# SB 573, CCN DECERTIFICATION, AND WATER UTILITY SERVICE ISSUES

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**CHAPTER 3**

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## I. INTRODUCTION

In the most recent session of the Texas Legislature, additional mechanisms were added to the Texas Water Code for landowners to utilize in determining which retail water or sewer service provider will serve their properties. Senate Bill 573 ("SB 573") streamlined and modified the applicability of the existing "expedited release" process, which authorizes certain landowners to petition the Texas Commission on Environmental Quality (TCEQ) to have their property removed from the existing retail service provider's certificate of convenience and necessity (CCN), which is the service area for the provider as designated by the TCEQ.[2] This paper discusses the basics of decertification, the reach of SB 573 and the first petitions processed under the new legislation, as well as some of the remaining issues in implementing the new expedited release process.

## II. BACKGROUND ON DECERTIFICATION OF CCNs

A CCN is a permit issued by the TCEQ 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.[3] While all retail public utilities can attempt to secure CCNs, "utilities" (which generally include private entities) and water supply corporations are required to obtain a CCN from the TCEQ before rendering retail water or sewer utility service directly or indirectly to the public.[4] The TCEQ's review ensures that the applicant for a CCN has the financial, managerial, and technical qualifications to provide continuous and adequate service.

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 is designed to provide service on a regional basis and 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 TCEQ.[5] 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 TCEQ may make findings relevant to decertification on its own motion and revoke or amend an existing CCN.[6]

If a CCN is revoked or amended, the TCEQ may require one or more retail public utilities with their consent to provide service to the area in question.[7] The retail public utility taking over the service area must provide compensation to the decertified retail public utility for any property that the TCEQ determines is rendered useless or valueless due to the decertification.[8] While the revocation process is still available, the Texas Legislature has created alternatives that are designed to accomplish decertification more quickly and easily.

## III. 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

[1] 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 LLP, Lloyd Gosselink Rochelle & Townsend, P.C., or any of their clients.

[2] Tex. S.B. 573, 82nd Leg., R.S. (2011).

[3] 30 Tex. Admin. Code (TAC) § 291.3(10).

[4] TEX. WATER CODE § 13.242(a).

[5] *Id.*

[6] *Id.* § 13.254(a).

[7] *Id.* § 13.254(c).

[8] *Id.* § 13.254(d).

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."[9]

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.

## IV. 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 the TCEQ to have their property removed from the CCN of the existing retail water or sewer provider.[10] 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 TCEQ may, on its own motion or receipt of a petition described by Section 13.254(a-1), 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.[11]

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 TCEQ 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.[12]

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.[13]

[9] 7 U.S.C. § 1926(b).

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

[11] TEX. WATER CODE § 13.254(a).

[12] TEX. WATER CODE § 13.254(a-1); 30 Tex. Admin. Code § 291.113(b). For regulatory guidance pertaining to expedited release, 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.

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

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

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, with the passage of SB 573, the TCEQ must also consider the approximate cost for the alternative service provider to provide service at a comparable level to the existing CCN holder. The TCEQ is now 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 TCEQ 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.[14]

This bracketed list of counties translates to Cameron, Willacy, Hidalgo, Fannin, Grayson, Wichita, Guadalupe, and Wilson Counties.[15]

After a petition for expedited release under Section 13.254(a-1) is deemed administratively complete, the TCEQ 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 TCEQ staff as an informal agency action without any opportunity for a contested case hearing.[16] 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 TCEQ 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.[17]

### 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 by the TCEQ 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.

The new 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 TCEQ 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

[14] *Id.* § 13.254(a-9)–(a-10).

[15] 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.

[16] TEX. WATER CODE § 13.254(a-3).

[17] *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.).

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 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.

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. As long as all of the applicability requirements are met, the TCEQ 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 many not be required to provide service to the removed land for any reason, including the violation of law or TCEQ rules by a water or sewer system of another person.[18]

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

The TCEQ has not yet conducted rulemaking to implement the changes made by SB 573, so there is currently no official guidance on how to petition for streamlined expedited release. Nevertheless, there have already been 24 petitions filed seeking streamlined expedited release under SB 573, of which 11 have been approved, 5 have been dismissed, 1 has been returned (for failing to demonstrate property ownership), 1 has been withdrawn, and 6 are still pending (current as of January 9, 2012).

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, 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.

The TCEQ has also requested specific mapping information showing the location of the property which is the subject of the expedited release petition. Specifically, the TCEQ 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 30 Tex. Admin. Code §291.105(a)(2)(A-G). Specifically, Section 291.105(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.[19]

Thus, although petitions for expedited release under Section 13.254(a-5) are relatively simple, the TCEQ does expect detailed information regarding the mapping of the specific property requested to be decertified.

Some of the petitions filed so far have been dismissed or returned because they failed to meet the minimum acreage requirement. The streamlined expedited release process is only available to "the owner of a tract of land that is at least 25 acres."[20] In practice, the TCEQ has 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

[18] *Id.* § 13.254(h).

[19] *See* 30 Tex. Admin. Code § 291.105(a)(2)(A-G).

[20] Tex. Water Code § 13.254(a-5).

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.

### D. Aqua WSC Lawsuits Challenging Decertification.

The most discussed streamlined expedited release petition 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 is currently the subject of both federal and state lawsuits. The federal suit is currently pending in the U.S. District Court for the Western District of Texas, and the state suit is currently pending in the Travis County District Court.

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.[21]

The application of Section 13.254(a-6) was challenged by Aqua WSC as violating the federal Supremacy Clause.[22] 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.[23] 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).[24] Thus, Aqua WSC asserts 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).[25]

### E. 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 TCEQ determines is rendered useless or valueless.[26] 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.[27] 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.

[21] 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.*

[22] Aqua Water Supply Corp. Original Petition, *Aqua Water Supply Corp. v. Tex. Comm'n on Envtl. Quality, et. al* (Nov. 23, 2011) (hereinafter referred to as the "Petition")

[23] Petition at 13-14.

[24] *Id.*

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

[26] TEX. WATER CODE § 13.254(d).

[27] *Id.* § 13.254(g).

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

After receiving the appraisals, the TCEQ 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.

## V. TCEQ RULEMAKING

The TCEQ intends to conduct rulemaking in the fall of 2012 regarding the implementation of the directives of SB 573. Such implementation will give stakeholders, including developers, landowners, and utilities, the opportunity to address certain unresolved issues that remain in the application of Section 13.254(a-5). Under the current milestones project document prepared by TCEQ staff, it is anticipated that proposed rules will be presented to the TCEQ Commission at its August 22, 2012 Agenda, after which there will be the opportunity for public comment and a public hearing on these draft rules. The proposed milestone for approval of final rules regarding Section 13.254(a-5) is January 23, 2013, and a proposed effective date of February 14, 2013.

One of the most debated issues that will likely be addressed by the upcoming rulemaking is what constitutes the definition of "service" as it relates to the application of expedited release statutes. Utilities, developers and landowners have proposed a wide range of standards for defining service. For example, it has been proposed by some that various degrees of infrastructure constructed up to or near the property at issue could constitute "service," where other entities have asserted that only the actual receipt of water or wastewater service meets the definition of "service."

## VI. CONCLUSION

The statutory changes made by SB 573 attempt to streamline the process by which a landowner may remove land from a provider's water or wastewater CCN. It is still early to anticipate the full impact of SB 573; however, further insight into SB 573's effect is likely to be obtained after resolution of the pending state and federal lawsuits by Aqua WSC and completion of the TCEQ rulemaking to implement the legislation.