



## **Filing Receipt**

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**Item Number - 38**

**DOCKET NO. 54617**

<b>APPLICATION OF TEXAS WATER UTILITIES, LP AND SOUTHERN HORIZONS DEVELOPMENT, INC. FOR SALE, TRANSFER, OR MERGER OF FACILITIES AND CERTIFICATE RIGHTS IN LIBERTY AND MONTGOMERY COUNTIES</b>	<b>§ § § § § § §</b>	<b>PUBLIC UTILITY COMMISSION  OF TEXAS</b>
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**COMMISSION STAFF'S RECOMMENDATION ON APPROVAL OF THE TRANSACTION**

**I. INTRODUCTION**

On February 2, 2023, Texas Water Utilities, LP (Texas Water) and Southern Horizons Development, Inc. (collectively, Applicants) filed an application for the sale, transfer, or merger of facilities and certificate rights in Liberty and Montgomery counties. Texas Water filed supplemental information on February 16, March 15, April 6, and June 23, 2023.

On June 22, 2023, the administrative law judge (ALJ) filed Order No. 9, directing the Staff (Staff) of the Public Utility Commission of Texas (Commission) to request a hearing or file a recommendation on approval of the transaction by July 17, 2023. Therefore, this pleading is timely filed.

**II. RECOMMENDATION ON APPROVAL OF THE SALE**

Staff has reviewed the application, as supplemented, and, as supported by the memoranda of James Harville, Infrastructure Division, and Fred Bednarski III, Rate Regulation Division, recommends and respectfully requests the entry of an order permitting the proposed transaction to proceed. Under 16 TAC § 24.239(i), and TWC §§ 13.246 and 13.301, Staff recommends that this transaction will serve the public interest and should be allowed to proceed without a public hearing. If the transaction is permitted to proceed, Staff further requests that the Applicants be required to file evidence that all assets have been transferred to the acquiring entity and that the disposition of any remaining deposits have been addressed as soon as possible, as required by 16 TAC § 24.239(l).

Staff notes that the approval of the sale expires 180 days from the date of the Commission's written approval of the sale. If the sale is not consummated within that period, and unless the

Applicants request and receive an extension from the Commission, the approval is void, and the Applicants must re-apply for the approval of the sale, as required by 16 TAC § 24.239(m).

### III. CONCLUSION

Staff respectfully requests the entry of an order permitting the proposed transaction to proceed.

Date: July 17, 2023

Respectfully submitted,

**PUBLIC UTILITY COMMISSION OF TEXAS  
LEGAL DIVISION**

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*/s/ Margaux Fox*  
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**DOCKET NO. 54617**

**CERTIFICATE OF SERVICE**

I certify that unless otherwise ordered by the presiding officer, notice of the filing of this document was provided to all parties of record via electronic mail on July 17, 2023 in accordance with the Second Order Suspending Rules, filed in Project No. 50664.

*/s/ Margaux Fox*  
Margaux Fox

# *Public Utility Commission of Texas*

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## **Memorandum**

**TO:** Margaux Fox, Attorney  
Legal Division

**FROM:** James Harville, Infrastructure Analyst  
Infrastructure Division

**DATE:** July 17, 2023

**RE:** Docket No. 54617 – *Application of Texas Water Utilities, LP and Southern Horizons Development, Inc. for Sale, Transfer, or Merger of Facilities and Certificate Rights in Liberty and Montgomery Counties*

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### **1. Application**

On February 2, 2023, Texas Water Utilities, LP (Texas Water) and Southern Horizons Development, Inc. (Southern Horizons) (collectively Applicants) filed an application for sale, transfer, or merger (STM) of facilities and certificate rights in Liberty and Montgomery counties, Texas, under Texas Water Code (TWC) §§ 13.242 through 13.250 and § 13.301 and 16 Texas Administrative Code (TAC) §§ 24.225 to 24.237 and § 24.239.

Specifically, Texas Water, Certificate of Convenience and Necessity (CCN) No. 12983, seeks approval to acquire facilities and to transfer all of the water service area from Southern Horizons under water CCN No. 12863.

Based on the mapping review by Hank Journey, Infrastructure Division:

- The requested area includes 452 customer connections and approximately 728.2 acres, comprised of:
  - 102.5 acres of uncertificated area to amend to CCN No. 12983;
  - 527 acres of transferred area from Southern Horizons (CCN No. 12863) to Texas Water (CCN No. 12983); and
  - 98.7 acres of decertified area from CCN No. 12863.
- The application proposes the subtraction of approximately 625.7 acres from CCN No. 12863 and the addition of approximately 629.5 acres to CCN No. 12983.

## **2. Notice**

Texas Water provided notice consistent with 16 TAC § 24.239(c). The deadline to intervene was May 22, 2023; motions to intervene were submitted.

## **3. Factors Considered**

Under TWC §§ 13.241, 13.246, and 13.301 and 16 TAC §§ 24.11(e), 24.227, and 24.239, the Commission must consider certain factors when granting or amending a water or sewer CCN. These factors are addressed below.

### **3.1. *Consideration of the adequacy of service currently provided to the requested area and system compliance (TWC § 13.246(c)(1), 13.301(e)(3)(A); 16 TAC §§ 24.227(a) and (e)(1), 24.239(h)(3)(A), (h)(5)(A), and (h)(5)(I)).***

Southern Horizons has two Texas Commission on Environmental Quality (TCEQ) approved public water systems (PWS) registered as Southern Crossing Water System Phase 2, PWS ID No. 1460158, and Southern Oaks Water System Phase 2, PWS ID No. 1460150. The last TCEQ compliance investigation of each system was on August 12, 2022. Southern Horizons has violations listed in the TCEQ database being addressed. The Commission's complaint records, which date back 5 years, show 4 complaints against Southern Horizons. All the complaints have been reviewed and closed by the Commission's Customer Protection Division.

### **3.2. *Consideration of the need for additional service in the requested area (TWC § 13.246(c)(2); 16 TAC §§ 24.227(e)(2) and 24.239(h)(5)(B)).***

The purpose of the transaction is to transfer Southern Horizons to Texas Water. The customers are currently receiving water service from Southern Horizons' water systems.

### **3.3. *Consideration of the effect of granting an amendment on the recipient of the certificate or amendment, on the landowners in the area, and on any other retail public utility of the same kind already servicing the proximate area (TWC § 13.246(c)(3), 16 TAC §§ 24.227(e)(3), 24.239(h)(5)(c)).***

Texas Water will be the certificated entity for the requested area and be required to provide continuous and adequate service to the requested area.

There will be no effect on landowners as the area is currently certificated. There are no landowners with 25 or more acres in the additional requested area.

There will be no effect on any retail public utility servicing the proximate area. All retail public utilities in the proximate area were provided notice of the transaction taking place in this application and did not request to intervene.

### **3.4. *Consideration of the managerial and technical ability of the applicant to provide adequate service (TWC §§ 13.241(a) and (b), 13.246(c)(4); and 13.301(b) and (e)(2); 16 TAC §§ 24.227(a) and (e)(4), and 24.239(f) and (h)(5)(D)).***

TCEQ rule, 30 TAC § 290.46, Minimum Acceptable Operating Practices for Public Drinking Water Systems, requires the operation of a public water system by trained and licensed personnel. The production, treatment, and distribution facilities at the public water system must be operated at all times under the direct supervision of a water works operator who holds an applicable, valid license issued by the TCEQ executive director. The licensed operator of a public water system may be an employee, contractor, or volunteer. Texas Water will have qualified TCEQ licensed operators licensed in water treatment to run the acquired systems.

Texas Water will have licensed operators to run the system operations. Class B, C, and D operators will be the responsible operators for the systems.

Texas Water has the ability to provide adequate service in the requested area. Texas Water has several registered TCEQ approved public water systems. Texas Water has violations listed in the TCEQ database which are being addressed. In addition, the Commission's complaint records, which date back 5 years, show 34 complaints against Texas Water. All the complaints have been reviewed and closed by the Commission's Customer Protection Division.

**3.5. *The applicants' demonstration that regionalization or consolidation with another retail public utility is not economically feasible when construction of a physically separate water or sewer system is required to provide service to the requested area. (TWC § 13.241(d); 16 TAC § 24.227(b)).***

The construction of a physically separate system is not necessary for Texas Water to serve the requested area. Therefore, concerns of regionalization or consolidation do not apply.

**3.6. *Consideration of the feasibility of obtaining service from an adjacent retail public utility (TWC § 13.246(c)(5); 16 TAC §§ 24.227(e)(5) and 24.239(h)(5)(E)).***

Southern Horizons is currently serving customers and has sufficient capacity. Obtaining service from an adjacent retail public utility would likely increase costs to customers because new facilities will need to be constructed. At the minimum, an interconnect would need to be installed in order to connect to a neighboring retail public utility. Therefore, it is not feasible to obtain service from an adjacent retail public utility.

**3.7. *An application for a certificate of public convenience and necessity or for an amendment to a certificate must contain: a capital improvements plan, including a budget and estimated timeline for construction of all facilities necessary to provide full service to the entire proposed service area (TWC § 13.244(d)(3)).***

Texas Water is proposing to make improvements to the Southern Horizons' water system. The proposed capital improvements are expected to exceed \$100,000, therefore the need for firm capital commitment under 16 TAC § 24.11(e)(5) is required. Construction of the water system facilities is expected to be in 2023 and 2024.

The Rate Regulation Division will be addressing the need for firm capital commitment criterion in a separate memo.

- 3.8. *Consideration of the financial ability of the applicant to pay for facilities necessary to provide continuous and adequate service (TWC §§ 13.246(c)(6) and 13.301(b); 16 TAC §§ 24.227(a) and (e)(6), 24.11(e), and 24.239(f) and (h)(5)(F)).*

The Rate Regulation Division will be addressing this criterion in a separate memo.

- 3.9. *Requirement of the applicant to provide a bond or other financial assurance in a form and amount specified by the Commission to ensure that continuous and adequate utility service is provided (TWC §§ 13.246(d), 13.301(c); 16 TAC §§ 24.227(f), 24.239(f)).*

The Rate Regulation Division will be addressing this criterion in a separate memo.

- 3.10. *Consideration of the environmental integrity and the effect on the land to be included in the certificated area (TWC § 13.246(c)(7) and (9); and 16 TAC §§ 24.227(e)(7) and (9) and 24.239(h)(5)(G)).*

The environmental integrity of the land will be minimally affected as facilities are constructed to provide service to the requested area.

- 3.11. *Consideration of the initial rates for certain water or sewer systems after purchase or acquisition (TWC § 13.3011).*

As allowed by the statute, Texas Water has requested that the customers' rates be changed to match Texas Water's currently effective approved rates. Texas Water's currently approved rates have been in effect since September 6, 2022<sup>1</sup> which is the most recent date prior to the date the application was deemed administratively complete, April 5, 2023.<sup>2</sup>

- 3.12. *Consideration of the probable improvement in service or lowering of cost to consumers (TWC § 13.246(c)(8); 16 TAC §§ 24.227(e)(8), 24.239(h)(5)(H)).*

The customers' rates will be higher than the current rates for the Southern Horizons. Reliability and quality of water service is expected to improve under Texas Water's management.

#### **4. Recommendation**

Based on the above information, I recommend that the Commission find that the transaction will serve the public interest and that the Applicants be allowed to proceed with the proposed transaction. There are no deposits held by Southern Horizons for the customers being served by Southern Horizons. I further recommend that a public hearing is not necessary.

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<sup>1</sup> Docket 52201, Item 54, Stamped Approved Tariff

<sup>2</sup> In Order No. 4 filed on 4/5/2023, the administrative law judge found the application administratively complete.



# *Public Utility Commission of Texas*

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## **Memorandum**

**TO:** Margaux Fox  
Legal Division

**FROM:** Fred Bednarski III  
Rate Regulation Division

**DATE:** July 17, 2023

**RE:** Docket No. 54617 – *Application of Texas Water Utilities, LP and Southern Horizons Development, Inc. for Sale, Transfer, or Merger of Facilities and Certificate Rights in Liberty and Montgomery Counties*

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On February 2, 2023, Texas Water Utilities, LP (TWU) and Southern Horizons Development, Inc. (Southern Horizons) filed an application for the sale and transfer of facilities and certificate rights in Liberty and Montgomery counties under the provisions of Texas Water Code § 13.301 and 16 Texas Administrative Code § 24.239.

An owner or operator of a retail public utility must have the financial resources to operate and manage the utility and to provide continuous and adequate service to the current and requested utility service areas, as established by 16 Texas Administrative Code (TAC) § 24.11. TWU must demonstrate that it meets one of the five leverage tests under 16 TAC § 24.11(e)(2) as well as the operations test under 16 TAC § 24.11(e)(3).

### ***Leverage Test***

TWU filed an affidavit stating that SouthWest Water Company (SouthWest) is capable, available, and willing to cover any temporary cash shortages and operating expense shortfalls.<sup>1</sup>

My analysis is based on financial statements ending December 31, 2021. These financial statements contain an unqualified auditor’s opinion from PricewaterhouseCoopers LLP stating that

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<sup>1</sup> Confidential attachments to STM application at pdf 98 and 99 (Feb. 2, 2023).

the financial statements present fairly, in all material respects, the financial position of SouthWest as of December 31, 2021.<sup>2</sup>

SouthWest's financial statements demonstrate a debt service coverage ratio of 7.56, as provided in confidential attachment FB-1. Because the ratio is greater than 1.25, I recommend a finding that SouthWest meets the leverage test specified in 16 TAC § 24.11(e)(2)(B). Therefore, I recommend a finding that—through its affiliate—TWU meets the leverage test as specified in 16 TAC § 24.11(e)(2)(E).

### ***Operations Test***

An owner or operator must demonstrate sufficient available cash to cover projected cash shortages for operations and maintenance expense during the first five years of operations; or an affiliated interest may provide a written guaranty of coverage of temporary cash shortages if the affiliated interest also satisfies the leverage test, as required by 16 TAC § 24.11(e)(3).

The affidavit provided by TWU demonstrates a written guarantee of coverage of temporary cash shortages from an affiliated interest. TWU projects no net operating and maintenance shortages, as provided in confidential attachment FB-1. Therefore, I recommend a finding that TWU meets the operations test specified in 16 TAC § 24.11(e)(3).

### ***Planned Capital Improvements and Purchase Price***

An applicant proposing service to a new CCN area must provide documentation of adequate funding for the purchase of an existing system plus any improvements necessary to provide continuous and adequate service to the existing customers per 16 TAC § 24.11(e)(5)(A).

TWU has filed documentation demonstrating a firm capital commitment for funding of the purchase price and planned system improvements for Southern Horizons' water system alongside all of TWU's other purchased systems and planned system improvements, as shown in confidential attachment FB-1. Therefore, I recommend a finding that TWU satisfies the requirements of 16 TAC § 24.11(e)(5)(A) and that a good cause exception should be granted if needed.

### ***Fair market value and ratemaking rate base (TWC 13.305(i))***

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<sup>2</sup> *Id.* at pdf 107 and 108.

Because TWU has filed notice with the Commission of its intent to use a fair market value (FMV) process to determine the ratemaking rate base of Southern Horizons, the following provisions of TWC § 13.305 apply to this proceeding:

(f) For the purposes of the acquisition, the fair market value is the average of the three utility valuation expert appraisals conducted under Subsection (c).

(g) For an acquisition of a selling utility, the ratemaking rate base of the selling utility is the lesser of the purchase price negotiated by the acquiring utility and the selling utility or the fair market value. The ratemaking rate base of the selling utility shall be incorporated into the rate base of the acquiring utility during the utility's next rate base case under Subchapter F.

(i) If the utility commission approves the application for acquisition under Section 13.301, the utility commission shall issue an order that includes:

(1) the ratemaking rate base of the selling utility as determined under Subsection (g); and

(2) any additional conditions for the acquisition the utility commission requires.

Consistent with the above statutory provisions, the table in confidential Attachment FB-1 shows the FMV appraisal amount reported by each of the utility valuation experts and the resulting average amount.

Because the average of the three appraisals yields a FMV which equals the sales price, the ratemaking rate base for Southern Horizons is the average of the three appraisal amounts, provided in confidential attachment FB-1, as prescribed by the provisions of TWC § 13.305(g).

***Recommendation***

Because TWU meets the financial tests, I do not recommend that the Commission require additional financial assurance.

Consequently, I recommend a finding that TWU demonstrates the financial and managerial capability needed to provide continuous and adequate service to the area subject to this application.

My conclusions are based on information provided by TWU before the date of this memorandum and may not reflect any changes in TWU's status after this review.