CURRENT WATER UTILITY CCN DECERTIFICATION ISSUES AT THE PUBLIC UTILITY COMMISSION OF TEXAS

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By Leonard H. Dougal and Mallory Beck[1]

I. INTRODUCTION

The responsibility for the regulation of water and sewer service, including the oversight of certificates of public convenience and necessity ("CCNs"), was recently transferred from the Texas Commission on Environmental Quality ("TCEQ") to the Public Utility Commission ("PUC"), effective September 1, 2014. Senate Bill 567 ("SB 567") and House Bill 1600 ("HB 1600") transferred "the powers, duties, functions, programs, and activities . . . relating to the economic regulation of water and sewer service, including the issuance and transfer of certificates of convenience and necessity, the determination of rates, and the administration of hearings and proceedings involving those matters, under Section 12.013 and Chapter 13, Water Code . . ." from the TCEQ to the PUC.[2] Among those duties, the PUC is now responsible for the streamlined expedited release process by which certain landowners may petition to have their property removed from the existing retail service provider's CCN. This paper discusses the transition to the PUC, the basics of decertification, expedited release, and some of the issues that have arisen since the PUC began implementing the expedited release process.

II. TRANSITION FROM THE TCEQ TO THE PUC

As of September 1, 2014, the PUC has assumed responsibility for oversight and enforcement of the statutory scheme applicable to CCNs. In transferring the duties of the TCEQ related to CCNs to the PUC, the Legislature specifically provided that "A rule, form, policy, procedure, or decision of the [TCEQ] related to a power, duty, function, program, or activity transferred under this Act continues in effect as a rule, form, policy, procedure, or decision of the [PUC] and remains in effect until amended or replaced by that agency."[3] Initially, the PUC adopted the substantive rules regulating water and sewer utilities from the TCEQ (30 Texas Administrative Code, Chapter 291) with the only changes being those necessary to implement the rules in accordance with PUC procedures and correct typographical errors.[4] The PUC has adopted revisions to those rules.[5] However, no changes have been made to the rule governing expedited releases (as of September 1, 2015).

III. BACKGROUND ON DECERTIFICATION OF CCNs

A CCN is a permit issued by the PUC that authorizes and obligates a retail public utility to furnish, make available, render, or extend continuous and adequate retail water or sewer utility service to a specified geographic area.[6] While all retail public utilities can attempt to secure CCNs, "utilities" (which generally include private for-profit entities) and water supply corporations are required to obtain a CCN from the PUC before rendering retail water or sewer utility service directly or indirectly to the public.[7] Agency review ensures that the applicant for a CCN has the financial, managerial, and technical qualifications to

[1] This paper is an update to a CLE paper titled "*SB 573, CCN Decertification, and Water Utility Service Issues*" authored by Leonard Dougal, Cassandra Quinn, Ty Embrey, and Stefanie Albright, which was presented at the State Bar of Texas, Changing Face of Water Rights 2012 CLE program. We greatly appreciate the assistance of Cassandra Quinn, Ty Embrey, and Stefanie Albright in preparation of that paper and for allowing us to update it. The views and opinions stated in this paper are solely those of the authors and do not necessarily represent the views or opinions of Jackson Walker L.L.P. or any of its clients.

[2] Tex. S.B. 567, 83d Leg., R.S. (2013); Tex. H.B. 1600, 83d Leg., R.S. (2013).

[3] Acts May 14, 2013, 83d Leg., R.S., ch. 170, § 2.96(j) Tex. Gen. Laws 770 (2013); *see also* 16 Tex. Admin. Code ("TAC") § 24.1.

[4] 39 Tex. Reg. 2667 (2014); 39 Tex. Reg. 5903 (2014).

[5] 16 TAC § 24.1, et seq.; *see also* PUC Order Adopting Amendments, Item No. 43, PUC Docket No. 43871 (August 24, 2015).

[6] 30 TAC § 291.3(10); 16 TAC § 24.3(10).

[7] TEX. WATER CODE § 13.242(a). By rule, the PUC may allow operations without a CCN for service to less than 15 connections, not located in another's CCN. TEX. WATER CODE § 13.242(c).

provide continuous and adequate service to the subject territory and customers.

Typically, a retail public utility with a CCN is the sole water or sewer service provider in the territory covered by the CCN. Having a single service provider to provide service on a regional basis is designed to ensure that utility services are supplied efficiently, such as by avoiding fragmented utility systems and producing economies of scale by spreading fixed costs over a larger number of customers. By this method, CCNs allow utilities to plan for growth on a long-term basis by being able to identify their service area.

In general, no other retail public utility may extend water or sewer utility service into the certificated territory of another retail public utility without first seeking to obtain the CCN rights for the area from the PUC.[8] As a result, entities that are not required to obtain CCNs, such as municipalities, may choose to do so in order to protect their service areas from encroachment by other retail public utilities.

However, acquiring a CCN does not protect the CCN holder from later decertification of all or part of the territory covered by the CCN. The PUC may make findings relevant to decertification on its own motion and revoke or amend an existing CCN.[9]

If a CCN is revoked or amended, the PUC may require one or more retail public utilities with their consent to provide service to the area in question.[10] The retail public utility taking over the service area must provide compensation to the decertified retail public utility for any property that the PUC determines is rendered useless or valueless due to the decertification.[11] While the revocation process is still available, the Texas Legislature has created alternatives that are designed to accomplish decertification more quickly and easily.

IV. SECTION 1926(B) FEDERAL DEBT PROTECTION.

When discussing CCNs and decertification, reference is often made to 7 U.S.C. § 1926(b). Non-profit water utilities may obtain loans from the United States Department of Agriculture Rural Development Division ("USDA") pursuant to 7 U.S.C. § 1926(b) to construct water infrastructure. When acquiring these loans, utilities must pledge as collateral their systems and infrastructure, including the right to provide service within the defined CCN service area.

Under Section 1926(b), a federally indebted utility's service territory may be protected by federal law. Section 1926(b) states that

> "The service provided or made available [by a federally indebted rural water] association shall not be curtailed or limited by inclusion of the area . . . within the boundaries of any municipal corporation or other public body, or by the granting of any private franchise for similar service within such area during the term of such loan."[12]

Section 1926(b) is often discussed in the context of decertification, as debate exists as to the exact nature of the protection a federally indebted water association has regarding its defined service area.

In *North Alamo Water Supply Corp. v. City of San Juan*,[13] the United States Court of Appeals for the Fifth Circuit addressed the requirement of service being "made available." The *North Alamo* court noted that the purpose of § 1926(b) was to prohibit the encroachment of local governments upon the services provided by rural water associations.[14] The court found two congressional goals behind § 1926(b): "(1) to encourage rural water development by expanding the number of potential users of such systems, thereby decreasing the per-user cost, and (2) to safeguard the viability and financial security of such associations (and [the federal government's] loans) by protecting them from the expansion of nearby cities and towns."[15] The *North Alamo* court then explained the requirement of Texas law that a water utility in possession of a CCN must provide continuous and adequate service to all customers within its service area.[16] The court concluded that "when state law obligates a utility to provide water service, that utility has, for the purposes of § 1926(b), 'made service available.'"[17]

In contrast, several other federal circuit courts apply the "pipes in the ground" test requiring a water

[8] *Id.*

[9] *Id.* § 13.254(a).

[10] *Id.* § 13.254(c).

[11] *Id.* § 13.254(d).

[12] 7 U.S.C. § 1926(b).

[13] 90 F.3d 910 (5th Cir. 1996).

[14] *Id.* at 915.

[15] *Id.*

[16] *Id.* at 915-16 (citing Tex. Water Code § 13.250(a)).

[17] *Id.* at 916 (quoting *Glenpool Util. Auth. v. Creek County Rural Water Dist. No. 2.*, 861 F.2d 1211, 1214 (10th Cir. 1988)).

utility to have "adequate facilities within or adjacent to the area to provide service to the area within a reasonable time after a request for service is made."[18] At least one Texas appellate court has concluded that the "pipes in the ground" test is the appropriate test.[19]

V. CCN DECERTIFICATION BY EXPEDITED RELEASE

In 2005, the Texas Legislature established the original "expedited release" process through House Bill 2876 ("HB 2876"), which provided a new method for certain landowners to petition to have their property removed from the CCN of the existing retail water or sewer provider.[20] Expedited release was adopted to remedy certain perceived abuses in the CCN process. However, some interests believed these legislative changes did not go far enough, and during the 2011 legislative session, further changes were made with the passage of SB 573. These changes included amending the existing expedited release process, as well as creating a new streamlined expedited release process that applies to property located in certain counties. A discussion of both the original and new processes follows.

A. Statutory Expedited Release.

The original CCN decertification process is set forth in Section 13.254(a) of the Water Code. Section 13.254(a) provides that the PUC may revoke or amend a CCN with the written consent of the CCN holder if it finds that:

(1) the CCN holder has never provided, is no longer providing, is incapable of providing, or has failed to provide service to all or part of the area covered by the CCN;

(2) in certain counties with economically distressed areas the cost of providing service is so "prohibitively expensive" so as to constitute a denial of service;

(3) the CCN holder has agreed in writing to allow another retail public utility provider to provide service within its service area, except for an interim period, without a CCN amendment; or

(4) the CCN holder has not filed a cease and desist action under Section 13.252 within 180 days of the date the CCN holder discovered that another utility was provided service in its service area, unless good cause is shown by such failure.[21]

This original standard is distinguished from the expedited release processes described below as its offers bases for decertification based on another retail public utility *already* providing service to the CCN service area, or, the incapability of the CCN holder to provide service without respect to another utility's ability to do so.

An alternative to this standard CCN decertification process was later added in Section 13.254(a-1) of the Water Code in 2005 by HB 2876. Section 13.254(a-1) authorizes a landowner with at least 50 acres that is not in a platted subdivision and not currently receiving water or sewer service to petition the PUC for expedited release of the land from the incumbent retail public utility's CCN area so that the land may receive service from another retail public utility.[22]

To use this provision, the landowner must first make a request for service to the incumbent utility, which then has 90 days in which to respond. The landowner may file a petition for expedited release if the incumbent utility:

(1) refuses to provide service;

(2) is not capable of providing adequate service within the timeframe, at the level, or in the manner reasonably requested by the landowner; or

(3) conditions the provision of service on a payment of costs not properly allocable directly to the petitioner's service request.[23]

Further, the petitioner must demonstrate that an alternate retail public utility is available to provide service.

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[18] *Sequoyah County Rural Water Dist. No. 7 v. Town of Muldrow*, 191 F.3d 1192, 1202 (10th Cir. 1999); *see also Rural Water System No. 1 v. City of Sioux Center*, 202 F.3d 1035 (8th Cir. 2000); *Lexington-South Elkhorn Water Dist. v. City of Wilmore, Ky.*, 93 F.3d 230, 237 (6th Cir. 1996).

[19] *Creedmoor-Maha Water Supply Corp. v. Tex. Comm'n on Envtl. Quality*, 307 S.W.3d 505 (Tex.App.—Austin 2010, no pet.).

[20] Tex. H.B. 2876, 79th Leg., R.S. (2005).

[21] TEX. WATER CODE § 13.254(a).

[22] TEX. WATER CODE § 13.254(a-1); 16 TAC § 24.113(b). For guidance pertaining to expedited release as interpreted by TCEQ before the transition to PUC, see *Preparing a Petition for Expedited Release from a Certificate of Convenience and Necessity* (Oct. 2006) (Tex. Comm'n on Envt'l Quality), available at http://www.tceq.state.tx.us/files/rg-441.pdf_4006495.pdf.

[23] *See* Tex. Water Code § 13.254(a-1).

The alternate provider must be capable of providing continuous and adequate service within the timeframe, at the level, and in the manner reasonably needed or requested by current and projected service demands in the area. In addition, the PUC must also consider the approximate cost for the alternative service provider to provide service at a comparable level to the existing CCN holder. The PUC is also required to consider the financial, managerial and technical capability of the alternate service provider.

SB 573 also added Section 13.254(a-8), which provides that if a certificate holder has never made service available to the area a petitioner seeks to have released under Subsection (a-1), then the PUC is not required to find that the proposed alternative provider is capable of providing better service than the certificate holder, only that the alternative provider is capable of providing service. However, Subsection (a-8) does not apply to the following areas:

(i) a county bordering Mexico or the Gulf of Mexico,

(ii) a county adjacent to either such county, or

(iii) a county

(1) with population of more than 30,000 and less than 35,000 bordering the Red River;

(2) with a population of more than 100,000 and less than 200,000 that borders a county described in (1);

(3) with a population of 130,000 or more that is adjacent to a county with population of 1.5 million or more, located within 200 miles of an international border; or

(4) with a population of more than 40,000 but less than 50,000 that contains a portion of the San Antonio River.[24]

This list of counties translates to Cameron, Fannin, Grayson, Guadalupe, Hidalgo, Willacy, and Wilson.[25]

After a petition for expedited release under Section 13.254(a-1) is deemed administratively complete, the PUC must grant the petition within 60 days unless it finds that the petitioner has failed to satisfy the elements required by statute. Expedited release petitions originally had to be acted upon within 90 days, but SB 573 shortened the timeframe to 60 days.

The evaluation of the petition and response by the CCN holder is conducted by PUC staff as an informal agency action without any opportunity for a contested case hearing.[26] If a petition is granted, the process then moves to valuation and compensation, if any, to the incumbent utility. A party aggrieved by the decision of the PUC on an expedited release petition (whether the landowner or the incumbent utility) only has a right to seek reconsideration of the action within the agency but may not appeal the decision to district court.[27]

B. Streamlined Expedited Release Under SB 573.

In addition to amending the existing expedited release process, SB 573 also created a new process, referred to as "streamlined expedited release."

SB 573 was filed in February 2011 during the 82nd Regular Legislative Session and was considered at public hearings in both the Senate and House Natural Resources Committees. A total of six amendments were added to the bill on the House floor, and the bill was finally adopted by both chambers in the form of a conference committee report. SB 573 was signed by the Governor on June 17, 2011, and became effective on September 1, 2011.

Section 13.254(a-5) of the Water Code creates a new procedure for CCN decertification that allows landowners with at least 25 acres who are not receiving water or wastewater service, and who are located in one of 33 counties referenced in Section 13.254(a-5) to petition the PUC to remove their property from an existing CCN. This streamlined expedited release process applies to petitions filed under this statutory provision on or after September 1, 2011.

As originally proposed, the streamlined expedited release process would have been available statewide. However, during consideration in the Senate Committee on Natural Resources, the applicability of the bill was bracketed to apply only in certain counties. Specifically, the new process applies only if the landowner's property is located in 1) a county with a population of at least 1 million; 2) in a county adjacent to such a county; or 3) in a county with more than 200,000 and less than 220,000 that does not contain a public or private university with an enrollment of

[24] *Id.* § 13.254(a-9)–(a-10).

[25] 30 TAC 291.113(u); 16 TAC 24.113(u). It appears that the intent of the sponsors of the amendments to exclude these counties was that these counties be excluded from all the changes to the existing expedited release process under Subsection (a-1); however, only Subsection (a-8) was bracketed accordingly.

[26] TEX. WATER CODE § 13.254(a-3).

[27] *See id.* § 13.254(a-4); *see also Creedmoor-Maha Water Supply Corp. v. Tex. Comm'n on Envt'l Quality*, 307 S.W.3d 505 (Tex. App.—Austin 2010, no. pet.).

40,000 or more (i.e. Smith County). The property may not be located in a county with population of more than 45,500 and less than 47,500 (i.e. Medina County). This language translates to the SB 573 expedited release process being available to landowners in the following 33 counties: Atascosa, Bandera, Bastrop, Bexar, Blanco, Brazoria, Burnet, Caldwell, Chambers, Collin, Comal, Dallas, Denton, Ellis, Fort Bend, Galveston, Guadalupe, Harris, Hays, Johnson, Kaufman, Kendall, Liberty, Montgomery, Parker, Rockwall, Smith, Tarrant, Travis, Waller, Williamson, Wilson, and Wise.[28]

The streamlined expedited release process under Section 13.254(a-5) varies in several ways from the Section 13.254(a-1) expedited release process. In the streamlined process, the petitioner is not required under Section 13.254(a-5) to first submit a written request for service to the existing CCN holder. In addition, there is no requirement that the petitioner demonstrate that an alternative service provider is available and capable of providing service to the property. In other words, with respect to water or wastewater service, the landowner must show only that no service is being provided by the CCN holder at the time the petition for streamlined expedited release is submitted. Further, the statute specifically prohibits the PUC from denying a petition based on the fact that a CCN holder is a borrower under a federal loan program, a provision clearly aimed at 7 U.S.C. § 1926(b) arguments. As long as all of the applicability requirements are met, the PUC is required to grant a petition for streamlined expedited release within 60 days.

After land is removed from the CCN of the incumbent utility using the streamlined expedited release process, the incumbent utility may not be required to provide service to the removed land for any reason, including the violation of law or PUC rules by a water or sewer system of another person.[29]

C. Petitions Using the SB 573 Streamlined Expedited Release Process.

On April 12, 2013, the TCEQ adopted rules pertaining to the streamlined expedited release process.[30] Those rules were contained in Chapter 291 of the TCEQ's rules which were adopted by the PUC into Chapter 24 of the PUC's rules. Largely, the PUC's rules track the language of the statute. However, the rules specifically require a petitioner to provide a copy of the petition to the CCN holder and permit the CCN holder to submit a response to the PUC.[31] The only other change from the statutory language is to specify that compensation is governed by the same rules governing compensation under 13.254(a-1).

As of April 21, 2015, there had been 119 applications seeking streamlined expedited release filed with the TCEQ and subsequently the PUC. Of those applications 68 were approved, 15 were dismissed, 6 were returned, 9 were withdrawn, and 23 remained pending.

The form of these petitions varies greatly. Some are simply in the form of a letter explaining how each of the elements necessary to qualify for decertification have been met and containing documentation to verify the acreage and ownership of the affected property. Others are in a more traditional petition format enclosing documents to verify acreage and property ownership, along with an affidavit from a knowledgeable official confirming the acreage and ownership of the affected property and averring that the property has not received water or wastewater service. Some even contain the more onerous elements required for petitions under Section 13.254(a-1), even though PUC's rules do not specifically require petitions under Section 13.254(a-5) to include the same information.[32]

For expedited release petitions under Section 13.254(a-1), PUC requires specific mapping information showing the location of the property which is the subject of the expedited release petition. Arguably one of the biggest obstacles for petitioners seeking expedited release is the mapping requirements. Few petitions have managed to meet the mapping requirements and obtain administrative complete rulings in their first try. Because PUC does not consider the 60-day clock to begin until after the petition is found to be administratively complete, the practice has been for PUC Staff to recommend a finding that the petition is not administratively complete and set a deadline for the petitioner to correct the deficiencies. The PUC has requested that the petition include a property description of the area to be certified consistent with the property descriptions required for an original CCN application, such requirements which are found in 16 Tex. Admin. Code

[28] 16 TAC § 24.113(r).

[29] *Id.* § 13.254(h).

[30] 38 Tex. Reg. 2365 (Apr. 12, 2013).

[31] 16 TAC § 24.113(s).

[32] *Compare* 16 TAC 24.113(b) *with* 16 TAC 24.113(r)-(s).

§24.105(a)(2)(A)-(G). Section 24.105(a)(2) requires a map and description of only the proposed service area by:

> (A) metes and bounds survey certified by a licensed state land surveyor or a registered professional land surveyor;
> (B) the Texas State Plane Coordinate System or any standard map projection and corresponding metadata;
> (C) verifiable landmarks, including a road, creek, or railroad line; or
> (D) a copy of the recorded plat of the area, if it exists, with lot and block number.[33]

Some of the petitions for streamlined expedited release under Section 13.254(a-5) filed so far have been dismissed or returned because they failed to meet the minimum acreage requirement. Others have been granted over the strenuous objections of the CCN holder.

The streamlined expedited release process is only available to "the owner of a tract of land that is at least 25 acres."[34] In practice, the TCEQ had interpreted this language to require that the 25 acres be contiguous. In one case, the Pflugerville Community Development Corporation ("PCDC") owned approximately 167 contiguous acres of land, with 140 acres located in the City of Pflugerville's CCN and 27.419 acres located in the Manville Water Supply Corporation's CCN. PCDC sought expedited release of the land located in Manville's CCN; however, the land in the Manville CCN consisted of three non-contiguous areas, each of which was less than 25 acres. The TCEQ dismissed PCDC's petition because each of the areas requested for decertification was less than 25 acres, even though they were part of a contiguous tract of land owned by the same landowner that was greater than 25 acres.

Since the PUC began implementing water and sewer CCNs, the issue of what constitutes a "tract of land" has arisen on multiple occasions. In a recent case, the PUC held that to meet the 25-acre requirement, the area within the CCN for which decertification is sought need not be greater than 25 acres, so long as that area is part of a tract of land that is at least 25 acres.[35] In another case, the PUC clarified that multiple deeded parcels of land could be aggregated into a single "tract" to meet the 25-acre requirement, as long as the acres were all contiguous and not separated by roads or other property.[36]

D. Austin Court of Appeals explains "Receiving Water or Sewer Service" under Section 13.254(a-5).

In the first appellate court decision regarding streamlined expedited release under Section 13.254(a-5), the Austin Court of Appeals examined the meaning of "receiving water or sewer service."[37] There, the General Land Office ("GLO") sought streamlined expedited release for five contiguous tracts, each over 25 acres, which did not contain any active meters, lines, or other facilities serving those tracts. The GLO did not seek decertification of approximately 151 acres from five additional contiguous tracts which did have certain facilities.[38] The CCN holder argued that (1) the GLO could not choose to decertify only a portion of its contiguous property; and (2) that the property was in fact "receiving water service."[39] The TCEQ disagreed and granted the GLO's petition.

The Austin Court of Appeals upheld the decision of TCEQ finding that there was no "all or nothing" requirement in Section 13.254(a-5) prohibiting the GLO from selecting only a portion of its property for the decertification request.[40]

In deciding whether a tract is "receiving water service," the Court stated that the term "service," as defined in the Texas Water Code, is broad and includes "facilities and lines as well as acts performed and anything furnished or supplied."[41] Yet, the Court stated that "service" was limited by the requirement that facilities or lines be "committed or used" in the performance of the CCN holder's duties and that "acts performed and things furnished or supplied must also

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[33] 16 TAC § 24.105(a)(2)(A)-(D).

[34] Tex. Water Code § 13.254(a-5).

[35] *Petition of Tyler Blue Ridge LLC to Amend Tall Timbers Utility Company, Inc.'s Certificate of Convenience and Necessity in Smith County by Expedited Release*, PUC Docket No. 44507, Item No. 21 (May 18, 2015).

[36] *Petition of SLF Assemblage IV – 114, L.P. to Amend Aqua Texas, Inc.'s Water Certificate of Convenience and Necessity in Denton County by Expedited Release*, PUC Docket No. 44667, Item No. 26 (September 11, 2015).

[37] *Tex. Gen. Land Office v. Crystal Clear Water Supply Corp.*, No. 03-13-00528-CV, 2014 Tex. App. LEXIS 9342 (Aug. 22, 2014).

[38] *Id.* at *3-4.

[39] *Id.* at *2.

[40] *Id.* at *12-14. Notably, the Court pointed out that the 151 acres was subsequently removed from the CCN holder's area by statute rendering the "gerrymandering" argument moot even if remanded.

[41] *Id.* at *23.

be in furtherance of performing those duties."[42] Ultimately, the Court held that the determination of whether a tract is receiving water service is "a fact-based inquiry requiring the Commission to consider whether the retail public utility has facilities or lines committed to providing water *to the particular tract* or has performed acts or supplied anything *to the particular tract* in furtherance of its obligation to provide water to that tract pursuant to its CCN."[43] In this particular case, the Court held that substantial evidence supported TCEQ's decision.[44] The CCN holder has appealed the decision to the Texas Supreme Court which has requested briefing on the merits.

E. Aqua WSC Lawsuits Challenging Decertification.

One of the most discussed streamlined expedited release petitions was also the first petition to be approved. The petition was filed by the Austin Community College District Public Facility Corporation ("ACC"), which requested the expedited release of 98 acres from the CCN held by the Aqua Water Supply Corporation ("Aqua WSC"). This petition involved both federal and state lawsuits.

The state court lawsuit, filed in the 201st District Court in Travis County, Texas, appealed the TCEQ's order.[45] In February of 2013, the TCEQ consented to an order entered by the state court vacating the decertification order, as part of a settlement agreement among the parties.[46]

In the federal suit, the TCEQ's order granting decertification was challenged by Aqua WSC based not only on the state statutory argument that service is being provided to the ACC property, but also based on the federal protections afforded to water associations with outstanding USDA debt under 7 U.S.C. § 1926(b).

Under Section 13.254(a-6) of the Water Code, once the landowner files the petition for decertification under Section 13.254(a-5), the TCEQ must grant the petition within 60 days. This subsection specifically states TCEQ may not deny a petition based on the fact that a certificate holder is a borrower under a federal loan program.[47]

The application of Section 13.254(a-6) was challenged by Aqua WSC as violating the federal Supremacy Clause.[48] In its Original Petition, Aqua WSC requested that the TCEQ Order for decertification be nullified because Aqua maintained debt under 7 U.S.C. § 1926(b) and had made service available to ACC, thus triggering federal protection of Aqua WSC's service area.[49] Aqua WSC argued that because water associations pledge as collateral on USDA debt the right to provide service to the association's existing service area, Section 1926(b) affords water associations with outstanding USDA debt the exclusive right to provide water in its service area, so long as service is made available, and that this protection of its service area under federal law pre-empts any application of 13.254(a-5).[50] Thus, Aqua WSC asserted that decertification of any portion of a water association's service area under 13.254(a-5), when such service area is federally protected on the basis of outstanding USDA debt, is an unconstitutional violation of the Supremacy Clause (U.S. Constitution, Art VI, cl. 2).[51] After years of litigation, Aqua WSC settled its claims against the ACC and, after the state court vacated the decertification order, the district court granted TCEQ's motion to dismiss finding Aqua WSC's preemption claims were moot.[52] Then, after TCEQ approved modifications between CCN acreage of Aqua WSC and the City of Elgin, those parties' claims were settled and dismissed and final judgment was entered.[53]

[42] *Id.* at *23-24.

[43] *Id.* at *23.

[44] *Id.* at *29.

[45] *Aqua Water Supply Corp. v. Tex. Comm'n on Envtl. Quality*, No. D-1-GN-11-003617, in the 201st Judicial District Court of Travis County Texas, filed Nov. 23, 2011.

[46] Order, *Aqua Water Supply Corp. v. Tex. Comm'n on Envtl. Quality*, No. D-1-GN-11-003617, in the 201st Judicial District Court of Travis County Texas (Feb. 15, 2013).

[47] TEX. WATER CODE § 13.254(a-6). However, TCEQ may require the petitioner to compensate the subject decertified retail public utility under (a-5) or as otherwise provided in this section. *Id.*

[48] Aqua Water Supply Corp. Original Petition, *Aqua Water Supply Corp. v. Tex. Comm'n on Envtl. Quality*, No. A-11-CV-885-LY (Nov. 23, 2011) (hereinafter referred to as the "Petition")

[49] Petition at 13-14.

[50] *Id.*

[51] *Id.* at 4, 14.

[52] *See* Report and Recommendation of the United States Magistrate Judge, *Aqua Water Supply Corp. v. Tex. Comm'n on Envtl. Quality*, No. A-11-CV-885-LY (February 7, 2014).

[53] *Id.* at 2.

F. Compensation to the Incumbent Utility.

Once an area is decertified through either expedited release process, the new retail public utility may not begin providing service in that area without first providing compensation to the incumbent utility for any property the PUC determines is rendered useless or valueless.[54] The value of real property owned and utilized by the retail public utility for its facilities is determined using the standards governing actions in eminent domain, while the value of personal property is determined by analyzing certain factors listed in the statute.[55] These factors include:

(1) the amount of debt allocable to the lost service area;
(2) the value of service facilities in the area;
the amount expended by the affected retail utility on planning, design and construction preparatory to service to the area;
(3) the amount of any contractual obligations, such as take-or-pay contracts, allocable to the area;
(4) any impairment of services or increase in cost to remaining customers;
(5) the loss of future revenues from existing customers that are transferred to the acquiring retail utility;
(6) legal and other professional fees incurred by the affected retail utility; and
(7) other relevant factors.

If the two retail public utilities agree on an independent appraiser, then the compensation amount determined by that appraiser is binding on the PUC. If they cannot agree, each must engage its own appraiser at its own expense, and each appraisal must be submitted to the PUC.

After receiving the appraisals, the PUC appoints a third appraiser to make a determination of the compensation, which may not be less than the lower appraisal or more than the higher appraisal.

Not surprisingly, CCN holders and landowners often disagree on the value of compensation to be paid following decertification. The CCN holder typically views the value to be quite dear, and the landowner views the value to be nearly worthless. Unless settled by agreement, the appraisal process will become a battle of the experts, with the differences in value quite vast.

In the first expedited release case where valuation was determined by the TCEQ, involving CCN holder BHP Water Supply Corporation, the TCEQ commissioners approved an amount close to the third appraiser's recommendation.[56] This expedited release was granted under 13.254(a-1). There the landowner's appraiser valued the CCN holder's loss at $0 because there were no facilities or customers in the area decertified, whereas the CCN holder valued the loss at approximately $300,000. Despite the lack of facilities in the area, the third appraiser valued the area at $63,848, concluding that there were debt obligations, expenditures for planning, design, and construction, and legal and professional fees allocated to the area. For the debt obligations and expenditures for planning, the third appraiser considered the percentage the decertified area represented of the entire CCN area and used that to calculate the value of the debt obligations and expenditures of the entire system for that area. Based on the Executive Director's recommendation, the TCEQ commissioners adjusted this amount downward to $57,348, subtracting the amount the CCN holder paid for its initial appraisal.

In another 13.254(a-1) expedited release case, involving CCN holder Creedmoor-Maha Water Supply Corporation, TCEQ determined the value of the utility property rendered valueless or useless to be exactly the amount the third appraiser recommended.[57] The landowner's appraiser valued the CCN holder's loss at $16,547.73. The CCN holder's appraiser valued the loss at $2,157,072. The third appraiser valued the loss at $179,392 and that is the amount the TCEQ found to represent the value of the property rendered useless or valueless due to the decertification. The third appraiser found that the CCN holder had invested substantially in system-wide facilities which would provide water service to the decertified area and that the CCN holder would lose future revenues from existing customers which were lost due to the decertification.

In a more recent compensation decision where area was decertified under 13.254(a-5), involving CCN

[54] TEX. WATER CODE § 13.254(d).

[55] *Id.* § 13.254(g).

[56] *Petition from Kerala Christian Adult Homes 1, L.P. for an Expedited Release from Water Certificate of Convenience and Necessity No. 10064 of BHP Water Supply Corporation (WSC) in Collin County*; Application No. 35724-C (TCEQ Order Granting Release Issued September 17, 2007)

[57] *Petition from Jona Acquisition, Inc. for an Expedited Release from Water Certificate of Convenience and Necessity (CCN) No. 11029 of Creedmoor-Maha Water Supply Corporation*, TCEQ Docket No. 2010-0100-UCR (TCEQ Order Determining Compensation Issued Apr. 26, 2010).

holder Monarch Utilities I, L.P., TCEQ also agreed with the third appraiser's valuation.[58] The landowner's appraiser concluded that the CCN holder suffered a loss of $25,223. The CCN holder's appraisal found the loss to be $3,748,489. The parties reached such vastly different valuations due to differences in evaluating several crucial factors. The CCN holder found that because the decertified area would not provide additional customers to share in the CCN holder's debt payments via payment of rates, existing customers would be required to pay more resulting a valuation of this factor of over $200,000. The landowner and third appraiser disagreed and valued this factor at $0. The CCN holder valued the amount of expenditures for planning, design, or construction of service facilities allocable to the decertified area at over $500,000 because all regional facilities were purportedly constructed with the intent to provide reliable service to the general area, including the decertified area. The landowner and third appraiser disagreed because none of those facilities were dedicated solely to the decertified area and the CCN holder did not have the water supply or infrastructure currently built to serve the decertified area. They valued this factor at approximately $16,000. Regarding the impairment of service or increase of costs to customers, the CCN holder pointed out that a water line, necessary to loop its system, would also serve the decertified area, but that, without that area, the entire costs of that line would be borne by existing customers. The landowner argued this factor should be valued at $0. The third appraiser found that, but for the decertification, developers within the decertified area would contribute to the costs of the line and thus valued the loss at approximately $221,000. Ultimately, the third appraiser concluded the loss was $275,512 and the TCEQ agreed.

Finally, in a fairly unique case, where the CCN holder (Southland Regional Service Corp.) was a defunct corporation with no assets or facilities, the TCEQ did not require the City of Austin to pay anything for the property and facilities after granting a Section 13.254(a-1) expedited release petition.[59]

Compensation to the incumbent utility, it seems, turns on the existence of physical assets dedicated to serving the decertified area more so than mere planning for future assets or existing assets that could contribute in some way to the service of the decertified area. Based on the limited cases to date, the compensation for property rendered useless or valueless appears to largely turn on the value of hard assets clearly dedicated to serve the subject land, such as water system facilities, that are adversely impacted by the decertification. However, it is too early to tell whether the compensation factors will be evaluated differently by the PUC.

VI. CONCLUSION

The PUC is now responsible for administering the statutes addressing water and sewer CCNs, including the streamlined expedited release process. That process allows a landowner with 25 acres or more to remove land from a provider's water or sewer CCN with relative ease, but the process only applies to land in 33 specific counties in Texas. As case law and petition precedent evolves, landowners and CCN holders need to consider how decertification, or the threat of decertification, will impact retail water planning and supplies to local areas within Texas.

[58] *Petition from E.B. Windy Hill, L.P. for an Expedited Release from Water Certificate of Convenience and Necessity No. 12983 of Monarch Utilities I, L.P.*, TCEQ Docket No. 2013-1871-UCR (TCEQ Order Determining Compensation Issued Nov. 22, 2013).

[59] *Petition from Jona Acquisition, Inc. for an Expedited Release from Water Certificate of Convenience and Necessity (CCN) No. 20663 of Southland Regional Service Corp.*, in Travis County, Texas; Application No. 36303-D (TCEQ Order Granting Expedited Release Issued June 15, 2009).