental Telephone Company, supra.

In light of these considerations, it is possible that the Nebraska Supreme Court, if called upon to reexamine the nature of the rate setting process in the context of addressing the issue of the need for a full due process hearing before a rate setting agency or body, may hold that such a proceeding actually constitutes a quasi-judicial process, necessitating procedural due process requirements of notice and an evidentiary, trial-type hearing. In this regard, we note that our Court has recognized the applicability of fundamental due process rights in the context of quasi-judicial proceedings. E.g., First Federal Savings & Loan of Lincoln v. Department of Banking, 187 Neb. 562, 192 N.W.2d 736 (1971) (Establishment of savings and loan associations); City of Auburn v. Eastern Nebraska Public Power District, 179 Neb. 439, 138 N.W.2d 629 (1965) (Granting of certificate of public convenience and necessity to construct electric transmission line); Block v. Lincoln Tel. and Tel. Co., 170 Neb. 531, 103 N.W.2d 312 (1960) (Withdrawal of existing telephone service from subscriber).

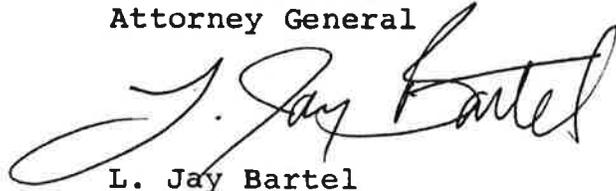
In summary, it is our opinion that, to the extent that LB 663 provides a gas supplier with the opportunity to receive a trial de novo before a court on the propriety of a full or partial denial of a requested rate increase, the bill could likely be successfully defended against constitutional attack on procedural due process grounds under the principles enunciated in Jordan v. American Eagle Fire Ins. Co., supra. This is particularly true in light of current Nebraska case law viewing the municipal rate setting process for public utilities as constituting a legislative activity. Kansas-Nebraska Natural Gas Co. v. City of Sidney, supra. Given the nature of the determinations involved in the rate setting process, however, including the various factual determinations previously discussed, we cannot definitively state that, if the Nebraska Supreme Court were called upon to examine the issue, the Court would not conclude that the determinations involved rendered the process quasi-judicial in character, and that the rate setting decision, affecting the rights and property of a specific

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company, necessitated a full due process hearing in the first instance before the rate setting agency or body.

Very truly yours,

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Assistant Attorney General

LJB/bae

cc: Patrick J. O'Donnell  
Clerk of the Legislature

APPROVED BY:



Attorney General