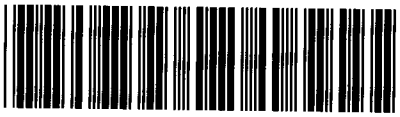

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SOAH DOCKET NO. 473-15-1149.WS
PUC DOCKET NO. 43674

PETITION OF THE CITY OF DALLAS FOR REVIEW OF A DECISION BY THE SABINE RIVER AUTHORITY TO SET WATER RATES (LAKE FORK RESERVOIR)	§ § § § §	BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS

SABINE RIVER AUTHORITY'S APPEAL OF SOAH ORDER NO. 4

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SOAH DOCKET NO. 473-15-1149.WS
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PETITION OF THE CITY OF DALLAS FOR REVIEW OF A DECISION BY THE SABINE RIVER AUTHORITY TO SET WATER RATES (LAKE FORK RESERVOIR)	§ § § § §	BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS

SABINE RIVER AUTHORITY'S APPEAL OF SOAH ORDER NO. 4

TO THE HONORABLE PUBLIC UTILITY COMMISSION:

COMES NOW, the Sabine River Authority ("Authority" or "SRA") and files this appeal of State Office of Administrative Hearings ("SOAH") Order No. 4 in Docket No. 43674, *Petition of the City of Dallas for Review of a Decision by the Sabine River Authority to Set Water Rates (Lake Fork Reservoir)* ("Petition"). SOAH Order No. 4 was filed on January 12, 2015. Pursuant to P.U.C. PROC. R. 22.123(a)(2), this appeal is timely filed. In support of its Appeal, the Authority would respectfully show the following:

I. EXECUTIVE SUMMARY

- The only relationship between the SRA and the City of Dallas ("City" or "Dallas") is contractual; the contract is the only source of Dallas' claim to Lake Fork water, and the only source of the SRA's right to charge Dallas a rate for that water.

- By taking *any* action other than abatement of the proceeding under P.U.C. SUBST. R. 24.131(d), the Administrative Law Judge ("ALJ") is wading into a contract matter and construing the contract.

- Most troubling is the ALJ's finding that the contract does not specify how the rate would be set. This finding amounts to a determination that the contract does not contain a provision for consideration to be paid by Dallas to the SRA. Under Texas contract law, if a contract is missing an essential term (such as consideration), then the contract fails in its entirety as a matter of law.

- Thus, Order No. 4 impermissibly places in doubt the entire relationship between Dallas and the SRA. This potential ramification stands as strong warning against the ALJ or the Public Utility Commission ("PUC" or "Commission") wading into the waters of contract interpretation.

- Therefore, the SRA requests that Order No. 4 be reversed in its entirety, and further requests that this proceeding be abated until the underlying contract dispute is resolved.

II. INTRODUCTION

The Administrative Law Judge has erroneously undertaken to render an unauthorized opinion on a contractual dispute between the parties. Order No. 4's finding that "there currently is no contractual rate," and therefore interim rates are appropriate and no public interest hearing is necessary, is based solely upon an interpretation of the written contract between the parties and a finding that the contractual terms have not been complied with.[1] Order No. 4 equates to a judicial determination of a contractual dispute between the parties, and is beyond the authority of the ALJ to perform.

Although Order No. 4 purports to recognize the lack of jurisdiction of SOAH and the Commission to determine and adjudicate the parties' obligations under a written contract,[2] Order No. 4 does exactly that. As such, the ALJ's decision is also beyond the jurisdiction of the Commission.

It must be noted specifically that Order No. 4's conclusion that "there is no current contractual rate,"[3] is quite troubling, because it casts into doubt the very *existence* of a contract, and ultimately of any contractual right of the City of Dallas to purchase water from Lake Fork Reservoir and any contractual obligation of the Authority to sell such water to the City. In the absence of a valid contract, all such rights and obligations disappear. By opining that the contract neither specifies a rate for a new term, nor sets out a specific methodology for determining the rate, the conclusion to be drawn from Order No. 4 is that the contract lacks an

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1 Order No. 4 at 2 and 6 (Jan. 12, 2015).

2 *Id.* at 4.

3 *Id*

essential term, *i.e.*, consideration. Under basic Texas contract law, such a finding would render the contract unenforceable and void.

The improper exercise of jurisdiction over a contractual dispute results in two findings that prejudice a substantial and material right of the Authority and materially affect the course of the hearing: (1) a finding that the Commission has the authority to establish interim rates in a wholesale rate case without first making a finding under the public interest standard of P.U.C. SUBST. R. 24.133, and (2) a finding that a public interest hearing is not required before the Commission can overturn mutually-agreed contractual provisions and rewrite a contract at the behest of one of the parties. Thus, this appeal is appropriate under P.U.C. PROC. R. 22.123(a).

If Order No. 4 is allowed to stand, then the Commission will have done exactly what the ALJ asserts it cannot do – determine and adjudicate the parties' obligations under the contract. Therefore, the Commission should void Order No. 4 in its entirety, and abate this matter pending resolution of the contract dispute between the parties.

III. BACKGROUND

Pursuant to its creation statute, Vernon's Article 8230-133, the Authority, governed by appointees of the Governor of the State of Texas, has jurisdiction over the watershed of the Sabine River in Texas, including Lake Fork Creek, a tributary of the Sabine River.[4] In the early 1970's, the Authority determined to construct a dam and reservoir on Lake Fork Creek in Wood, Rains, and Hopkins Counties, Texas.

In 1974, the Authority entered into an agreement with Dallas Power & Light Company, Texas Electric Service Company, and Texas Power & Light Company (the "Corporations"), by which the reservoir known as Lake Fork Creek Reservoir and the water supply facilities located

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[4] The Authority was created in 1949 by Act of the 51st Legislature, Tex. H.B. 467, 51st Leg., R.S. (1949), Chapter 110.

thereon would be constructed. These facilities were defined in the 1974 agreement as "[t]he water supply facilities consisting of the lands, easements, rights of way, dam, reservoir, and related facilities to be acquired, constructed, and owned by the Authority on Lake Fork Creek."[5] The 1974 agreement between the Corporations and the Authority was for a term of forty (40) years after the date of the delivery and payment for the first issue or series of bonds, and for any period thereafter during which any bonds are outstanding.

In furtherance of the agreement with the Corporations, the Authority issued a series of revenue bonds, and the Corporations committed to retire the bonded indebtedness through payment of a semi-annual Facilities Charge. The Corporations also became responsible for payment of a Service Charge amounting to 74% of the Authority's annual direct costs and expenses directly associated with the operation and maintenance of the facilities, and based upon the Authority's annual operating budget for Lake Fork Creek Reservoir. The Corporations were to construct at their expense all of the necessary works to provide for water intake and withdrawal at the points of delivery identified in the agreement. The reservoir was completed and the dam closed in 1980.

Under the 1974 agreement and a subsequent agreement in 1981, in consideration for the payment of the Facilities Charge and the Service Charge, the Corporations were entitled to withdraw certain amounts of water, ultimately for purposes of generating power at their generating plant on Lake Fork Creek Reservoir. The 1981 agreement with the Corporations was to have expired on January 1, 2014, but contained a renewal provision whereby the Corporations would have the option to thereafter continue to purchase water from Lake Fork Creek Reservoir

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[5] Water Supply Facilities Agreement at § 1.11 (1974). A copy of this agreement is attached to Sabine River Authority's Response to City of Dallas' Original Petition and Request for Interim Rates at Attachment A (Dec. 2, 2014). The reservoir is also sometimes referred to as the Lake Fork Reservoir.

for "such price as is prevailing in the general area at that time for contract sales of water of similar quality, quantity, and contract period."[6]

In 1981, after the construction of the dam was completed in 1980 and the reservoir began to fill, the Corporations determined to sell their interest in the water impounded in the reservoir. An agreement between the Corporations, the Authority, and the City of Dallas was executed on October 1, 1981.[7] Under this 1981 agreement, the City of Dallas stepped into the shoes of the Corporations, and paid for the right to divert up to 74% of the firm yield of the Lake Fork Reservoir. The compensation to be paid by Dallas for such purchase during the initial term of the agreement (which expired on November 1, 2014) consisted of two parts: (1) the City agreed to pay 74% of the Authority's operating and maintenance budget for Lake Fork Reservoir ("Service Charge"); and (2) the City agreed to pay the debt service connected with the Authority's sale of bonds to impound the waters of the Sabine River and construct the Lake Fork Reservoir and its attendant facilities ("Facilities Charge").

In the 1981 contract, Dallas and the Authority agreed that the contract would renew for an additional term of forty (40) years unless the City opted by a date certain to terminate the contract. The City timely notified the Authority that the City wanted to renew the contract. Under the terms of the 1981 contract, the parties agreed to a ***different*** amount of compensation to be payable by the City for the renewal term. Anticipating that the debt incurred to construct the reservoir and the facilities would be retired by the time of the renewal,[8] the parties wrote into the contract that compensation under the renewal term would also consist of two parts: (1) the City agreed to continue to pay 74% of the Authority's operating and maintenance budget for Lake

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[6] *See* Water Purchase Agreement at § 13.01 (Oct. 1, 1981). A copy of this 1981 Agreement is attached to Sabine River Authority's Response at Attachment B.

[7] The Water Supply Contract and Conveyance (Oct. 1, 1981) between the Authority, the Corporations, and the City is attached to Sabine River Authority's Response at Attachment C.

[8] In fact, the debt was retired in 2005.

Fork Reservoir ("Service Charge"); and (2) the City agreed to pay a ***new rate*** to compensate the Authority for the value of the Lake Fork Reservoir water. This new rate was to be determined "taking into account such price as is prevailing in the general area at the time for like contract sales of water of similar quality, quantity, and contract period."[9]

On October 9, 2014, after years of unsuccessful negotiations with the City, in which the City refused to take into account the prevailing rate, the Authority adopted a new rate taking into account the prices prevailing in the general area at the time for like contract sales of water of similar quality, quantity, and contract period. The City of Dallas filed its petition appealing the rate on October 30, 2014. A prehearing conference was held at SOAH on January 6, 2015, at which time the ALJ determined that a public interest hearing under P.U.C. SUBST. R. 24.133 was necessary, and also determined that he was without authority to order interim rates without the Commission having first determined that the protested rate adversely affects the public interest.[10] However, when Order No. 4 was issued, the ALJ reversed his position both on interim rates and on the necessity to hold a public interest hearing.

IV. ORDER NO. 4 IS AN UNAUTHORIZED ADJUDICATION OF CONTRACTUAL OBLIGATIONS

Order No. 4 is an improper exercise of authority to resolve a contractual dispute, and fails to give the required deference to the written contract of the parties. The Order accepts the Commission's jurisdiction over the contractual rates that were set by the Authority, while at the same time determining that the contract is of no force or effect.

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[9] Water Supply Contract and Conveyance at § 6.02 (Oct. 1, 1981).

[10] Order No. 4 at 4 and 6.

A. The Commission May Not Adjudicate Contract Disputes.

Texas courts have long held that state agencies such as the PUC and the Railroad Commission cannot adjudicate contractual rights.[11] Consistent with the courts' rulings, the PUC has previously recognized it has no general authority to resolve contractual disputes.[12] That is why P.U.C. SUBST. R. 24.131(d) ***requires*** the ALJ to abate the proceedings in order to allow the contractual disputes to be resolved in a proper forum. Therefore, the Commission has no authority to determine whether or not the protested rate was set in compliance with the contract.

1. Order No. 4 negates the validity of the contract.

The ALJ determined in Order No. 4 that the contract did not specify a rate, therefore, the rate set by the Authority could not be a rate set pursuant to the contract. Even if the ALJ is correct in his determination to resolve the contractual dispute by ruling that the rate was *not* set "pursuant to the contract" so as to bypass the public interest test, setting interim rates is still beyond the Commission's authority because such a determination essentially means that there is no valid contract. If the prevailing rate set by the SRA was not set pursuant to the contract, the inevitable conclusion is that the contract itself fails as a matter of law.

It is well settled that if an agreement leaves material matters open for a future agreement that does not in fact occur, the contract is not binding on the parties, and "merely constitutes an agreement to agree."[13] The Texas Supreme Court has held that if an agreement for a future contract lacks the essential term of the compensation one party would receive, the contract is

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[11] *Railroad Commission of Texas v. City of Austin*, 512 S.W.2d 345, 348-349 (Tex. Civ. App.—Austin 1974, writ granted), rev'd on other grounds, 524 S.W.2d 262 (Tex. 1975).

[12] *See e.g., Complaint of Frazier & Frazier Industries, Inc. Against TXU Energy*, Docket No. 27530, Preliminary Order at 5-6 (July 30, 2004); *Complaint of CenterPoint Energy, Inc. and Texas Genco, LP Against Utility Choice LLC*, Docket No. 27745, Preliminary Order at 6 (Aug. 18, 2003); *Complaint of Greater Houston Retailers Association Against Tara Energy LP*, Docket No. 33967, Preliminary Order at 3 (June 13, 2007).

[13] *Fort Worth Independent School District v. City of Fort Worth*, 22 S.W.3d 831, 846 (Tex. 2000).

unenforceable.[14] Thus, either the prevailing rate being charged by SRA must be a rate being charged "pursuant to the contract," or the contract itself is unenforceable for failure to include an essential term. If Dallas's claim results in the latter outcome, the Commission does not have jurisdiction to adjudicate the enforceability of a contract and this proceeding must be dismissed.

One element of the contract between the parties requires the parties to mutually agree to the new rate taking into account the prevailing price, as quoted above. This contractual provision is currently in dispute between the parties. It is the Authority's position that the City's insistence on removing the prevailing price provision from the renewal term is contrary to the requirements of the contract that the parties mutually agree on the prevailing price. Obviously, the City views the situation differently. Therein lies the substance of the parties' dispute. Notably, the parties do ***not*** dispute the fact that their relationship is governed by a contract. Instead, the only dispute involves the interpretation and construction of the contract term setting forth how the renewal rate is to be established.

2. Even if the contract is not unenforceable for indefiniteness, the ALJ's ruling that the contingent term has not occurred means there is no contract.

If the Commission agrees with and adopts the ALJ's finding that there is no rate because there is no mechanism in the contract for setting the rate, the result is that there simply is no contract agreement in place at all. The renewal provision of the contract provides for the rate to be set by mutual agreement of the parties taking into account prevailing rates. This is the contractual mechanism for setting the rate. If the ALJ's ruling, that the rate was set without support by any contractual provision, remains in effect, the only possible outcome is that there is no "mutual agreement" as to the prevailing rate and the contract fails by its own terms. Price is an essential contract term. The contract fails for failure of an essential term if the parties cannot

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[14] *Fort Worth Independent School District*, 22 S.W.3d at 847.

reach a mutual agreement as required by the contract.[15] If there is no contract between the parties, then there are no corresponding rights or obligations and the Commission has no authority to set a rate under Subchapter I of the PUC rules on wholesale rate appeals.

3. The ALJ must abate the proceeding and not adjudicate the contractual dispute.

The provisions of P.U.C. SUBST. R. Chapter 24, Subchapter I, provide "substantive guidelines and procedural requirements" concerning petitions filed to review rates charged for the sale of water for resale under Texas Water Code Chapter 12.[16] These provisions specifically anticipate that the parties may have disputes involving the documents governing their relationship and the setting of rates, by ***requiring*** the ALJ to abate proceedings at SOAH "until the contract dispute over whether the protested rate is part of the contract has been resolved by a court of proper jurisdiction."[17] The ALJ has acknowledged the existence of a contractual dispute and has provided an opportunity to either party to file a motion to abate by January 20, 2015. The Authority is filing such a motion concurrently with the filing of this Appeal. This Appeal will not be rendered moot if this proceeding is abated; the ALJ has stated in Order No. 4 that "no public interest hearing is necessary."[18] Therefore, unless Order No. 4 is overturned, the Authority will continue to be deprived of its right to have contractual rates reviewed under the public interest standard of P.U.C. SUBST. R. 24.133.

Given the existence of the contractual dispute, it is error for the ALJ to take any further action, including making a judicial determination that the contract does not set a rate. By

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[15] *Fiduciary Financial Services of the Southwest, Inc. v. Corilant Financial, L.P.*, 376 S.W.3d 253, 258 (Tex. App.—Dallas 2012, pet. denied) (explaining that a court has no authority to supply an essential term of a contract on which the parties were unable to mutually agree).

[16] P.U.C. SUBST. R. 24.128(1). The ALJ has declined to rule on whether jurisdiction also lies under Chapter 13; the Authority contends it does not.

[17] P.U.C. SUBST. R. 24.131(d).

[18] Order No. 4 at 2 and 4.

rendering his interpretation of the contractual provisions, the ALJ may have called into question the very existence of a valid contract between the parties. The only possible result of such an interpretation is that the contract will fail due to lack of an essential term, and the Authority has no continuing obligation to Dallas thereunder.

B. The Commission Does Not Have Authority to Modify Contractual Rates Without a Public Interest Finding.

At the prehearing conference in this matter on January 6, 2015, the ALJ made an oral ruling, finding that he was without authority to order interim rates in the appeal without first undertaking a public interest inquiry. Order No. 4 reversed that position, and the ALJ has now determined that he does have authority to order interim rates. The only basis for this reversal is his interpretation of P.U.C. SUBST. R. 24.131, to-wit: the protested rate was not set "pursuant to a written contract" because it was not set "in compliance with the written contract," and therefore there is no need to hold a public interest inquiry before modifying the contractual rates.[19]

Order No. 4 is incorrect. The rate currently being charged was set pursuant to the contract; therefore, the Commission does not have authority to change that rate prior to a finding that the rate is adverse to the public interest.

1. The rate was set pursuant to the written contract.

The contract term at issue in this proceeding states that the contract between Dallas and SRA could be renewed pursuant to the following:

> 6.02 The amount of compensation that the Authority shall be entitled to receive during any renewal term (exclusive of the City's pro rata share of the Service Charge) shall be determined by mutual agreement between the City and the Authority, ***taking into account such price as is prevailing in the general area at the time***

[19] Order No. 4 at 2 and 6.

> ***for like contract sales of water of similar quality, quantity, and contract period***.... [Emphasis added.][20]

The ALJ's conclusion that there is ***no*** contractual rate in place is incorrect – the SRA set a rate at the "prevailing price" pursuant to the contract, and Dallas is currently taking the water being provided and invoiced at that prevailing rate.

Order No. 4 construes the provisions of the contract and finds them lacking: "While the Contract specifies that SRA and Dallas shall take the prevailing rate into account when setting the rate for the new term, the Contract does not say that Dallas would pay the prevailing rate or specify exactly how the new rate would be set."[21] Right or wrong, that finding is a construction of the contract by the ALJ, and is thus outside the authority of SOAH and the Commission. Further, even if it was within the ALJ's authority, such finding is wrong under the law.

Texas courts have long applied the maxim "*expressio unius est exclusio alterius*," which explains that in contract interpretation the expression of one thing is the exclusion of another. When this maxim is applied as a rule of construction, a contract's expression of "one or more things of a class implies the exclusion of all not expressed, even though all would have been implied had none been expressed."[22] Therefore, the fact that Dallas and SRA specifically identified in the contract ***only*** the "prevailing rate" as the factor to be considered in setting rates for the renewal term of the contract, necessarily excludes other factors from being considered.

The Authority set the rate pursuant to the only requirement set forth in the contract – the prevailing rate. If the ALJ believes that some other unidentified factor must be considered, that is a contract determination that must be made by a court with the authority to adjudicate a contractual dispute, not this Commission.

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[20] *See* Water Supply Contract and Conveyance (Oct. 1, 1981).

[21] Order No. 4 at 4.

[22] *Oxy USA, Inc. v. Southwestern Energy Production Company*, 161 S.W.3d 277, 285 (Tex. App.—Corpus Christi 2005, pet. denied).

2. "Pursuant to" does not mean "in compliance with."

The ALJ has also erroneously construed P.U.C. SUBST. R. 24.131(b), (c), and (d). These provisions direct the procedures to be used for rates depending on whether or not they are "charged pursuant to a written contract." The ***only*** relationship the parties have regarding raw water is the 1981 contract.[23] Clearly, the rates are charged under the 1981 contract, otherwise the Authority would have no obligation to sell, and Dallas would have no obligation to buy, the water in Lake Fork Reservoir. However, the ALJ effectively has accepted Dallas's allegations that the Authority violated the contract, and has unavoidably thereby determined that "pursuant to" equates to "in compliance with." This is in direct contradiction to the acknowledged prohibition on the Commission determining and adjudicating the parties' obligations under the contract, and is also contrary to the stated purpose of the public interest rule when it was originally adopted and subsequently revised.

The courts have ruled that these very same regulatory provisions do not require that a contract set a fixed water price in order for the rate to be charged "pursuant to a contract." In *Canyon Regional Water Authority v. Guadalupe-Blanco River Authority,* the parties to a contract disagreed as to whether the rates were set pursuant to the contract. Rather than undertake an impermissible construction of the contract, the ALJ in that proceeding appropriately abated the petition and allowed the parties to take the contractual dispute to district court. Ultimately, the court of appeals concluded that an open-term price provision in the contract that calculated the price of wholesale water based upon a different water rate was, in fact, a rate set "pursuant to the contract," thereby making the buyer's rate appeal subject to a public interest hearing.[24] The

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[23] The ALJ acknowledges the existence of the 1981 agreement, and also acknowledges that "SRA provides wholesale raw water to Dallas ***pursuant to a set of written contracts*** ...." Order No. 4 at 2. (Emphasis added.)

[24] *Canyon Regional Water Authority v. Guadalupe-Blanco River Authority*, 286 S.W.3d 397, 403-04 (Tex. App.—Corpus Christi 2008, pet. granted).

court explained that a rate does not need to be a permanent, fixed number in a contract in order for the rate to be considered as being set "pursuant to the contract."[25]

The rate "charged pursuant to the written contract" in this case is the prevailing rate. If Dallas disputes what the term "prevailing" rate means, that dispute must be litigated in district court. But, it is improper for the ALJ to conclude that the rate was not set "pursuant to the contract," both because such a conclusion is beyond his authority, and because it is legally incorrect. Indeed, the ALJ's determination that the rate was not set ***in compliance*** with the contract deprives the Authority of the right to have the courts resolve the contractual dispute and to have the Commission determine whether the rate is adverse to the public interest.[26]

3. Order No. 4 is contrary to the purpose of the rule as originally adopted and as later revised.

When the original public interest rules were adopted by the Texas Natural Resource Conservation Commission ("TNRCC") in 1994, there was a significant amount of discussion in comments to the proposed rules regarding the new public interest standard to be applied in the appeal of wholesale rates. In responding to a comment that the rule should be amended to limit its applicability to instances where service is provided pursuant to a contract, the TNRCC agreed and stated: "The commission agrees that these rules should apply only to those petitions filed that ***involve a written contract***, including filings submitted pursuant to Chapters 11 and 12 of the Texas Water Code...[R]ates set forth in a contract do not generally give rise to appeals before the commission. It is those rates demanded *pursuant* to a contract that are usually appealed."[27]

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[25] *Id.*

[26] P.U.C. SUBST. R. 24.132(c).

[27] 19 Tex. Reg. 6227 (1994) (emphasis added).

As originally adopted in 1994, 30 Tex. Admin. Code §§ 291.128 and 291.131 read as follows:[28]

> **§ 291.128. Petition or Appeal Concerning Wholesale Rates.** This subchapter sets forth substantive guidelines and procedural requirements concerning:
>
> (1) a petition to review rates charged pursuant to a written contract for the sale of water for resale filed pursuant to the Texas Water Code, Chapter 11 or 12; or
>
> (2) an appeal pursuant to the Texas Water Code, §13.043(f), (appeal by a retail public utility concerning a decision by a provider of water or sewer service).
>
> **§ 291.131. Executive Director's Determination of Probable Grounds.** When a petition or appeal is filed, including a petition subject to the Texas Water Code, § 11.041, the executive director shall determine within ten days of the filing of the petition or appeal whether the petition contains all of the information required by this subchapter. For purposes of this section only, the executive director's review of probable grounds shall be limited to a determination whether the petitioner has met the requirements of §291.130 of this title (relating to Petition or Appeal). If the executive director determines that the petition or appeal does not meet the requirements of §291.130, the executive director shall inform the petitioner of the deficiencies with the petition or appeal and allow the petitioner the opportunity to correct these deficiencies. If the executive director determines that the petition or appeal does meet the requirements of §291.130, the executive director shall forward the petition or appeal to the office of *hearings examiners for an evidentiary hearing.*[29]

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[28] When the PUC assumed jurisdiction over the economic regulation of water and sewer utilities on September 1, 2014, and adopted new substantive rules to implement that regulation, the TCEQ's rules in 30 Tex. Admin. Code Chapter 291 were essentially renumbered to change the prefix of "291" to "24" and were included within Chapter 24 of the PUC's substantive rules.

[29] 10 Tex. Reg. 6230 (1994).

The current versions of P.U.C. SUBST. R. 24.128 and 24.131(d) were adopted in 2000 when the TNRCC revised 30 Tex. Admin. Code §§ 291.128 and 291.131. The TNRCC's explanation for the revisions was as follows:

> The following amendments are adopted to clarify when a public interest hearing versus a cost of service hearing is appropriate.
>
> The amendments to §291.128 makes this section applicable to petitions for the review of rates charged for the resale of water ***regardless of whether there is a contract or not.***
>
> The amendments to § 291.131 change the section title from "Executive Director's Determination of Probable Grounds" to "Executive Director's Review of Petition or Appeal" and add subsections (b), (c), and (d) that allow the executive director to forward petitions to review a rate that is charged pursuant to a written contract to the State Office of Administrative Hearings (SOAH) for an evidentiary hearing on public interest, ***or, where there is no contract,*** to SOAH for an evidentiary hearing on the rate. The amendments also provide that if the seller and buyer do not agree that the protested rate is charged pursuant to a written contract, the administrative law judge (ALJ) will abate the hearing until the dispute is resolved by a court of proper jurisdiction.[30]

The history of P.U.C. SUBST. R. 24.128 and 24.131(d) provides clear evidence that ***if there is a contract***, the appeal of rates is an appeal that must proceed through the bifurcated hearing process, including the initial determination of whether the rates are adverse to the public interest. Dallas has pled no right to the Lake Fork Reservoir water independent of the written contract. Order No. 4 ignores the foundation for the Commission's rule, and is in error.

4. The Constitution requires that the parties' contract be given deference.

Texas courts have held that wholesale rates set pursuant to a written contract are not to be lightly set aside. In *Texas Water Commission v. City of Fort Worth*, the Third Court of Appeals held that before the agency could modify contract rates (an action that logically must include

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[30] 25 Tex. Reg. 10369 (2000).

changing the rates, even for an interim period), the agency must "first make a finding that the ***rates affected by a 'decision of the provider'*** adversely affect the public interest by being unreasonably preferential, prejudicial, or discriminatory."[31]

The court of appeals' decision in *City of Fort Worth* was soundly based on its prior opinion in *High Plains Natural Gas Company. v. Railroad Commission of Texas,* in which it wisely decided to:

> ...follow the mandate of the United States Supreme Court in its construction [of statutory provisions charging the state agency with establishing and fixing fair and reasonable rates]. We hold that in order to set the contract aside, the Appellant was charged with the burden of showing that a continuance of the contract would adversely affect the public interest in that it might impair the ability of the pipeline to continue its service, cast upon other consumers an excessive burden or be unduly discriminatory. At this point the contract would become subject to 'review, revision and regulation by the Commission.' It is not enough that the pipeline made a bad bargain.[32]

An appeal of wholesale water rates set by a "decision of the provider" when a written contract exists is a two-phase process. The initial review is focused exclusively on whether the petitioner has met its burden of showing that the protested rates are adverse to the public interest. The Commission's rules list the specific factors to be considered in determining whether this burden has been met.[33] Unless the public interest proceeding has been held and the Commission has found that the petitioner has met its burden, there can be no overturning of contractually-set rates, including the imposition of interim rates. Otherwise, any petitioner who becomes unhappy with a contract that it negotiated 30 years ago could argue to the Commission that ***now*** the rates are unjust and unreasonable and obtain immediate rate relief through interim rates without any

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[31] *Texas Water Commission v. City of Fort Worth*, 875 S.W.2d 332, 336 (Tex. App.—Austin 1994, writ denied) (emphasis added).

[32] *High Plains Natural Gas Company v. Railroad Commission of Texas*, 467 S.W.2d 532, 537 (Tex. Civ. App.—Austin 1971, writ ref'd n.r.e).

[33] P.U.C. SUBST. R. 24.133(a).

examination as to whether the contractual rates are, indeed, adverse to the public interest. Neither case law nor the Commission's rules allow the Commission to change contract rates, even on an interim basis, on the simple allegation that the petitioner now considers the rates to be unjust, or unreasonable, or not quite the deal that it thought it was getting at the onset of the contractual relationship.

The Commission's public hearing inquiry was fashioned in order to implement the court opinions in *High Plains Natural Gas Company v. Railroad Commission of Texas*,[34] and *Texas Water Commission v. City of Fort Worth*[35] and to give due deference to written contracts:

> The commission believes a review process with an ***inherent deference to contracts*** will encourage careful planning by sellers and purchasers, foster regionalization and generate an efficiency factor absent from the current process.[36]

C. Neither P.U.C. SUBST. R. 24.29 Nor P.U.C. PROC. R. 22.125(c) Apply to this Proceeding.

Even if jurisdiction of the petition exists under Texas Water Code Chapter 12, the Commission rules do not allow for interim rates. P.U.C. PROC. R. 22.125(c), cited by the ALJ for his authority to set an interim rate, is inapplicable, as indicated by its structure and content. An examination of this rule illustrates that it is applicable to rate increases proposed by utilities over whom the Commission has original rate jurisdiction. Subsection 22.125(b) addresses "requests for interim rates" being filed 30 days before the rate is proposed to take effect; Subsection 22.125(d) addresses the burden of proof and places that burden on the utility to show that the change (*i.e.*, interim rate) proposed by the utility is just and reasonable. The Authority is

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[34] *High Plains Natural Gas Company v. Railroad Commission of Texas*, 467 S.W.2d 532 (Tex. Civ. App.—Austin 1971, writ ref'd n.r.e).

[35] *Texas Water Commission v City of Fort Worth*, 875 S.W.2d 332 (Tex. App.—Austin 1994, writ denied).

[36] 19 Tex. Reg. 6227 (2004) (emphasis added).

not requesting interim rates, therefore it bears no burden proving the need for same. The selection of only one subsection of the rule by the ALJ, Subsection 22.125(c), pulls that provision out of context of the entire rule, which clearly not does apply to this proceeding.

Neither does P.U.C. SUBST. R. 24.29 apply here. P.U.C. SUBST. R. 24.29(a) applies only to proceedings under Texas Water Code § 13.043(a), (b), or (f), and Rule 24.29(b) only applies to the filing of a statement intent to change rates under Chapter 13 of the Texas Water Code. Therefore, Rules 24.29(a) and (b) cannot apply to a proceeding brought under Chapter 12.[37]

Additionally, P.U.C. PROC. R. 22.125(c) and P.U.C. SUBST. R. 24.29(d) and (e) do not stand alone, but must be read in tandem with P.U.C. SUBST. R. 24.128–24.138. These provisions do not override the specific regulatory provisions that provide the ***substantive and procedural requirements*** for the Commission's review of wholesale contractual rates. P.U.C. SUBST. R. 24.128 specifically so provides:

> **§ 24.128. Petition or Appeal Concerning Wholesale Rate.**
>
> This subchapter sets forth ***substantive guidelines and procedural requirements*** concerning:
>
> (1) a petition to review rates charged for the sale of water for resale filed pursuant to TWC, Chapter 12; or
>
> (2) an appeal pursuant to TWC, §13.043(f) (appeal by retail public utility concerning a decision by a provider of water or sewer service).
>
> [Emphasis added.]

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[37] It is instructive to review the Staff Strawman Rule Amendments to Chapter 24, filed on January 16, 2015, in PUC Project No. 43871, *PUC Rulemaking Proceeding to Amend Chapters 22 and 24 for Implementation of Phase II of the Economic Regulation of Water and Sewer Utilities.* In the strawman rule amendments, which will be the topic of a workshop to be held on January 27, 2015, the Commission Staff has proposed revisions to P.U.C. SUBST. R. 24.29 that make it very clear that the rule applies ***only*** to proceedings under Texas Water Code Chapter 13. Paragraph (a) of the strawman reads: "(a) Application. This section sets criteria by which a utility may charge interim rates or bonded rates during the pendency of a proceeding established pursuant to TWC, §§ 13.043, 13.187, or 13.1871." Paragraph (b) applies to proceedings pursuant to Texas Water Code § 13.043, paragraph (c) to TWC §§ 13.187 and 13.1871. While it is understood that the rule has not yet been revised, the clarification provided by this draft rule on the inapplicability of the existing rule to the instant proceeding is quite valuable.

Although neither P.U.C. PROC. R. 22.125(c) nor P.U.C. SUBST. R. 24.29(d) or (e) override this provision that protects the parties' fundamental right to contract as they see fit, Order No. 4 removes this protection, giving notice of the ALJ's intent to set an interim rate prior to a public interest finding. As previously addressed, a finding that rates are "unjust or unreasonable" can only take place ***after*** the ALJ has applied the specific public interest criteria in P.U.C. SUBST. R. 24.133(a). Substantive Rule 24.29(d) and Procedural Rule 22.125(c) are not independent, free-standing authorization for interim rates in the context of a written wholesale water contract.

Nor can the parties themselves waive the holding of a public interest hearing prior to the modification of contractual rates. The public interest hearing is jurisdictional; before modifying contractual rates, the Commission ***must*** find that the rates adversely affect the public interest.[38] P.U.C. SUBST. R. 24.132(d) allows the parties to agree to consolidate the evidentiary hearing on the public interest and the evidentiary hearing on the cost of service, but neither party may compel that consolidation. Therefore, the finding that interim rates may be set in this proceeding must be reversed.

V. CONCLUSION AND PRAYER

The City's allegations of violation of contract require this matter to be abated to be litigated by a court with appropriate jurisdiction. The Commission does not have the authority to change the rates set pursuant to a written contract without a finding on the public interest. Therefore, the Authority requests that the Commission hold that this matter must be abated and, if the matter returns to the Commission, it be processed in accordance with the Constitution of the State of Texas, in accordance with controlling case law, and in accordance with the

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[38] *Texas Water Commission*, 875 S.W.2d at 336.

provisions of P.U.C. SUBST. R. 24.133. The Authority specifically requests that Order No. 4 be reversed.

Respectfully submitted,

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ATTORNEYS FOR SABINE RIVER AUTHORITY

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing document was transmitted by e-mail, fax, hand-delivery and/or regular, first class mail on this 20th day of January, 2015, to the parties of record.

GEORGIA N. CRUMP