

# State Office of Administrative Hearings



**Shelia Bailey Taylor**  
Chief Administrative Law Judge

May 30, 2008

Les Trobman, General Counsel  
Texas Commission on Environmental Quality  
PO Box 13087  
Austin Texas 78711-3087

Re: SOAH Docket No. 582-07-3473; TCEQ Docket No. 2007-0879-UCR; In Re  
Petition of Flagship Hotel, Ltd., to Review City of Galveston's Denial of a  
Request to Refund Past Due Water Bills

Dear Mr. Trobman:

Attached please find a Request to Answer a Certified Question in the above-referenced case.  
Please schedule this matter at the Commission's earliest convenience.

Sincerely,

*Carol Wood*  
Carol Wood  
Administrative Law Judge

CW/ds  
Enclosures  
cc: Mailing List

CHIEF CLERKS OFFICE

2008 MAY 30 PM 4: 30

TEXAS  
COMMISSION  
ON ENVIRONMENTAL  
QUALITY

**SOAH DOCKET NO. 582-07-3473  
TCEQ DOCKET NO. 2007-0879-UCR**

**PETITION OF FLAGSHIP HOTEL,  
LTD., TO REVIEW CITY OF  
GALVESTON'S DENIAL OF A  
REQUEST TO REFUND PAST DUE  
WATER BILLS**

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**BEFORE THE STATE OFFICE  
OF  
ADMINISTRATIVE HEARINGS**

**REQUEST TO ANSWER A CERTIFIED QUESTION**

**I. INTRODUCTION**

Flagship Hotel, Ltd. (Flagship or Petitioner) has filed a petition with the Texas Commission on Environmental Quality (TCEQ or Commission) to review the City of Galveston's (City) denial of Flagship's request to refund \$215,920.15 that Flagship paid, under protest, to avoid disconnection of its water service. In an amended petition, Flagship has requested that the Commission determine whether it has jurisdiction over this matter. The City argues the Commission has jurisdiction because four appellate courts have concluded that, based on their plain reading of Texas Water Code (Water Code) § 13.042(d), the Commission has exclusive appellate jurisdiction over disputes such as this one. The City also contends, however, that Flagship's petition should be dismissed as untimely. The Commission's Executive Director (ED) asserts Flagship's petition should be dismissed because the Commission in another case has already determined it does not have appellate jurisdiction over appeals of customers of a city-owned utility who reside within the corporate limits. Pursuant to Commission Rule 80.131(b), the Administrative Law Judge (Judge) submits the following certified question to the Commission:

Whether the Commission, pursuant to § 13.042(d), has exclusive appellate jurisdiction to review orders of a governing municipality, including those orders pertaining to the municipality's own water and sewer service customers.

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## II. BACKGROUND

This matter grows out of a dispute between Flagship and the City that spans nearly two decades. In 1963, the City and Nide Corporation (Nide) entered into a lease agreement under which the City was to construct a hotel on the pier and then lease the hotel and the pier to Nide. The hotel was built and, after a series of assignments, Flagship became the lessee in January 1990.

Petitioner asserts that, upon taking over the hotel, Flagship began receiving water service bills from the City that were far in excess of the bills that the previous lessee had received. In January 1991, Flagship's chief engineer sent the City a list of needed repairs, including fixing major leaks in the water lines to the hotel. Petitioner alleges that, because the City "had neither the funds nor the expertise to perform the needed repairs," the then-city manager agreed to adjust Flagship's water service bills to account for overcharges for the water lost as a result of the leaks and for sewage treatment not being used.

In 1996, the City notified Flagship that it did not consider the then-city manager's adjustment to Flagship's water bills either legal or valid. In March 1998, the City sent Flagship a "Final Notice," demanding payment of \$196,291.15. In September 1998, Flagship sued the City for breach of the parties' lease agreement.

On March 21, 2001, the City notified Flagship that water service would be disconnected in 24 hours if Flagship did not pay the delinquent bill. On March 22, 2001, Flagship amended its lawsuit against the City, seeking a temporary injunction restraining the City from disconnecting water service. The district court in Galveston County granted Flagship's petition and enjoined the City from disconnecting water service. The City appealed.

On March 14, 2002, the First Court of Appeals in Houston, Texas, held that the district court did not have jurisdiction to enter an order enjoining the City from disconnecting the hotel's water service and that exclusive appellate jurisdiction over the City's final disposition of this

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dispute lay with the Commission.<sup>1</sup> On March 15, 2002, the City issued another 24-hour disconnection notice and demanded Flagship pay \$215,920.15. On March 18, 2002, Flagship went to TCEQ and filed a request for an emergency order enjoining the City from ceasing water service, pending resolution of the dispute. Petitioner alleges that TCEQ staff informed Flagship the Commission did not have jurisdiction over the matter. Flagship paid the City \$215,920.15, under protest.

On March 27, 2002, the Galveston County district court ruled on competing motions for summary judgment in the lawsuit between Flagship and the City over the lease term and interpretation of the repair obligations under the lease. The court, citing the First Court of Appeals' decision, held it did not have jurisdiction to hear the dispute over the adjustment of Flagship's water bills.

In April 2002, Flagship requested the City refund the \$215,920.15 that Flagship had paid under protest. The City denied Flagship's request. On October 23, 2002, Flagship filed with the Commission a petition for review of the City's denial of Flagship's application for refund of the \$215,920.15.

In October 2003, the Texarkana Court of Appeals (Sixth Court) affirmed the district court's holding that it had no jurisdiction over the dispute between Flagship and the City to adjust Flagship's water bills.<sup>2</sup> The Sixth Court of Appeals found persuasive the reasoning of the First Court of Appeals in *Flagship I* and held that the Water Code granted the Commission exclusive appellate jurisdiction over the dispute.

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<sup>1</sup> *City of Galveston v. Flagship Hotel, Ltd.*, 73 S.W.3d 422, 427 (Tex. App. - Houston [1<sup>st</sup> Dist.] 2002, pet. denied), hereinafter *Flagship I*.

<sup>2</sup> *Flagship Hotel, Ltd. v. City of Galveston*, 117 S.W. 3d 552 (Tex. App. - Texarkana 2003, pet. denied), hereinafter *Flagship II*.

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In July 2004, Flagship filed for Chapter 11 bankruptcy protection. In July 2005, Flagship filed an adversarial proceeding in the bankruptcy court, seeking a turnover order for the funds that Flagship had paid to the City to avoid disconnection of the hotel's water service. In February 2007, the bankruptcy court abated the adversarial proceeding and ordered Flagship to liquidate its claims against the City "in the appropriate forum" before it could seek a turnover order. On April 4, 2007, Flagship filed its amended petition with the Commission.

### III. APPLICABLE LAW

"Rate" is defined in Section 13.002(17) of the Water Code and means, among other things:

[E]very compensation, tariff, charge, fare. . . demanded, observed, charged, or collected. . . by any retail public utility for any service, product, or commodity. . . and any rules, regulations, practices, or contracts affecting that compensation, tariff, charge, fare. . . .

Section 13.002(23) of the Water Code defines "water and sewer utility," in pertinent part, as follows:

. . . any person, corporation, cooperative corporation, affected county, or any combination of these persons or entities, other than a municipal corporation, water supply or sewer corporation, or a political subdivision of the state, except. . . .

In pertinent part, Section 13.042 of the Water Code, entitled "Jurisdiction of Municipality: Original and Appellate Jurisdiction of Commission," reads as follows:

- (a) [T]he governing body of each municipality has exclusive original jurisdiction over all water and sewer utility rates, operations, and services provided by a water and sewer utility within its corporate limits.
- (b) The governing body of a municipality . . . may elect to have the commission exercise exclusive original jurisdiction over the utility

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rates, operations, and services of utilities, within the incorporated limits of the municipality.

- (c) The governing body of a municipality that surrenders its jurisdiction to the commission may reinstate its jurisdiction by ordinance . . . except that the municipality may not reinstate its jurisdiction during the pendency of a rate proceeding before the commission. . .
- (d) The commission shall have exclusive appellate jurisdiction to review orders or ordinances *of those municipalities as provided in this chapter.*
- (e) The commission shall have exclusive original jurisdiction over water and sewer utility rates, operations, and services not within the incorporated limits of a municipality exercising exclusive original jurisdiction over those rates, operations, and services as provided in this chapter.
- (f) This subchapter does not give the commission power or jurisdiction to regulate or supervise the rates or services of a utility owned and operated by a municipality, directly or through a municipally owned corporation, within the corporate limits or to affect or limit the power, jurisdiction, or duties of a municipality that regulates land and supervises water and sewer utilities within the corporate limits, *except as provided by this code.* (Emphasis added.)

Section 13.043(a), (b), and (c) of the Water Code, entitled "Appellate Jurisdiction," reads as follows:

- (a) Any party to a rate proceeding before the governing body of a municipality may appeal the decision of the governing body to the commission. This subsection does not apply to a municipally owned utility. . . .
- (b) Ratepayers of the following entities may appeal the decision of the governing body of the entity affecting their water, drainage, or sewer rates to the commission:

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- (1) a nonprofit water supply or sewer service corporation. . .
  - (2) a utility under the jurisdiction of a municipality inside the corporate limits of the municipality;
  - (3) a municipally owned utility, *if the ratepayers reside outside the corporate limits of the municipality;*
  - (4) a district or authority. . . that provides water or sewer service to household users; and
  - (5) a utility owned by an affected county. . .
- (c) An appeal under Subsection (b) of this section must be initiated by filing a petition for review with the commission and entity providing service within 90 days after the effective day of the rate change or, if appealing under Subdivision (b)(2) or (5) of this section, within 90 days after the date on which the governing body of the municipality . . . makes a final decision. . . . (Emphasis added.)

#### IV. DISCUSSION

##### A. ED's Position

The ED asserts that the Commission has neither original nor appellate jurisdiction over the rates and services of a municipally owned utility for customers residing within the corporate limits. The ED contends the First Court of Appeals in *Flagship I* "planted the seed of this jurisdictional misconception" when it relied on Water Code § 13.042 as the controlling statute in this matter. The ED argues that the First Court ignored the definition of "water and sewer utility" set forth in Water Code § 13.002(23), quoted above, which explicitly excludes a municipal corporation. The ED asserts that Water Code § 13.042, particularly § 13.042(d), concerns the Commission's jurisdiction over entities, other than the municipality itself, that operate within the corporate limits.

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Citing the Commission's Order in "Victoria Palms Resort, Inc. v. City of Donna,"<sup>3</sup> the ED argues that the Commission has already determined it does not have appellate jurisdiction over appeals of customers of a city-owned utility who reside within the corporate limits. The ED points out that Conclusion of Law No. 24 in that order states the following: "[r]ead in context and considering all of Water Code Chapter 13, Water Code §13.042(d) does not give the Commission appellate jurisdiction to review the rates, operations, or services of a municipality when it acts as a municipally owned utility because such a municipality, by statutory definition, is not a "water or sewer service utility." The ED contends that the appropriate location to find the grants of appellate jurisdiction to the Commission is in Water Code §13.043(a) and (b). In summary, the ED asserts that, "[b]ecause the Commission has already decided that the *Flagship* cases do not give it jurisdiction over in-city customers' appeals from city decisions on a rate of a municipally owned utility, and because the statutes make it abundantly clear that the *Flagship* Texas cases were decided incorrectly," this matter should be dismissed on the grounds that the Commission does not have jurisdiction.

#### **B. Flagship's Position**

Flagship argues the Commission has no jurisdiction over this matter because Water Code § 13.043 expressly excludes a city-owned utility from TCEQ's jurisdiction for rate disputes. Flagship points out that § 13.043(a) specifically excludes municipally owned utilities and § 13.043(b) only applies to a municipally owned utility when the ratepayers reside outside the municipality's corporate limits. Because this matter involves a municipally owned utility whose ratepayer (Flagship) resides within the corporate limits, Flagship asserts that neither § 13.043(a) nor §13.043(b) gives the Commission appellate jurisdiction over this case.

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<sup>3</sup> "Petition of Victoria Palms Resort," TCEQ Docket No. 2003-0697-UCR, issued May 14, 2004, hereinafter "Victoria Palms." (ED Ex. 4.)

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Furthermore, Flagship contends the Sixth Court's opinion in *Flagship II* is "clearly erroneous" and thus the law of the case doctrine does not preclude the Commission from finding it does not have jurisdiction. Contrary to the holding in *Flagship II*, Flagship asserts that "those municipalities" in Water Code § 13.042(d) pertain to the limited set of municipalities referred to in the previous subsections of § 13.042; therefore, it is "completely and unambiguously clear" that the Legislature did not intend to give the Commission appellate jurisdiction over municipally owned utilities. Also, Flagship asserts that neither *Flagship I* nor *Flagship II* was appealed to the Travis County District Court or the Austin Court of Appeals (Third Court) and the Commission was not a party to those appeals. For those reasons, Flagship argues the clearly erroneous decisions in *Flagship I* and *Flagship II* do not constrain the Commission from finding it has no jurisdiction over this matter.

### C. City's Position

The City asserts that both appellate courts considering the issue have found that the Commission has exclusive appellate jurisdiction over this dispute and that those decisions establish the law of the case and cannot be disregarded.<sup>4</sup> Additionally, the City notes that all other appellate courts examining the issue (including the one that considered "Victoria Palms" cited by the ED) are in agreement that the Commission has exclusive appellate jurisdiction over the orders and ordinances of a municipality concerning water service disputes.<sup>5</sup> Thus, the City argues, four appellate courts have concluded, based on their plain reading of the statute, that the Commission, pursuant to Water Code § 13.042(d), has exclusive appellate jurisdiction over disputes such as this one. Furthermore, the City asserts that, if the wording of the statute leaves room for improvement so

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<sup>4</sup> *Flagship I* and *Flagship II*.

<sup>5</sup> *City of Donna v. Victoria*, 2005 WL 1831593 (Tex. App. - Corpus Christi 2005, pet. denied) (unpublished), hereinafter *City of Donna*; *City of Willow Park v. Squaw Creek Downs*, 166 S.W.3d 336 (Tex. App. - Fort Worth 2005, no pet.), hereinafter *City of Willow Park*.

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that it reads as argued by the ED, then the Texas Legislature must address the matter. The City contends, however, that the present language of the Water Code is sufficiently clear for four appellate courts to have determined that the Commission has exclusive appellate jurisdiction. Citing Water Code § 13.043(c), the City urges the Commission to dismiss Flagship's amended petition as untimely because it was filed more than five years after the disputed water charges were paid.

#### D. Judge's Analysis

The Judge recommends the Commission find that it has exclusive appellate jurisdiction under Water Code § 13.042(d) to review the orders of a governing municipality, including those orders pertaining to the municipality's own water and sewer service customers.

Four appellate courts have concluded that the Commission, pursuant to Water Code § 13.042(d), has exclusive appellate jurisdiction over orders and ordinances of a municipality – including those of a municipality when it acts as a municipally owned utility. Despite arguments to the contrary, the Commission is not free to reach a conclusion different from the appellate courts that have issued opinions regarding this matter. As noted by the City, although the Commission was not a party in either *Flagship I* or *Flagship II*, the other two parties, the City and Flagship, are the same, and those two appellate courts found that the Commission has exclusive appellate jurisdiction to review orders of a municipality.

Furthermore, in *City of Donna*, the Thirteenth Court of Appeals noted that the Commission specifically found in "Victoria Palms" that it had no jurisdiction to review the billing or sewer rate disputes between Victoria Palms and the City of Donna and that Victoria Palms filed a motion for rehearing with the Commission that was overruled. However, after analyzing Chapter 13 of the Water Code, the Thirteenth Court, in effect, disagreed with the Commission and concurred with both the First and Sixth Courts of Appeals' construction of Water Code § 13.042.

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The Thirteenth Court held that the Commission, pursuant to Water Code § 13.042(d), has exclusive appellate jurisdiction to review the orders or ordinances of a municipality. Likewise, the Fort Worth Court of Appeals (Second Court) in *City of Willow Park* construed Water Code § 13.042 and, in agreement with the First Court in *Flagship I*, held that “the water code confers exclusive original jurisdiction over water service disputes to the municipality and exclusive appellate jurisdiction over such disputes to the Commission.”<sup>6</sup>

The ED argues that the Texas Supreme Court (Supreme Court) has not decided this question of law and, therefore, the law of the case doctrine does not apply to this jurisdictional issue. The Judge notes, however, that the Supreme Court denied the petitions for review filed in *Flagship I*, *Flagship II*, and *City of Donna*. As the ED correctly asserts, the opinions in those cases are not the law of the case because the Commission was not a party. Nevertheless, those decisions establish the rule of law and thus are authoritative and precedential. By the notation “denied,” the Supreme Court indicates it is not satisfied that the opinions of the courts of appeals have correctly declared the law in all respects; however, the Supreme Court has determined that the petitions present no error that requires reversal or is of such importance to the jurisprudence of the state as to require correction.<sup>7</sup> If the wording of Water Code § 13.042(d) needs to be revised to read, in no uncertain terms, what the ED argues it does mean, then that is a matter the Texas Legislature must address.

The Third Court has never held that the Commission has exclusive appellate jurisdiction to review the orders of a municipality; however, that is of no moment. Pursuant to the Administrative Procedure Act,<sup>8</sup> a petition initiating judicial review must be filed in a Travis County

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<sup>6</sup> *City of Willow Park* at 340.

<sup>7</sup> TEX. R. APP. P. 56.1(b)(1).

<sup>8</sup> TEX. GOV'T CODE § 2001.176.

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district court and may be transferred to the Third Court. However, there is no guarantee that the case will then be reviewed and decided by the Third Court. Because the Supreme Court equalizes the dockets of the courts of appeals by transferring cases from courts of appeals with "heavy" dockets to courts of appeals with lighter dockets, a case filed with the Third Court might possibly be transferred to another court of appeals.

Regarding the City's argument that Flagship's petition should be dismissed as untimely, the Judge recommends the Commission first answer the certified question. If the Commission determines it has appellate jurisdiction, then an evidentiary hearing concerning the timeliness of Flagship's filing of its petition and whether the Commission's jurisdiction can be invoked would be appropriate.

The Judge requests that the Commission address this certified question in order to determine whether an evidentiary hearing is required to consider Flagship's petition to review the City's denial of Flagship's request to refund the \$215,920.15 that Flagship paid under protest. The Judge further notes that the parties will be expected to comply with the Commission's rules for written briefing related to this certified question, particularly the deadlines set forth in 30 TEX. ADMIN. CODE § 80.131(c).

SIGNED May 30, 2008.

*Carol Wood*

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CAROL WOOD  
ADMINISTRATIVE LAW JUDGE  
STATE OFFICE OF ADMINISTRATIVE HEARINGS

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**STYLE/CASE:** CITY OF GALVESTON

**SOAH DOCKET NUMBER:** 582-07-3473

**REFERRING AGENCY CASE:** 2007-0879-UCR

**STATE OFFICE OF ADMINISTRATIVE  
HEARINGS**

**ADMINISTRATIVE LAW JUDGE  
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THE FLAGSHIP HOTEL, LTD.

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DATE: **05/30/2008**

NUMBER OF PAGES INCLUDING THIS COVER SHEET: **15**

REGARDING: **ORDER NO. 2 SETTING HEARING DATE**

DOCKET NUMBER: **582-07-3473**

**JUDGE CAROL WOOD**

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