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Municipality Monopoly Is Not Fun For Everyone

Law360, New York (February 24, 2012, 1:28 PM ET) -- Unlawful tying arrangements are a frequent point of contention between electric cooperatives and municipalities. On Jan. 17, 2012, the U.S. Supreme Court let stand a decision that permits an unlawful tying/monopolization claim to go forward against the city of Newkirk, Okla.

The underlying facts are as follows: Newkirk and Kay Electric Cooperative are both electric providers in Oklahoma. Newkirk typically provides electric service to customers within its city limits, and Kay, a nearby utility, normally serves customers outside the city limits.

After it was announced that a new jail was being built outside the city limits of Newkirk, Kay offered to provide electricity. Newkirk, however, later annexed the area around the jail into the city limits and made its own offer.

Even though Kay offered a far more competitive rate for electricity than Newkirk, the jail chose Newkirk. The reasoning for that choice, as explained by the U.S. Tenth Circuit Court of Appeals, was that the jail found itself “stuck between a rock and a pile of sewage.” More specifically, Newkirk, as the only provider of sewage services in the area, refused to provide the jail with any sewage services unless the jail agreed to purchase electricity from Newkirk. (Click here for the opinion.)

The Tenth Circuit concluded that the facts, as alleged, showed an unlawful tying arrangement and attempted monopolization by Newkirk in violation of the Sherman Act. The court explained that “[w]hen a city acts as a market participant it generally has to play by the same rules as everyone. It can’t abuse its monopoly power or conspire to suppress competition.”

The only exception to that general rule is when the city’s parent state has clearly authorized the city “to upend normal competition.” But the court reasoned that Newkirk failed to show that Oklahoma provided any such authorization. “Put simply, at the end of the day, a municipality shares the state’s ‘immunity’ [from federal antitrust claims] ... only when it is implementing anticompetitive policies authorized by the state.”

To make matters worse for Newkirk, the court pointed out that Oklahoma’s Rural Electric Cooperative Act entitled rural cooperatives like Kay to continue serving areas they traditionally served, even after annexation by a city. Thus, not only did the Cooperative Act authorize Kay to compete in annexed areas, it also protected Kay from municipal interference in those areas.

In short, the “Oklahoma legislature has spoken with specificity to the question whether there should be competition for electricity services in annexed areas ... [a]nd it has expressed a clear preference for, not against, competition.”

Other states, of course, may not have the same legislative landscape as Oklahoma. But the Tenth Circuit’s decision is still a helpful guidepost for electric cooperatives and their customers who find themselves stuck between “a rock and a pile of sewage” — or facing the loss of water, or gas, or phone, or any other municipal service in which the city is the dominant supplier.

When a city chooses to act in a monopolistic or some other competitively unfair fashion, a cooperative should make sure that the city is doing so only with express legislative permission.

The Newkirk decision is similar in many respects to a decision from the United States District Court for the Northern District of Georgia nearly a quarter of a century ago. Schwartz Partnership v. City of Cartersville, No. C86-359R (N.D. Ga. July 2, 1987).

In that case, the city of Cartersville required the purchase of its electricity as a precondition to the sale of land to industrial customers. In so doing, Cartersville represented that its rates were lower than those of Georgia Power, the other available electric supplier.

When the industrial customers later discovered that the city’s rates were not lower than Georgia Power’s available rate, they questioned any obligation to purchase electricity from Cartersville. In response, Cartersville refused to provide gas, water and sewer facilities to the customer, despite a prior arrangement to do so, and refused to convey an option property.

In a 141-page opinion, the district court concluded, in relevant part, that Cartersville had engaged in an illegal tying arrangement under both the Sherman Act and state law prohibitions. The district court further noted that the tie-in had “no pro-competitive effects or redeeming social value.” (Click here for the opinion.)

Kay Electric Cooperative v. City of Newkirk, No. 10-6214 (10th Circuit, opinion filed July 29, 2011); City of Newkirk v. Kay Electric Cooperative, No. 11618 (U.S. Supreme Court, certiorari denied Jan. 17, 2012)

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