IN THE COURT OF APPEALS OF TENNESSEE
AT NASHVILLE
September 7, 2016 Session

CANEY FORK ELECTRIC COOPERATIVE., INC., ET AL. v. TENNESSEE STATE BOARD OF EQUALIZATION

Appeal from the Tennessee State Board of Equalization
No. 1571 Executive Secretary, Kelsie Jones

No. M2016-00316-COA-R12-CV – Filed September 23, 2016

The Tennessee Attorney General opined that a tax exemption in favor of electric cooperatives found at Tenn. Code Ann. § 65-25-122(a) violates Article II, Section 28 of the Tennessee Constitution. The Board of Equalization began proceedings to recalculate the taxes of the electric cooperatives. Several electric cooperatives objected and maintained that the exemption under Tenn. Code Ann. § 65-25-122(a) was valid. The Board recalculated their taxes anyway. The electric cooperatives appealed. Although the Board of Equalization cannot rule on the constitutionality of the statute, we can. We find that Tenn. Code Ann. § 65-25-122(a) violates Article II, Section 28 of the Tennessee Constitution.

Tenn. R. App. P. 3 Appeal as of Right; Judgment of the Tennessee State Board of Equalization Affirmed

ANDY D. BENNETT, J., delivered the opinion of the court, in which D. MICHAEL SWINEY, and W. NEAL MCBRAYER, JJ., joined.

J. Richard Lodge, Jr. and Robert C. Guth, Nashville, Tennessee, for the appellants, Caney Fork Electric Cooperative Inc., Pickwick Electric Cooperative, Powell Valley Electric Cooperative, Upper Cumberland Electric Membership Corporation, and Volunteer Energy Cooperative.

Herbert H. Slatery, III, Attorney General and Reporter; Andrée Sophia Blumstein, Solicitor General; and Mary Ellen Knack, Senior Counsel; for appellee, Tennessee State Board of Equalization.

Leslie Clark Ledbetter, Clarkrange, Tennessee, for appellee, Fentress County, Tennessee.

Robert T. Lee, Mt. Juliet, Tennessee, for the appellees, McNairy County and Smith County.

OPINION

This case presents several unusual situations. The appellants are five rural electric cooperatives that dispute the State Board of Equalization's calculation of their annual ad valorem taxes for 2015. Tennessee Code Annotated section 65-25-122(a) provided[1] that an electric cooperative's newly-constructed plants and facilities were exempt from taxation for a period of four years. In October 2015, the Tennessee Attorney General issued an opinion stating that the tax exemption was "unconstitutional because it purports to grant a tax exemption that is not authorized by Article II, Section 28, of the Tennessee Constitution." Op. Tenn. Att'y Gen. No. 15-71, 2015 WL 6520689, at *1 (Oct. 21, 2015).

In November 2015, the Office of State Assessed Properties (OSAP) notified the Board of Equalization ("the Board") that the rural electric cooperatives had not been adequately assessed for the 2015 tax year because the assessments included exemptions under Tenn. Code Ann. § 65-25-122(a), which the Attorney General had stated was unconstitutional. The Board then recertified the assessments and issued a final decision memorializing its rulings. The electric cooperatives appealed from this decision.

Initially, we note the curious situation presented here—that the Tennessee Attorney General is, in the course of representing his client, arguing that a statutory provision passed by the Tennessee General Assembly is unconstitutional. Tennessee law assigns to the Attorney General the duty to defend the constitutionality of legislation of statewide applicability, "except in those instances where the attorney general and reporter is of the opinion that such legislation is not constitutional, in which event the attorney general and reporter shall so certify to the speaker of each house of the general assembly[.]" Tenn. Code Ann. § 8-6-109(b)(9). The speakers, in turn, "acting jointly, may employ legal counsel to defend the constitutionality of such law." Tenn. Code Ann. § 8-6-109(c). The representative of the Attorney General's office appearing at oral argument told this Court that the certification to the speakers had been made. Because no counsel for the speakers made an appearance, we may infer that no one was employed by them. Rather, the legislature repealed the law, and the Attorney General continued to represent the Board. No one has challenged the Attorney General's authority to participate and, indeed, the other appellees, McNairy County, Smith County and Fentress County, deferred to the Attorney General's Office to present the appellees' oral argument. So, we will consider the issue waived.

[1] The four-year tax exemption contained in Tenn. Code Ann. § 65-25-122(a) was repealed effective April 27, 2016. 2016 TENN. PUB. ACTS, ch. 937.

A second unusual aspect of this case is the conclusion by an administrative agency that this statute is unconstitutional. The appellants maintain that the Board has no authority to determine whether the statute in question is constitutional because this action involves a facial challenge.

> Administrative tribunals do not lack the authority to decide every constitutional issue. It is essential, however, to distinguish between the various types of constitutional issues that may arise in the administrative context. In *Richardson*,[2] we developed three broad categories of constitutional disputes: (1) challenging the facial constitutionality of a statute authorizing an agency to act or rule, (2) challenging the agency's application of a statute or rule as unconstitutional, or (3) challenging the constitutionality of the procedure used by an agency. *Id*. at 454-55. Administrative tribunals have the power to decide constitutional issues falling into the second and third categories, but the first category falls exclusively within the ambit of the judicial branch. *Id*. The separation of powers clause reserves for the judiciary constitutional challenges to the facial validity of a statute. *Id*.

Colonial Pipeline Co. v. Morgan, 263 S.W.3d 827, 843 (Tenn. 2008).

"A facial challenge to a statute involves a claim that the statute fails an applicable constitutional test and should be found invalid in all applications." *Waters v. Farr*, 291, S.W.3d 873, 921 (Tenn. 2009). The record shows that the issue of the constitutionality of Tenn. Code Ann. § 65-25-122(a) was presented to the Board in the course of determining the recertification of the assessments against various electric cooperatives. A representative of the Comptroller's Office presented the Attorney General's opinion, and a representative of the electric cooperatives and a representative of McNairy and Smith counties spoke. No evidence was presented. The challenge to Tenn. Code Ann. § 65-25-122(a) is a challenge to the statute on its face—that is, an assertion that "no set of circumstances exists under which the statute, as written, would be valid." *Id.* at 882. The challengers to the statute maintain that it does not fit within the charitable exception of Article II, Section 28 of the Tennessee Constitution.

The Board has been placed in a difficult situation. Because this issue is a facial challenge to the constitutionality of Tenn. Code Ann. § 65-25-122(a), the Board does not have the authority to address it. Yet, as a matter of public policy and common sense, shouldn't state officials follow the advice of their attorney?[3] While the situation may be

[2] *Richardson v. Tenn. Bd. of Dentistry*, 913 S.W.2d 446 (Tenn. 1995).

[3] Indeed, it has long been the position of the Attorney General that state officials should follow his advice. In his opinions, the Attorney General has stated:

delicate, the answer is clear. The Supreme Court has said that "[t]he separation of powers clause reserves for the judiciary constitutional challenges to the facial validity of a statute." *Colonial Pipeline Co.*, 263 S.W.3d at 843 (citing *Richardson*, 913 S.W.2d at 455). The Board cannot rule on the constitutionality of this statute.[4] It can, and should, acknowledge the issue and take whatever evidence is appropriate from the parties to build a record for the reviewing courts to use when the issue goes up on appeal. In this case, the Board heard legal arguments as to the constitutionality of Tenn. Code Ann. § 65-25-122(a).

We finally arrive at the heart of this case: whether the exemption found in Tenn. Code Ann. § 65-25-122(a) violates Article II, Section 28 of the Tennessee Constitution. The relevant portion of Article II, Section 28 states: "In accordance with the following provisions, all property real, personal or mixed shall be subject to taxation, but the Legislature may except . . . such as may be held and used for purposes purely religious, charitable, scientific, literary or educational . . . ." We are to "interpret constitutional provisions in a principled way that attributes plain and ordinary meaning to their words, and that takes into account the history, structure, and underlying values of the entire document." *Estate of Bell v. Shelby Cnty. Health Care Corp.*, 318 S.W.3d 823, 835 (Tenn. 2010) (citations omitted). The primary

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> This Office has stated on a number of occasions that if a board or agency is called upon to implement a statute which this Office, as its statutory legal advisor, has opined as unconstitutional, the board or official is advised not to enforce the statute. Op. Tenn. Atty. Gen. No. 83-418 (Dec. 16, 1983); Op. Tenn. Atty. Gen. No. 88-41 (Feb. 25, 1988). This latter opinion is based upon the following language in the case of *Cummings v. Beeler*, 189 Tenn. 151, 159–60 (1949):
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> > State officials are presumed to do their duty and we feel sure and have no hesitancy in saying that they will and do their duty as they see it. Would it not be the duty of the Comptroller to refuse to approve these when he knows that his official legal advisor has held that the Act under which these warrants were to be issued was illegal, invalid, and unconstitutional?
>
> It may be inferred from the above quotation from the *Cummings* case that when a public official is aware of an Attorney General's opinion concerning an aspect of his official responsibilities, he or she is under a duty to conform his conduct with the view of the state's legal advisor. This duty arises not from any binding effect of an opinion, but rather from recognition that a public official, in performing his official duties, should conform his or her conduct with the advice provided by the state's attorney. In other words, the duty to follow the Attorney General's advice arises from the attorney-client relationship rather than from any legal or binding effect of an opinion.

Op. Tenn. Att'y Gen. No. 89-20, 1989 WL 434659, *3-4 (Feb. 13, 1989).

[4] It was suggested at oral argument that the Board never said the statute was unconstitutional; it just followed the advice of the Attorney General. In doing so, the Board acted as though the exemption at issue did not exist and, therefore, implicitly found the exemption unconstitutional.

guide for the courts is the words of the text. *Id*.

The language of Article II, Section 28 is permissive. "Article II, Section 28 is not self-executing, nor does it establish public policy regarding exemptions from taxation." *Metro. Gov't of Nashville & Davidson Cnty. v. Tenn. State Bd. of Equalization*, 817 S.W.2d 953, 954 (Tenn. 1991). The language is also limiting. The legislature is not permitted to enact exemptions for areas not specified in the constitution. However, the constitution does not define the term "charitable."[5] *Club Sys. of Tenn., Inc. v. YMCA of Middle Tenn.*, No. M2004-01966-COA-R3-CV, 2005 WL 3479628, at *7 (Tenn. Ct. App. Dec. 19, 2005). The Tennessee Supreme Court has defined the term "charity" as follows:

> Probably the most comprehensive and carefully drawn definition of a charity that has ever been formulated is that it is a gift, to be applied consistently with existing laws, for the benefit of an indefinite number of persons, either by bringing their hearts under the influence of education or religion, by relieving their bodies from disease, suffering or constraint, by assisting them to establish themselves for life, or by erecting or maintaining public buildings or works or otherwise lessening the burdens of government.

Id. at *7-8 (quoting *Baptist Hosp. v. City of Nashville*, 3 S.W.2d 1059, 1060 (Tenn.1928)). Thus, a charitable purpose under Article II, Section 28 involves an element of gifting.

All statutes are presumed to be constitutional. *CitiMortage, Inc. v. Drake*, 410 S.W.3d 797, 803 (Tenn. Ct. App. 2013). The lack of a constitutional definition "necessarily allows the Legislature some discretion in determining the meaning of the term." *Club Sys.*, 2005 WL 3479628, at *7. While the authority to determine the meaning of the constitution rests with the judiciary, "courts must give careful consideration to the interpretation placed upon the constitution by the legislature." *Metro. Gov't of Nashville & Davidson Cnty.*, 817 S.W.2d at 955 (citing *LaFever v. Ware*, 365 S.W.2d 44, 47 (Tenn. 1963)). Statutes providing property tax exemptions are construed liberally in favor of the institution. *Book Agents of the Methodist Episcopal Church v. State Bd. of Equalization*, 513 S.W.2d 514, 521 (Tenn. 1974).

In 1939, the Tennessee legislature first created the statutes allowing electric cooperatives. 1939 TENN. PUB. ACTS, ch. 176, § 2. In 1945, in what was, until April 26, 2016, Tenn. Code Ann. § 65-25-122(a), the legislature created a tax exemption for electric cooperatives that stated: "all facilities and plants constructed for such primary purpose shall be exempt from ad valorem property taxes for a period of four (4) years from and after the date of such construction." 1945 TENN. PUB. ACTS, ch. 157, § 1.

[5] All parties seem to agree that only the charitable exemption might apply to the electric cooperatives.

To receive the exemption, an organization must be a charitable institution and use the property exclusively for its charitable purposes. Tenn. Code Ann. § 67-5-212(a)(1).[6] The term "charitable institution" has been defined by the Legislature to include "any nonprofit organization or association devoting its efforts and property, or any portion thereof, exclusively to the improvement of human rights and/or conditions in the community." Tenn. Code Ann. § 67-5-212(c).

Electric cooperatives were originally conceived as "cooperative, non-profit, membership corporations . . . organized . . . for the purpose of supplying electric energy and promoting and extending the use thereof." 1939 TENN. PUB. ACTS, ch. 176, § 2. Today's statutes identify them as "ideal business organizations in providing adequate and reliable electric services at reasonable rates throughout the rural communities of Tennessee." Tenn. Code Ann. § 65-25-101(b)(1). As such, the legislature in 1988 revised the laws governing electric cooperatives to allow them to engage in the provision of other utility services. Tenn. Code Ann. § 65-25-104(a)(2). They are charged with furnishing services "at the lowest cost consistent with sound business principles." Tenn. Code Ann. § 65-25-103.

Electric cooperatives are membership based.[7] *See* Tenn. Code Ann. § 65-25-102(4). Each member is entitled to vote for the directors and upon other matters. Tenn. Code Ann. §§ 65-25-102(6), 106(a). Members and nonmember patrons must agree to pay for the electric cooperative's services and abide by its terms and conditions of service. Tenn. Code Ann. § 65-25-111(a)(1). Electric cooperatives are organized for the mutual benefit of their members, not the general public.

There is no element of charity associated with electric cooperatives. Members and nonmember patrons pay for the services they receive. The rates they pay are based on sound business practices. While no doubt exists that the conditions of the communities where these cooperatives were established improved because of access to electricity, there is no charitable purpose or activity involved. Therefore, we must conclude that Tenn. Code Ann. § 65-25-122(a) is incompatible with the charitable exemption framework established in Tenn. Code Ann. § 67-5-212(a)(1) and violates Article II, Section 28 of the Tennessee Constitution.[8]

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[6] Statutes relating to the same subject should be considered together. *Faust v. Metro. Gov't of Nashville & Davidson Cnty*, 206 S.W.3d 475, 490 (Tenn. Ct. App. 2006). Thus, we construe Tenn. Code Ann. § 65-25-122(a), which creates the exemption, with Tenn. Code Ann. § 67-5-212, which creates the framework for charitable exemptions.

[7] Electric cooperatives can have customers who are not members. They are called "nonmember patrons." Tenn. Code Ann. § 65-25-102(8).

[8] We also note that the language of the exemption itself would seem to indicate it is not a

Costs of appeal are assessed against the appellants, for which execution may issue if necessary.

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ANDY D. BENNETT, JUDGE

charitable exemption because of the limitation of the exemption to four years. If the property is being used for charitable purposes, that use would not predictably end after four years. Rather, the exemption appears to be a mechanism to recoup expenses of construction.