

BILL ANALYSIS

C.S.H.B. 2400
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Natural Resources
Committee Report (Substituted)

BACKGROUND AND PURPOSE

Utilities are among the most capital intensive industries, with water utilities more capital intensive than natural gas, electric, and telephone utilities. Water and wastewater utilities face a significant financial challenge to replace aging infrastructure and upgrade treatment as required by increasingly stringent requirements. Currently, Chapter 13 of the Texas Water Code establishes a rate setting method for public utilities based on a concept known as a “historical test year”. A historical test year consists of actual expenses over a recent 12 month period and includes adjustments for “known and measurable changes” such as power, chemical, and salary expense changes to establish the public utility’s reasonable cost of service. Rates are set to be charged during the first year following an historical test year.

Nationwide, the water and wastewater industry face a combined capital investment requirement near one trillion dollars over the next 20 years, according to the EPA. The Environmental Protection Agency estimates that water systems serving under approximately 1,000 connections generally lack the economy of scale to sustain themselves. Single-tariff pricing is a means to provide the economy of scale to allow small water systems to operate in compliance with federal, state, and local requirements by offering a unified rates structure for multiple water utility systems that are owned and operated by a single utility. These systems may or may not be contiguous or physically interconnected.

Current law authorizes the Texas Commission on Environmental Quality (TCEQ) to approve rate changes for investor owned water and sewer utilities. Investor owned water and sewer utilities provide notice to their customers of a rate change and put their proposed rates into effect 60 days after the notice was provided and the customers have another 90 days after the effective date to protest the rate change. If protests are received from the lesser of 10% or 1000 affected customers the case is referred to the State Office of Administrative Hearings. Since the proposed rates are being charged, interim rates are often an issue in these contested rate cases.

C.S.H.B. 2400 authorizes the TCEQ to base a utility’s expenses on information for either a historic test year of the most recent 12-month period or future test year of the 12-month period ending on the first anniversary of the filing date of the rate application.

C.S.H.B. 2400 authorizes a utility to consolidate more than one system under a single tariff on a regional basis. The bill removes the requirement that only substantially similar systems in terms of facilities, quality of service, and cost of services are allowed to consolidate these fees.

C.S.H.B. 2400 amends current law to require a water or sewer investor owned utility to provide notice to ratepayer at least 90 days before the proposed effective date of the proposed change. If sufficient protests are received to refer the case to SOAH the rates are suspended until a final rate is set by the Commission. This approach will alleviate the need for the TCEQ to have to consider interim rates in these cases. If the rate change is uncontested the investor owned utility can put the proposed rates into effect after the comment period ends.

C.S.H.B. 2400 prevents a utility from enacting its desired rate until a final decision of the Commission is rendered. The State Office of Administrative Hearings (SOAH) is required to issue a proposal for decision not later than the 120th day after the last date of the preliminary hearing. The Commission then has 60 days to issue its final decision. The executive director with Commission approval may extend the time period if deemed necessary to protect a party’s due process or other constitutional right.

C.S.H.B. 2400 creates a system infrastructure improvement charge which allows drinking water and wastewater utilities to replace infrastructure to improve reliability, to comply with environmental requirements, and to create solutions to regional water supply problems in a timely, cost-effective manner. Such a surcharge was adopted in Pennsylvania in 1996 and has since been implemented in at least seven other states.

Additionally, the bill grants the executive director authority to issue administrative orders in uncontested cases to transfer CCNs and to convert or dissolve a water district. These uncontested cases currently have to go before the Commission so this will save the applicant time because of notice requirements the ED will be able to approve the request sooner. Finally, the bill will allow a similar exemption for small sewer systems that is already provided to small water utility systems. Small water utility systems with less than 15 connections can register as an exempt utility and does not have to obtain a CCN unless it is in another utility's service area.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the Texas Commission on Environmental Quality in SECTIONS 5 and 6 of this bill.

ANALYSIS

SECTION 1. Amends Section 13.002(22), Water Code as follows:

- (22) Defines the term "test year" to mean the annualized period for which costs are to be analyzed and rates established.

SECTION 2. Amends Section 13.145(a), Water Code as follows:

- (a) Provides that a utility may to consolidate more than one system under a single tariff on a regional basis. Strikes the requirement that systems under the same tariff must be substantially similar in terms of facilities, quality of service, and cost of service.

SECTION 3. Amends Section 13.185(d), Water Code as follows:

- (d) Requires a regulatory authority to base a utility's expenses on information for either, at the utility's choice, a historic test year that is the most recent 12-month period that ended less than 12 months before the filing date of the rate application or the future test year of the 12-month period ending on the first anniversary of the filing date of the rate application for which representative and supporting information for the utility is available.

SECTION 4. Amends Sections 13.187 (a), (b), (d), (e), (f), (k), (o), and (p), Water Code as follows:

- (a) Prohibits a water and sewer utility from making changes in its rates except by delivering a statement of intent to each ratepayer and the regulatory authority having original jurisdiction at least 90 days, rather than 60 days, before the proposed effective date of the proposed changes. Revises the contents required to be included in the statement of intent by requiring the statement to include the following, in addition to certain billing comparisons: the utility's name, address, current rates, and proposed rates; the effective date of the proposed rates; information on the procedure for protesting a rate change, the minimum number of protests needed to ensure a hearing, and the length of the protest period; contact information for the Texas Commission on Environmental Quality (TCEQ) and the office of public interest counsel; and a brief description of the contested case hearing process. Requires the statement to include a billing comparison of the existing water or sewer rate and a new water or sewer rate based on specified increments of usage, unless the utility proposes a flat rate for sewer service. The bill, for that billing comparison, requires a comparison regarding the existing water or sewer rate and the new water or sewer rate computed for the use of 5,000, 10,000, 15,000, and 30,000 gallons of water or sewer, rather than only 10,000 and

30,000 gallons of water. Makes related conforming changes.

- (b) Adds the executive director of TCEQ to the entities to whom a copy of the statement of intent is required to be mailed or delivered.
- (d) Stipulates the conditions by which an application or statement of intent may be rejected and the conditions by which a proposed effective date of the rate change may be suspended.
- (e) Requires the regulatory authority to hold the proposed rate increase hearing before the 61st day after the date the statement of intent was provided to the authority and each ratepayer as stipulated.
- (f) Authorizes the regulatory authority to set the matter for hearing anytime within 90 days after the statement of intent was provided as described under Subsection (a).
- (k) Stipulates that should a regulatory authority set a matter for hearing as described under Subsection (e), the effective date of the rate change is required to be left pending until a final decision is issued. Requires the administrative law judge to issue a proposal for decision no later than the 120th day after the preliminary hearing's last date. Requires issuance of the commission's final decision not later than the 60th day after the administrative law judge issues the proposal for decision. Should the commission deem it necessary, the process can be extended by the executive director in an effort to protect a party's right to due process or other constitutional right.
- (o) If the regulatory authority does not set a hearing on the proposed rate increase as stipulated, the rates are automatically approved as requested
- (p) Adds language stating, except as provided, a utility or two or more utilities under common ownership may not file a statement of intent to increase its rates for the same customer more than once a year.

SECTION 5. Amends Subchapter F, Chapter 13, Water Code by adding Section 13.193.

- (a) Authorizes a water and sewer utility to assess a utility facilities construction and improvement charge to recover the depreciation and return on investment of a utility facilities construction and improvement project that is completed and placed into service between two consecutive statements of intent to change the utility's rates or tariff and serves the utility's certificated service area, including a facility used for the production, transmission, storage, distribution, or provision of potable or recycled water to the public or the collection, transportation, treatment, or disposal of sewage.
- (b) Requires the commission by rule to require a utility that proposes to assess a utility facilities construction and improvement charge to file a tariff establishing a just and reasonable manner for calculating the charge and to receive the executive director's approval of the tariff.
- (c) Not later than the 60th day before a utility's proposed inclusion of such a charge or a proposed increase of such a charge in a tariff, the utility must submit to the executive director for review of a project's eligibility a written notice that contains the amount of the proposed charge or increase of a charge; the proposed implementation date for the charge or increase of a charge; a list of completed, eligible capital projects, and related depreciation and return on investment for which the utility seeks reimbursement through the charge or increase of a charge; and a calculation of the projected total annual increase in revenue due to the charge or increase of a charge. Provides that the total amount the utility is authorized to recover annually through a utility facilities construction and improvement charge and the amount the utility actually recovers are subject to annual audit by the executive director. Provides that the amount of the charge the utility requests authorization to assess is based on the amount necessary to ensure that the charge

yields a rate of return on invested capital that is equal to the rate of return approved by the utility in the utility's most recent approved base rate or tariff change application or the rate of return proposed by the utility, if the rates in the utility's most recent base rate or tariff change application were approved by settlement. Provides that the cumulative annual amount the utility proposes to recover from the charge does not exceed an amount equal to 10 percent of the utility's annual revenue. Provides that the utility does not implement an increase under these provisions relating to a utility facilities construction and improvement charge more often than twice every calendar year. Provides that the charge is applied to each customer included in the tariff. Provides that the utility provides to each customer written notice of the charge on the initial tariff filing that proposes to implement the charge. Provides that the charge is subject to a true-up or reconciliation at the utility's next rate case.

- (d) Establishes that the implementation of a utility facilities construction and improvement charge or an increase in such a charge is not subject to a contested case hearing under the Administrative Procedure Act.
- (e) Prohibits a utility from collecting the charge after the first anniversary of the completion of a utility facilities construction and improvement project.
- (f) Provides that these provisions relating to a utility facilities construction and improvement charge inapplicable to a utility that has in place a negotiated stay-out agreement on September 1, 2011.

SECTION 6. Amends Section 13.242(c), Water Code as follows:

- (c) Authorizes the commission by rule to allow a municipality or utility or water supply corporation to render sewer service, in addition to retail water service, without a certificate of public convenience and necessity if the municipality has given applicable notice that it intends to provide such service to an area or if the utility or water supply corporation has less than 15 potential connections and is not within the certificated area of another retail public utility.

SECTION 7. Amends Section 13.248, Water Code as follows:

Sec. 13.248 Establishes that contracts between retail public utilities designating areas to be served and customers to be served by those retail public utilities are valid and enforceable and are incorporated into the appropriate areas of public convenience and necessity when approved by the executive director, as an alternative to the commission, after public notice. Removes a requirement that such validation, enforcement, and incorporation be after a public hearing.

SECTION 8. Amends Section 49.321, Water Code as follows:

Sec 49.321 Authorizes the executive director, in addition to the commission, and after notice, to dissolve any water district that is inactive for a period of five consecutive years and has no outstanding bonded indebtedness.

SECTION 9. Amends Section 49.324, Water Code as follows:

Sec. 49.324. Authorizes the commission or executive director to enter an order dissolving a district if it finds that the district has performed none of the functions for which it was created for a period of five consecutive years and that the district has no outstanding bonded indebtedness.

SECTION 10. Amends Section 49.326(a), Water Code as follows.

- (a) Appeals from an order dissolving a district shall be filed and heard in district court as stipulated.

SECTION 11. Amends Section 54.030(b), Water Code, as follows:

- (b) Provides for a governing body of a district the ability to convert into a municipal utility district operating under this chapter and Article XVI, Section 59, Texas Constitution by entering into the minutes a resolution that in its judgment the conversion would be in the best interest of the district and benefit to the land and property included. Requires the resolution to request that the commission approve the conversion of the district.

SECTION 12. Amends Section 54.032, Water Code as follows:

- (a) Strikes reference hearing, to read that notice of a conversion shall be given by publishing notice as stipulated.
- (b) Strikes language to make the section read the notice shall be published once a week for two consecutive weeks.
- (c) Specifies the notice is required to set out the adopted resolution in full and notify all interested persons how they may offer comments for or against the proposal contained in the resolution.

SECTION 13. Section 54.033, Water Code is amended as follows:

- (a) Adds the executive director as an alternative to the commission, for the purposes of provisions requiring an order to be entered relating to the conversion of a municipal utility district if the commission or the executive director find that such conversion would serve the best interest of the district and would be a benefit to the land and property included in the district.
- (b) If the commission or the executive director determine the conversion of the district is not in the best interest of the district, either the commission or the executive director is required to order against the conversion.
- (c) The commission or the executive director's findings shall be subject to appeal or review as stipulated
- (d) Requires a copy of the order converting the district to be filed as stipulated.

SECTION 14. The following sections of the Water Code are repealed:

- (1) Sections 13.187 (d-1), (i), (j), (l), (m) and (n); and
- (2) Sections 49.322 and 54.031.

SECTION 15. Prospective clause.

This Act applies only to a statement of intent filed on or after the effective date of this Act. Statements filed prior are governed by the law in effect on that date and continued in effect for that purpose.

SECTION 16. Provides for the effective date of this Act.

EFFECTIVE DATE

This Act takes effect September 1, 2011.

COMPARISON OF ORIGINAL TO SUBSTITUTE

C.S.H.B. 2400 contains a provision redefining "test year," whereas the original bill had no such provision.

C.S.H.B. 2400 contains a provision authorizing a water and sewer utility to consolidate more than one system under a single tariff on a regional or statewide basis, if the tariff provides for

rates that promote water conservation for single-family residences and landscape irrigation, and removing certain conditions required to be satisfied before such a utility is authorized to consolidate more than one system under a single tariff, whereas the original bill had no such provision.

C.S.H.B. 2400 contains a provision requiring a regulatory authority to base a utility's expenses on information for either, at the utility's choice, a specified historic or a specified future test year, whereas the original bill had no such provision.

C.S.H.B. 2400 contains a provision, not included in the original, revising the information required to be included in a utility's rate change statement of intent. Requires a statement of intent at least 90 days before the proposed effective date of the change, rather than 120 days. Strikes a provision in the original bill regarding billing comparison regarding the existing sewer rate and the new sewer rate computed for the use of 10,000 gallons as stipulated.

C.S.H.B. 2400 changes the date the regulatory authority is required to hold a hearing on the proposed rate increase to the 61st day after the statement of intent was provided to the authority as set out, whereas the original bill stated the regulatory authority had 91 days.

C.S.H.B. 2400 states the regulatory authority may set the matter for hearing 90 days after the date the statement of intent was provided to the authority as stipulated, whereas the original bill allowed for 120 days.

C.S.H.B. 2400 adds language stating the administrative law judge is required to issue a proposal for decision not later than the 120th day after the date of the preliminary hearing. The commission is required to issue a final decision not later than the 60th day after the date the administrative law judge issues the proposal for decision. The substitute provides a means by which an extension for the process may be issued. Clarifies that a utility or two or more utilities under common control and ownership may not file a statement of intent to increase its rates for the same customer more than once in a 12-month period. The original bill had no such provisions.

C.S.H.B. 2400 contains provisions authorizing a water and sewer utility to assess a utility facilities construction and improvement charge to recover the depreciation and return on investment of certain utility facilities construction and improvement projects, requiring the commission by rule to make certain requirements of a utility proposing to assess such a charge, detailing elements such rules are required to ensure, establishing that the implementation of such a charge or an increase in the charge is not subject to a contested case hearing under the Administrative Procedure Act, prohibiting a utility from collecting the charge after the first anniversary of the completion of a utility facilities construction and improvement project, and making the bill's provisions relating to the charge inapplicable to a utility that has in place a negotiated stay-out agreement on September 1, 2011. The original bill had no such provisions.