TCEQ Docket No. 2008-0831-MIS-U

In The Texas Commission on Environmental Quality

Appeal of the Executive Director's Negative Use Determination
Issued to Freestone Power Generation, LLC
f/k/a Freestone Power Generation, LP
for the Freestone Energy Center
Application No. 07-11966

Reply to Executive Director's and Office of Public Interest Counsel's Responses to Notice of Appeal Filed on Negative Use Determination for Heat Recovery Steam Generator Application

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TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

LOCKE LORD LLP

Elizabeth E. Mack
State Bar No. 12761050
Geoffrey R. Polma
State Bar No. 16105280
2200 Ross Ave., Suite 2200
Dallas, Texas 75201
Telephone: (214) 740-8598
Facsimile: (214)-756-8598
emack@lockelord.com

Counsel for Freestone Power Generation, LLC

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2200 Ross Ave., Suite 2200
Dallas, Texas 75201
Telephone: (214) 740-8598
Facsimile: (214)-756-8598
emack@lockelord.com

Counsel for Freestone Power Generation, LLC

Pursuant to 30 Texas Administrative Code Section 17.25 and in accordance with the August 31, 2012 briefing schedule issued by the General Counsel of the Texas Commission on Environmental Quality (the "**TCEQ**"), Freestone Power Generation, LLC ("**Appellant**"), 717 Texas Ave., Suite 1000, Houston, Texas, 77002, hereby timely files its Reply to the Responses filed by the Executive Director of the TCEQ (the "**ED Response**") and the Office of Public Interest Counsel (the "**OPIC Response**")[1], both of which were filed in response to Appellant's August 1, 2012 Notice of Appeal of the negative use determination issued in connection with application number 07-11966.

Appellant's Notice of Appeal explained why the TCEQ Commissioners should reverse the negative use determinations issued with regard to its heat recovery steam generators ("**HRSGs**") and steam turbines and should remand its application to the Executive Director for a positive use determination; this Reply explains why the ED Response and OPIC Response do not change those conclusions.[2]

I. Summary of Reply

As an initial matter, the ED Response insists that the inclusion of HRSGs on the statutory list of pollution control equipment has no effect beyond allowing for expedited review of the listed equipment, and in particular inclusion on the list does not affect the Executive Director's

[1] Although the Freestone County Appraisal District received the briefing schedule and had the right to file a Response to Appellant's Notice of Appeal, the Appraisal District filed no Response. The Appraisal District evidently did not feel that it had a particularly compelling position.

[2] The ED Response and OPIC Response focused almost exclusively on issues affecting the HRSGs, taking the position that the steam turbines' negative use determination was not timely appealed and cannot now be considered. This Reply accordingly also focuses on the HRSGs, addressing in its concluding section the appeal of the steam turbines.

duty to assess independently whether HRSGs satisfy multiple other statutory criteria to qualify as pollution control equipment. This position—without meaningful textual analysis—blithely disregards the actual words, structure, and logic of the statute, which in plain language establishes a conclusive legislative finding that HRSGs *per se* meet all criteria necessary to qualify as pollution control equipment, and limit the Executive Director's role to evaluating the percentage of positive use. The Executive Director's attempts to delve into other issues is an improper attempt to supersede the statute and disregard the Legislature in order to implement his policy views, and must be disregarded.

After incorrectly assuming that the TCEQ has authority to independently assess whether HRSGs perform a pollution control function, the Responses argue, in essence, that: (i) because HRSGs reduce pollution by avoiding emissions via production process efficiencies, they are automatically and fully barred from any finding of positive use; and (ii) because no environmental law directly states "you must use a HRSG," the HRSGs cannot qualify for positive use. In doing so, the Executive Director again attempts improperly to overlay the actual requirements of the Tax Code with his policy preferences. Multiple, substantial environmental laws and regulations actually *favor* pollution avoidance at the source—the function accomplished by HRSGs—over scrubbing or other pollution removal methodologies embraced by the Executive Director as the sole permissible category of exempt pollution control equipment. Moreover, the Executive Director's insistence on some direct "nexus" establishing that a specific law or rule dictates use of HRSGs, in particular, to control pollution is another failed attempt to push forward an agency policy preference that is contrary to what the law actually requires, namely, a demonstrated impact of HRSGs in meeting pollution control standards.

The Responses also purport to rebut the multiple other procedural and substantive deficiencies identified in the Notice of Appeal: the Executive Director's violation of the Texas Constitution by denying positive use to Appellant while granting it to other identically situated applicants; the Executive Director's failure to adhere to the Tax Code and Administrative Procedures Act's requirements for reversing policy and disqualifying HRSGs from positive use; the Executive Director's improper and unauthorized remand of Appellant's original positive use determination; and the Executive Director's insistence that the negative use determinations regarding Appellant's steam turbines are final and nonappealable. Appellant responds below in detail to each of these points.

Finally, the Executive Director and OPIC saw fit to draft single briefs that lumped Appellant and other so-called "Group 1" applicants together with "Group 2" HRSG owners, despite the facts that the use determination applications were filed at a different times, are in different procedural postures, and are subject to different computational methodologies for computing positive use. The Executive Director dismissed the distinctions by asserting that "the issues surrounding the applications and negative uses determinations are consistent across all of the applications." To the contrary, factors such as application of Tier IV standards to Group 1 applicants versus Tier III standards to Group 2, and distinctions in the application of the Equal and Uniform Taxation Clause to the two sets of applicants, mandate different considerations. The Group 1 applicants—unlike Group 2—were issued positive use determinations that have been in place for years, and as explained in Section II(F) the Executive Director is bound by and cannot now reverse those determinations.

II. Detailed Reply to Response Brief Contentions and Arguments

The analysis below is organized to respond to the specific contentions enumerated in the ED Response, but within that framework also replies to the OPIC Response's substantive contentions. The analysis first explains why the HRSGs qualify factually and legally as exempt pollution control equipment, then turns to the multiple procedural and constitutional flaws in the Executive Director's processes for his abrupt reversal of policy to deny positive use for HRSGs. Even though these issues are discussed second, they are of paramount importance: Appellant's position is that the Executive Director's processes were so fatally flawed as to be void and without effect, and the positive use determination must stand as originally issued, without further reconsideration of the nature or operation of the equipment.

A. The Tax Code Requires that the Executive Director Treat HRSGs as Pollution Control Devices.[3]

(1) The Statutory Presumptions Mandate a Positive Use Determination.

The Texas Legislature expressed its intent that HRSGs be treated as pollution control devices when it amended Section 11.31 of the Tax Code in 2007 to include subsection (k). That subsection requires that TCEQ adopt a list of such devices and mandates that HRSGs be included on that list. *See* TEX. TAX CODE § 11.31(k).

The Legislature's intent is determined by the words that it chose to use in a given statute. *See* TEX. GOV'T CODE § 312.003; *Tex. Dept. of Transp. v. City of Sunset Valley*, 146 S.W.3d 637, 642 (Tex. 2004). The law presumes that the Legislature chose those words "deliberately and

[3] This section of the Reply responds to Section III(A) of the ED Response.

purposefully." *See Tex. Lottery Comm'n v. First State Bank of DeQueen*, 325 S.W.3d 628, 635 (Tex. 2010). And where those words are unambiguous, the statute must be interpreted in a manner consistent with those words unless such an interpretation would lead to absurd results. *See TGS-NOPEC Geophysical Co. v. Combs*, 340 S.W.3d 432, 439 (Tex. 2011). Here, the Legislature "deliberately and purposefully" included HRSGs in its list of items that "must" be treated as "facilities, devices, or methods for the control of air, water, or land pollution ..." TEX. TAX CODE § 11.31(k). The Legislature did so with full knowledge that HRSGs are devices that are necessarily part of the production process and commonly used as power plant components. *See Mass. Indem. and Life Ins. Co. v. Tex. State Bd. of Ins.*, 685 S.W.2d 104, 109 (Tex. App. Austin, 1985—no writ) ("[T]he legislature, in its enactment of a statute regulating a business activity, is presumed to be familiar with the manner in which the business was conducted at the time."). Accordingly, the Legislature's intent could not be more clear—HRSGs must be treated as pollution control devices—and the Executive Director cannot interpret the statute in an alternative manner in order to avoid this unambiguous legislative mandate.

The Executive Director's interpretation—that the listed devices are merely given "expedited review" but must still satisfy criteria applicable to non-listed devices[4]—reads words into the statute that the Legislature did not include. This interpretation is contrary to Texas law,

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[4] The Executive Director asserts:

> The equipment listed in §11.31(k) is not automatically entitled to a positive use determination, but is subject to the same statutory and regulatory eligibility as any other piece of equipment. Those criteria are the equipment must be used wholly or partially for pollution control, the equipment must provide an environmental benefit, and the equipment must be installed to meet or exceed an environmental rule. If any one of these criteria is not met, then the equipment is not entitled to a positive use determination.

ED Response, pgs. 7-8.

which presumes "that the Legislature chooses a statute's language with care, including each word chosen for a purpose, while purposefully omitting words not chosen." *TGS-NOPEC Geophysical Co.*, 340 S.W.3d at 439 (citing *In re M.N.*, 262 S.W.3d 799, 802 (Tex. 2008)). In other words, if the Legislature had wanted Section 11.31(k) to serve such a limited purpose, it would have expressly included language to that effect in the statute. Instead, the Legislature expressly chose to treat listed devices (such as HRSGs) differently from non-listed devices, and the Executive Director must give effect to that intent.

The Executive Director's suggested interpretation is particularly notable for what it lacks: a close examination of the actual language of the statue. Section 11.31(m) states:

> (m) **Notwithstanding the other provisions of this section, if the** facility, **device,** or method for the control of air, water, or land pollution described in an application for an exemption under this section **is a** facility, **device,** or method **included on the list adopted under Subsection (k), the executive director** of the Texas Commission on Environmental Quality, not later than the 30th day after the date of receipt of the information required by Subsections (c)(2) and (3) and without regard to whether the information required by Subsection (c)(1) has been submitted, **shall determine that the** facility, **device,** or method described in the application **is used wholly or partly as a** facility, **device,** or method **for the control of** air, water, or land **pollution** and shall take the actions that are required by Subsection (d) in the event such a determination is made.

TEX. TAX CODE § 11.31(m) (emphasis added). This legislative directive is definitive and unambiguous: the list comprises equipment that the Legislature has conclusively determined meet all criteria to constitute pollution control equipment. The phrase "notwithstanding the other provisions of this section" directly contradicts the Executive Director's position that it must independently evaluate and apply criteria found in other parts of Section 11.31 before a positive use finding may be issued. This plain reading of the statute also readily resolves a supposed

conundrum identified by the Executive Director, *i.e.*, that although Section 11.31(k) merely "provided for an expedited review of applications . . . and exempted applicants from submitting information regarding the anticipated environmental benefit," nonetheless "if environmental benefit information is not submitted; the Executive Director still must make a determination." ED Response, pg. 6. The obvious reason applicants are exempted from submitting information regarding environmental benefit is because inclusion of equipment on the list represents a legislative determination that environmental benefit exists. There is no "precarious situation" because the determination has been taken out of the Executive Director's hands, and the only role assigned to the Executive Director is to consider the percentage of exempt use.[5]

The ED Response also states that "[t]he Legislature cannot extend a tax exemption beyond what is provided in the Constitution," seeming to imply that the Executive Director can disregard the plain reading of Section 11.31(k) as unconstitutional. ED Response, pg. 6. He cannot. The Legislature has by statute created a conclusive presumption that HRSGs are property used, constructed, installed, or acquired to meet or exceed an environmental rule. The Executive

[5] The TCEQ implemented the Section 11.31(k) equipment list by promulgating 30 T.A.C. § 17.17(b). During the TCEQ Agenda Meeting for January 16, 2008, discussing final adoption of the rule (the audio tapes of which are in TCEQ's possession), Commissioner Shaw made several statements which seemed to recognize that the legislative intent in Section 11.31(k) was to identify equipment that the Legislature had determined *per se* qualified as pollution control equipment:

> Commissioner Shaw: My reading of 3732 didn't leave any indication to me that there was a stipulation that was changing the eligibility of the equipment – it was eligible for the tax abatement prior to that, if it were proved up before the commission following 3732. It was just an expedited process that identified certain pieces of equipment that no longer had to be proved up but were automatically accepted as eligible for the tax abatement. . . .
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> * * *
>
> Commissioner Shaw: . . .[T]he legislature actually directed us that these items were previously eligible, they didn't add any new eligibility criteria, and so in effect I see this as the legislature indicating to us: those items, if we had in the past failed to grant them the status, that they disagreed with that. . . . . They should be eligible for tax abatement.

Director has no authority to disregard this statutory presumption based on his opinion as to whether the Legislature has exceeded its constitutional authority in creating the presumption. *See, e.g., Tex. State Bd. of Pharm. v. Walgreen Tex.*, 520 S.W.2d 845 (Tex. Civ. App.—Austin 1975, writ ref'd n.r.e.) ("Administrative agencies have no power to determine the constitutionality of statutes."); *Mitz v. Tex. State Bd. of Vet. Examiners*, 278 S.W.3d 17 (Tex. App.—Austin 2008, pet dism'd) (same).

Perhaps recognizing this inconsistency between its own interpretation and the Legislature's plain intent, the Executive Director attempts to invoke the doctrine of "legislative acceptance"—arguing that, whatever the Legislature's original intent was, it has now conformed to the Executive Director's interpretation by leaving the law unchanged during the 2009 amendment process. In other words, the Executive Director wants to capitalize on his misinterpretation of the statute. However, the doctrine of legislative acceptance does not apply under these circumstances for several reasons.

First, the doctrine cannot be invoked when the original statute is unambiguous or not of "doubtful meaning," as is the case with Section 11.31(k) and (m). *See Fleming Foods of Tex., Inc. v. Rylander*, 6 S.W.3d 278, 282 (Tex. 1999). Likewise, the doctrine does not apply when the agency's interpretation conflicts with the plain language of the statute or is otherwise inconsistent or unreasonable. *See id.*

Moreover, even if the statute at issue were ambiguous and the Executive Director's interpretation reasonable, that interpretation has not been expressed in such a way that is sufficient for the Executive Director now to invoke the doctrine of legislative acceptance. In the ED Response, the Executive Director points to a "flowchart" and a "preamble" as the sources of its

public articulation about how Section 11.31(k) is to be interpreted, but the legislative acceptance doctrine should only be applied to agency interpretations expressed in "promulgated rules," not informal policies. *See Tex. Citrus Exchange v. Sharp*, 955 S.W.2d 164, 171 (Tex. App.–Austin 1997, no pet.). Further, the agency cannot have "equivocated" on the interpretation, as the Executive Director has done with respect to Section 11.31(k). *See Grocers Supply Co., Inc. v. Sharp*, 978 S.W.2d 638, 644 (Tex. App.–Austin 1998, pet. denied). Rather, the interpretation must be "longstanding, uniform, and clear," and the agency must have "consistently" applied that interpretation to its decisions. *See Reynolds Metals Co. v. Combs*, No. 03-07-00709-CV, 2009 WL 961615, at *3 (Tex. App.—Austin Apr. 8, 2009, pet. denied) (citing *Humble Oil & Refining Co. v. Calvert*, 414 S.W.2d 172, 180 (Tex. 1967)).

In summary, Sections 11.31(k) and (m) of the Tax Code mandate that the Executive Director "shall determine" that a HRSG "is used wholly or partly as a . . . device . . . for the control of . . . pollution." Disregarding the statute, the Executive Director has decided that HRSGs *per se* do not control pollution. The Executive Director has neither authority nor discretion to reach this conclusion, and accordingly the negative use determination must be reversed.

(2) *Mont Belvieu* Does not Affect the HRSGs.

The ED Response and OPIC Response both emphasize the recent case of *Mont Belvieu Caverns, LLC v. Tex. Comm'n. on Envtl. Quality*, No. 03-11-00442-CV, 2012 WL 3155763 (Tex. App.—Austin Aug. 3, 2012). However, the issue actually decided in that case has little relevance to the HRSG negative use determination that is the subject to the current appeal. *Mont Belvieu* stated:

> [W]hen asserting its exemption claim before TCEQ, Mont Belvieu **opted to stand or fall based on a claimed entitlement to a 100% positive use determination for its North Storage brine-pond system—an all-or-nothing claim that the system is wholly pollution-control property**—and in particular a Tier I determination based on category S-20 of the relevant listing [in 30 T.A.C. § 17.14] of predetermined pollution-control property. Consequently, the merits of Mont Belvieu's underlying judicial-review claim turn on whether TCEQ acted arbitrarily or capriciously in determining that the brine-pond system was not in category S-20 of that listing and thereby failed to qualify for a Tier I determination.

Id. at *10 (emphasis added). Thus, Mont Belvieu filed a Tier I application claiming a 100% exemption based on the assumption that the equipment at issue was on the list of pollution control equipment promulgated under Section 11.31(k) of the Tax Code; the Executive Director determined that the equipment was not, in fact, on the list; and the Executive Director determined that some unspecified percentage of the equipment was not pollution control equipment, disqualifying Mont Belvieu from its "all or nothing" Tier I claim. In comparison, Appellant's facts and the applicable law are very different. First, the Executive Director concedes that Appellant's HRSGs are found in Section 11.31(k) of the Tax Code and are on the list of equipment promulgated at 30 T.A.C. § 17.17, and therefore the HRSGs—unlike Mont Belvieu's equipment—are entitled to the favorable consequences of inclusion on the list. Second, Appellant's use determination for the HRSGs was a Tier IV application, so even if there is a finding of some non-pollution control use, Appellant is not disqualified from a positive use determination. As a result, the analysis and holding in *Mont Belvieu* have no bearing on the HRSGs' qualification as pollution control equipment.

B. Alternatively, Appellant Qualifies for a Positive Use Determination.[6]

(1) All Statutory and Regulatory Requirements To Qualify for a Positive Use Determination Have been Satisfied.

[6] This section of the Reply responds to Sections III(B) through III(E) of the ED Response.

The Executive Director would have the Commissioners believe that even though the Texas Legislature specifically called out HRSGs for tax exemption, HRSGs do not qualify for the exemption because, according to him, they do not provide an environmental benefit and they do not meet the requirement that the "property is used, constructed, installed, or acquired to meet or exceed an environmental rule." ED Response, pg. 10. As a threshold matter, the analysis in the preceding section of this Reply establishes that by statute the Legislature has already made a specific, binding determination that HRSGs meet these criteria. Assuming without conceding that the Executive Director can independently evaluate these criteria, the Executive Director's strained analysis defies both the facts and the law, and breezes right past the uses and benefits of HRSGs—realities that are so significant that they led the Executive Director to issue 100% positive use determinations for this facility just a few years ago, in which he specifically stated that "[t]his equipment is considered to be pollution control equipment and was installed to meet or exceed federal or state regulations." Freestone Energy Center, Tracking No. 07-11966, 100% Positive Use Determination, dated 05/01/08.

The Executive Director's incorrect conclusions can be traced to several flawed premises, each of which he carefully crafted to give the impression that despite the Legislative proclamation that HRSGs are pollution control equipment, HRSGs have no value whatsoever in controlling pollution. However, the Executive Director's premises cannot stand up to meaningful scrutiny. Examples of the Executive Director's fundamental mistakes are:

- According to the Executive Director, HRSGs don't reduce air pollution, despite the clear science to the contrary: HRSGs reduce fuel use, which in turn reduces production of NOx, which is a major air pollutant in the United States.

- According to the Executive Director, HRSGs remove heat, and heat is not regulated, flatly ignoring that both Texas and federal regulations expressly target heat input. Heat is very clearly regulated, and it is regulated to reduce the amount of NOx produced, in other words—to reduce pollution.

- According to the Executive Director, because pollutants enter and leave a HRSG, a HRSG cannot be pollution control equipment, sidestepping that a HRSG is not intended to be a scrubber; instead, it controls pollution in a different manner—it reduces the amount of fuel (and therefore emissions) used to generate electricity. Whether the argument is intended to be misleading or whether the Executive Director is simply misinformed, any argument about pollutants entering and leaving a HRSG simply misses the point of what a HRSG actually does.

- According to the Executive Director, HRSGs aren't installed wholly or partly to meet or exceed a rule, despite the facts that: (i) federal and state regulations restrict the rate of NOx that can be emitted into the atmosphere based on the amount of fuel burned; and (ii) HRSGs are installed to reduce the amount of fuel burned (and the amount of NOx emitted).

- According to the Executive Director, emission avoidance isn't an environmental benefit, despite the express policy of both Texas and federal law that "pollution should be prevented or reduced at the source whenever feasible." 42 U.S.C. § 13101(b). Emission avoidance is the overarching theme of pollution control in the United States and in Texas.

The Executive Director concedes that if Appellant meets all the statutory and regulatory requirements, it qualifies for a positive use determination. ED Response, pg. 7 n. 28. Here, the Appellant meets all requirements, notwithstanding the Executive Director's attempts to divert the focus of the discussion away from the salient elements. As a consequence, the Executive Director's negative use determination must be reversed.

(2) Contrary to the Executive Director's Arguments, Emission Avoidance is Pollution Control.

The Executive Director's entire argument dismissing HRSGs as a pollution control device is built on the incorrect premise that emission avoidance is not pollution control. ED Response, pg. 8. As a subset of that premise, the Executive Director would have the Commissioners believe that the tax exemption is reserved only for equipment that is considered an add-on pollution control device. Notably, the Executive Director does not cite any authority for this unreasonable proposition. To the contrary, the Tax Code provides an exemption for any equipment that is used for the "prevention, monitoring, control, or reduction of air, water, or land pollution." TEX. TAX CODE § 11.31(b). The plain language of the Tax Code imposes no requirement that the equipment be classified as a "traditional" pollution device. *See State v. Mauritz-Wells Co.*, 175 S.W.2d 238, 241 (Tex. 1943); *see also USA Waste Servs. of Houston, Inc. v. Strayhorn*, 150 S.W.3d 491, 494 (Tex. App.–Austin 2004, pet. denied) ("We read every word, phrase, and expression in a statute as if it were deliberately chosen, and presume the words excluded from the statute are done so purposefully."). Therefore, the Commissioners must read the Tax Code as it is written, not how the Executive Director wishes it had been written.

Equally important, there is no technical distinction in benefit between a device that scrubs and a device that prevents pollution at the source. Both devices boast pollution control benefit. Because a HRSG prevents pollution at the source by reducing the amount of fuel used to generate heat, it is of no consequence that the same amount of contaminants enter and leave a HRSG. In fact, given that it is a different type of pollution control device altogether (where the pollution control benefits occur as a result of capturing waste heat entering the HRSG), it is fundamentally misguided to proclaim that HRSGs are not pollution control equipment on the basis of the amount of air contaminants entering and leaving the HRSG. And the Executive Director's focus on air contaminants in/out, instead of the real pollution benefits, is directly at odds with Texas and federal policy favoring pollution prevention over add-on devices. *See* 42 U.S.C. § 7401(c); 42 U.S.C. § 13101(b); *see also* TEX. HEALTH & SAFETY CODE ch. 386. The HRSG is no less entitled to an exemption than an "add-on" device.

As the Tax Code is written, the equipment qualifies for the exemption because it is used in whole or in part for pollution control, pollution prevention, pollution monitoring, or the reduction of pollution. HRSGs provide a significant pollution benefit by reducing the amount of pollutants emitted in the first place. In fact, even the Executive Director does not contest that HRSGs limit the amount of pollution generated when producing electricity. The Executive Director's attempt to restrict the tax exemption to the "traditional" concept of pollution control equipment is contrary to the Tax Code and is an injustice to the benefits a HRSG provides.

The Executive Director implies that there is something less worthy about emission avoidance, and as a consequence, it should not be entitled to the exemption. However, both Texas and federal law identify pollution prevention as the preferred pollution control option. Under

federal law, the Pollution Prevention Act states that it is the policy of the United States that "pollution should be prevented or reduced at the source whenever feasible." 42 U.S.C. § 13101(b).[7] Pollution prevention is the preferred method for dealing with pollution, followed by recycling, treated in an environmentally safe manner, and finally disposal or release into the environment. *See id.* This same preference is found in the federal Clean Air Act, which provides that pollution prevention is of primary importance in reducing emissions. *See* 42 U.S.C. § 7401(c). Federal law strongly identifies pollution prevention as being more effective in controlling pollution then add-on controls.

Pollution prevention is also a strategy employed under Texas law. The Texas Emissions Reduction Plan is specifically designed to reduce emissions from polluting vehicles and equipment. *See* TEX. HEALTH & SAFETY CODE ch. 386.[8] This statute targets older, higher polluting vehicles and equipment to reduce contaminants released into the air. HRSGs also reduce the amount of pollution produced at the source. The Executive Director sidesteps TCEQ's own directives when he discounts the value and environmental benefit of pollution prevention, and the HRSGs.

Wholesale ignoring Texas policy (as well as the Tax Code), the Executive Director sweepingly pushes his position one step further by asserting that he has "never recognized emissions avoidance as pollution control." ED Response, pg. 8. He is mistaken. Appellant's facility, the five other facilities characterized in the ED Response as "Group 1," and multiple other nonappealed HRSG applications have had 100% positive use determinations where the Executive

[7] *See also id.* § 13101(a)(4)(source reduction is fundamentally different and more desirable than waste management and pollution control).

[8] Texas also recognizes the benefits of pollution prevention under the Solid Waste Disposal Act. *See* TEX. HEALTH & SAFETY CODE § 361.0215.

Director specifically found that "[t]he use of this property at a combined cycle plant, as opposed to having a simple cycle plant, provides an environmental benefit of *reduced* NOx emissions at the site." Freestone Energy Center, Tracking No. 07-11966, 100% Positive Use Determination, dated 05/01/08 (emphasis added). The Executive Director has found multiple times that emission avoidance through the use of HRSGs provides an environmental benefit.

Quite simply, emission avoidance is a pollution control strategy and one that is favored under the law. The HRSGs are eligible for the tax exemption.

(3) HRSGs Provide an Unmistakable Pollution Control/Environmental Benefit.

The Executive Director claims that because HRSGs are also used in production, they cannot possibly have a pollution or environmental benefit. The Tax Code, by its plain language, expects that some equipment will have both a production and pollution benefit by providing that the equipment must be used, constructed, acquired or installed "wholly or partly" to meet or exceed rules or regulations. TEX. TAX CODE 11.31(b). Indeed, production benefits and pollution benefits are not mutually exclusive concepts. The pollution benefit from HRSGs is not dependent upon how much waste heat is being converted into additional electricity.[9] Rather, the 100% positive use determination is appropriate as a result of the amount of pollution prevented at the source, and preventing pollution at the source—pollution reduction—is the policy of both Texas and federal law. *See* 42 U.S.C. § 7401(c) (primary importance of the rules under the Clean Air Act is pollution prevention); 42 U.S.C. § 13101(b) (it is the policy of the United States that pollution should be prevented or reduced at the source whenever feasible); *see also* TEX. HEALTH & SAFETY CODE ch. 386.

[9] For example, increasing the production benefit does not reduce the pollution benefit and vice versa.

The Executive Director makes several other scattershot arguments to try to support his technically and legally unjustifiable policy reversal. He sinks deeply into technically unsupportable territory when he claims that the exemption is not warranted because "heat is not a regulated pollutant." ED Response, pg. 8. Both federal and Texas regulations specifically target "heat input." *See, e.g.*, 40 C.F.R. pt. 60, subpt. KKKK (New Source Performance Standards or NSPS); 30 T.A.C. § 116.111(a)(2)(D) (incorporating by reference the EPA's NSPS set forth in 40 C.F.R. pt. 60). Heat input is regulated to reduce overall emissions, especially NOx. Thus, while heat is not a regulated pollutant (an immaterial point), heat is regulated to reduce the amount of NOx produced.

The Executive Director also complains without support that the facility's quantification of the amount of pollution benefit provided by HRSGs is wrong because it compares the pollution benefit of a combined-cycle facility to a simple-cycle facility. ED Response, pg. 8. Far from wrong, such a comparison is entirely appropriate because if a HRSG is removed from a combined-cycle facility, the facility becomes a simple-cycle system, which emits more pollutants for the same amount of electricity produced. *See* Exhibit A, Declaration of Patrick Blanchard, ¶ 6. In a word, the Executive Director doesn't like the quantification because it doesn't support his argument. [10]

Notably, in all his apparent vexation about HRSGs having no "environmental benefit," the Executive Director does not contest that the use of HRSGs at Appellant's facility results in a

[10] The TCEQ has also developed a standard permit for electric generating units that regulates NOx emissions based upon the pounds of pollutants emitted per megawatt hour. This standard permit imposes significantly less abatement equipment for a combined-cycle unit as compared to a simple-cycle unit. The TCEQ's permitting scheme explicitly recognizes the pollution reducing benefit of a combined-cycle facility as compared to a simple-cycle facility.

reduction in NOx emissions of 48.6%. *See* Freestone Energy Center Application, dated 03/25/08. One of the contaminants responsible for ozone formation is NOx. HRSGs provide substantial environmental benefits by reducing the amount of NOx emitted, which in turn reduces the amount of ozone produced.

None of the Executive Director's arguments defeats the fact that Appellant has met the statutory and regulatory requirements for the tax exemption. The Executive Director's negative use determination should be reversed and Appellant's application should be remanded for a positive use determination.

(4) HRSGs Meet or Exceed an Environmental Rule.

The Executive Director incorrectly asserts that there is no rule that requires the use of HRSGs:

> No Applicant has cited to a rule that requires the installation of the HRSG. There is no rule that explicitly requires the installation of a HRSG nor is there a generally applicable efficiency standard that could only be met by installation of a HRSG.

ED Response, pg. 11. Preliminarily, it is important to note that the Executive Director has misstated the requirement of the Tax Code. The Tax Code requires that the environmental rule apply to the "prevention, monitoring, control, or reduction of air, water, or land pollution." TEX. TAX CODE §11.31(b). Nothing in the Tax Code requires Appellant to identify a specific rule saying "HRSGs must be used." Instead, the device must be part of prevention, monitoring, control, or reduction of pollution.

In addition to being unsupported by the statute, the Executive Director's purported standard makes little policy sense, as it would preclude a positive use finding for, *e.g.*, new add-on technologies that unquestionably and dramatically reduce pollutants merely because such technologies or devices are not specifically named in law or regulations. Moreover, the purported standard contradicts the TCEQ's own established policy. Two typical add-on pollution control devices used at electric generating facilities to reduce NOx emissions are: (i) low-NOx combustors; and (ii) selective catalytic reduction ("**SCR**"). Low-NOx combustors are a combustion control designed to minimize combustion temperatures to inhibit NOx formation when the fuel is fired in the combustion chamber. SCR is a post-combustion technology that uses ammonia as a reagent to reduce NOx to molecular nitrogen and water in the presence of a catalyst. There is no regulatory requirement that these pollution control devices be used to control NOx. However, the TCEQ's published guidance—*i.e.*, TCEQ Combustion Sources, Current Best Available Control Technology ("**BACT**") Requirements—indicates that these devices satisfy BACT's requirements. As a consequence, they are entitled to a positive use determination even though they are not specifically named in the BACT rule.

Here, the facility is required to reduce pollutants under the: (i) Clean Air Interstate Rule ("CAIR"); and (ii) BACT.[11] Both of these rules are for the prevention and control of pollution. The CAIR rules were implemented by EPA to reduce the interstate transport of pollutants, especially NOx and sulfur dioxide.[12] *See* 72 Fed. Reg. 251562 (2005). TCEQ's rules directly rely

[11] At this time, the Freestone facility is not subject to the most stringent NSPS applicable to stationary combustion turbines, located at 40 C.F.R. pt. 60, subpt. KKKK. NSPS KKKK directly correlates pollution prevention with the amount of electricity produced by the facility. Nevertheless, the Freestone facility is already compliant with this standard and providing a pollution reduction benefit above and beyond its current applicable requirements.

[12] The Texas Legislature directed the TCEQ to develop rules to implement the CAIR program in Texas

upon increased fuel efficiency to implement CAIR in Texas. *See* 30 T.A.C. § 101.506. The increased fuel efficiency resulting from the use of a HRSG meets or exceeds TCEQ's CAIR rules. *See* Exhibit A, Declaration of Patrick Blanchard, ¶¶ 8-9.

Ignoring the regulatory definition of BACT, the Executive Director claims that BACT is an "emission limit" and "a HRSG does not help meet such a limit."[13] ED Response, pg. 11. Indeed, the TCEQ's own definition of BACT provides that BACT is the reduction in total emissions that can be achieved through the use of *either*: (i) add-on pollution control equipment; or (ii) *production processes*, systems, methods, or work practices. *See* 30 T.A.C. § 116.10(1) (emphasis added). As the rule clearly states, BACT can be an add-on pollution control device OR a "production process." As a consequence, a HRSG is not excluded from consideration as satisfying BACT simply because it is part of the production process. In this instance, the BACT requirement is surpassed through the use of a HRSG. The facility's BACT requirement is a restriction on the amount of NOx that can be emitted into the atmosphere per megawatt hour of electricity produced. A HRSG reduces the amount of fuel used to produce electricity. Reduced fuel use corresponds to fewer total pollutants, including NOx, being emitted from the facility. This increased fuel efficiency goes above and beyond TCEQ's BACT requirement. *See* Exhibit A, Declaration of Patrick Blanchard, ¶ 10.

The Executive Director also makes a generalized attack to the applicable regulatory requirements by claiming there is an insufficient nexus between pollution control and the various environmental rules cited by Appellant and the other applicants involved in the current appeal.

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based upon EPA's program. *See* TEX. HEALTH & SAFETY CODE § 382.0173.

[13] The Executive Director also reiterates his mistaken emphasis on the need for a specifically mandated use of a HRSG, stating "BACT does not require the installation of HRSGs."

ED Response, pg. 11. Again, to reach this conclusion, the Executive Director, without legal authority, restricts the applicability of the tax exemption to traditional pollution control equipment. The tax exemption also applies to equipment that prevents pollution in the first place. *See* TEX. TAX CODE § 11.31(b). Nothing mandates that only scrubbers are entitled to the exemption. The applicable rules establish restrictions on the amount of emissions based upon fuel use. Reducing fuel use results in fewer emissions needing to be addressed through add-on controls. The Executive Director deliberately fails to acknowledge the pollution prevention function of these rules.

The Executive Director's conclusion that the HRSG is not "used, constructed, acquired, or installed wholly or partly to meet or exceed rules or regulations. . . for the prevention, monitoring, control, or reduction of air, water, or land pollution" cannot stand up to the facts or law. The applications submitted by Appellant show that the installation and operation of the HRSGs meet all of the statutory requirements and qualify for an exemption under Section 11.31 of the Tax Code as set forth in its applications submitted in 2008.

C. The Tax Code Prohibited the General Counsel from Remanding the Group 1 Applications, Including Applicant's Application.[14]

Section 11.31(e) of the Texas Tax Code provides, in relevant part, that after an appeal of the Executive Director's determination is filed:

> **[t]he commission shall consider the appeal** at the next regularly scheduled meeting of the commission for which adequate notice may be given. The person seeking the determination and the chief appraiser may testify at the meeting. **The commission may remand the matter to the executive director for a new determination or deny the appeal and affirm the executive director's**

[14] This section of the Reply responds to Section III(F) of the ED Response.

> **determination.** On issuance of a new determination, the executive director shall issue a letter to the person seeking the determination and provide a copy to the chief appraiser as provided by Subsection (d).

TEX. TAX CODE § 11.31(e) (emphasis added). Thus, the plain language of the statute makes clear that only the Commission itself—and not the General Counsel—may remand a matter to the Executive Director for a new determination. The Legislature could have expressly provided the General Counsel or another TCEQ employee with the authority to remand a matter, but it did not. The Legislature's choice of language must be given its intended effect, as "[i]t is a settled rule that the express mention or enumeration of one person, thing, consequence, or class is equivalent to an express exclusion of all others." *Mauritz-Wells Co.*, 175 S.W.2d at 241.[15]

Further, in the sentence immediately following the reference to the Commission's authority to remand a matter, the Legislature expressly provides that "the **executive director** shall issue a letter to the person seeking the determination," demonstrating that when the Legislature desires to place the authority to act in a specific TCEQ employee, it can and will do so through express language. TEX. TAX CODE § 11.31(e) (emphasis added).[16]

The Executive Director argues in the ED Response that Section 5.110(d) of the Texas Water Code provides the Commission with sufficient authority to delegate the power to remand a determination under Section 11.31 to the General Counsel. ED Response, pg. 12. Section 5.110(d) grants the Commission general authority to delegate duties and powers to the General Counsel, providing:

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[15] *See also USA Waste Servs. of Houston, Inc.*, 150 S.W.3d at 494 ("We read every word, phrase, and expression in a statute as if it were deliberately chosen, and presume the words excluded from the statute are done so purposefully.").

[16] *See also FM Properties Operating Co. v. City of Austin*, 22 S.W.3d 868, 884-85 (Tex. 2000) (holding that when the legislature expressly provides a particular right elsewhere in the code, a statute's omission of similar language must be given its intended effect).

> [t]he general counsel shall perform the duties and may exercise the powers specifically authorized by this code or delegated to the general counsel by the commission.

TEX. WATER CODE § 5.110(d). However, this general grant of delegation authority is not sufficient to overcome the plain language of Section 11.31(e).

First, to the extent that there is a conflict between general authority of the Commission to delegate duties to the General Counsel under Section 5.110(d) of the Water Code and the specific language of Section 11.31(e) of the Tax Code providing that the Commission alone may remand a determination, the more specific language must be given effect. It is a well-established rule of statutory construction that specific provisions prevail over more general ones. *See* TEX. GOV'T CODE § 311.026(b).[17]

Second, the general authority of a governmental body to delegate duties and powers to its employees is not unlimited. Even when a statute—like Section 5.110(d) of the Water Code—authorizes a governmental body to delegate functions to its employees, the governmental body may not delegate any function that is specifically entrusted to it by the Legislature. As the Austin Court of Appeals explains:

> [a] commission may hire employees to carry out its delegated functions, if such power is provided by statute. Where a statute entrusts specified functions to a commission, the legislature presumably intends that only that commission will exercise the delegated functions. The commission may not subdelegate assigned functions to its employees. To do so would mean that the Commission acted outside of its statutory authority, and its employees' actions would be invalid for want of authority.

[17] *See also Horizon/CMS Healthcare Corporation v. Auld*, 34 S.W.3d 887, 901 (Tex. 2000) (recognizing "the traditional statutory construction principle that the more specific statute controls over the more general").

Schade v. Texas Workers' Compensation Comm'n, 150 S.W.3d 542, 549-49 (Tex. App.–Austin 2004, pet. denied) (internal citations omitted).[18]

Thus, the Commission contravened the plain language of Section 11.31(e) of the Tax Code by giving the General Counsel the authority to remand the determination, and the General Counsel's remand was therefore improper and is invalid for want of authority.

D. The Executive Director Impermissibly Applied the Law in a Retroactive Manner.[19]

(1) Section 17.25(d) Cannot Be Applied Retroactively.

The 2010 amendments to the TCEQ's administrative rules added a new Section 17.25(d), which provides that "[t]he general counsel may remand a matter from the commission agenda to the executive director if the executive director or the public interest counsel requests a remand." 30 T.A.C. § 17.25(d). The General Counsel exercised this new authority to remand Appellant's application, despite the fact that the application was filed prior to the adoption of the amended rules.

An agency rule is presumed to apply prospectively unless expressly made retrospective. *See* TEX. GOV'T CODE § 311.022 ("A statute is presumed to be prospective in its operation unless expressly made retrospective."). Nothing in the 2010 amendments to the TCEQ Rules indicates that any of the changes thereunder were intended to apply retrospectively. Rather, the legislation pursuant to which the 2010 rule amendments were adopted expressly provides that the changes in

[18] *See also Horne Zoological Arena Co. v. City of Dallas*, 45 S.W. 2d 714, 715 (Tex. Civ. App. 1931) (holding that a governmental body cannot "delegate to others the discharge of duties which call for reason or discretion, and which are regarded as a part of the public trust assumed by the members of such board").
[19] This section of the Reply responds to Section III(G) of the ED Response.

law do not apply to applications filed before January 1, 2009. *See* H.B. 3206, 81st Leg., Reg. Sess. (Tex. 2009); H.B. 3544, 81st Leg., Reg. Sess. (Tex. 2009).

In the ED Response, the Executive Director argues that the application of Section 17.25(d) to Appellant's application is not retroactive because the application was remanded after the effective date of the amendments, citing case law for the proposition that a law "is not retroactive merely because it draws on antecedent facts for its operation." *Bd. of Med. Exam'rs v. Nzedu*, 228 S.W.3d 264, 271 (Tex. App.—Austin 2007, pet. denied). In *Nzedu*, however, the court considered the question of whether a statute passed prior to the date that an application for a medical license was filed operated retroactively because it required the Board of Medical Examiners to take into account conduct that occurred prior to the enactment of the statute and the submission of the application. The court found that the "look back" feature of the statute did not make it retroactive, noting specifically that the new statute did *not* apply to applications filed before its effective date. *Id.* at 272. Here, the Executive Director is attempting to apply the new rule to an application filed before its effective date. This application of Section 17.25 to a pre-2010 application is improper, as OPIC explicitly acknowledges in the OPIC Response. *See* OPIC Response, pg. 8 ("Appellant argues that remand of the 2008 Consolidated Appeals by the TCEQ Office of General Counsel under 30 T.A.C. § 17.25(d) was improper. **Remanding the matter under a rule that was not in effect when the Appellant submitted its application—and has no basis in the governing statute—would be improper.**") (emphasis added).

The Executive Director and OPIC attempt to circumvent Appellant's arguments that the remand was improper by asserting that the General Counsel already had the authority to remand the determination pursuant to 30 T.A.C. § 10.4(d), which provides that "[t]he general counsel may

remand a matter from the commission's agenda to the executive director if the executive director or the public interest counsel requests a remand." 30 T.A.C. § 10.4(d). There are two significant problems with this argument.

First, the Executive Director's Request for Remand on the Consolidated Applications stated, "**Pursuant to 30 TAC § 17.25(d)**, the Executive Director of the Texas Commission on Environmental Quality requests that the General Council [*sic*] remand the above listed applications for further processing." (emphasis added). The request therefore makes clear that the Executive Director was exercising his authority pursuant to Section 17.25(d)—not Section 10.4(d). Second, the preamble to the 2010 rule amendments clearly indicates that the addition of Section 17.25(d) was intended to provide new remand authority for the General Counsel and *not* to clarify existing authority, as the Executive Director suggests. *See* 35 Tex. Reg. 10964 ("Adopted § 17.25(d) is added to provide a mechanism for the general counsel to remand appeals back to the executive director without formal action by the commission . . .").

Because retroactive application of Section 17.25(d) to a pre-2010 application is improper and 30 T.A.C. § 10.4(d) does not provide an alternative basis for the remand, the General Counsel was without authority to remand Appellant's application for further processing.

(2) The Elimination of Tier IV Applications Cannot Be Applied Retroactively.

As Appellant argued in its Notice of Appeal, retroactive application of the Tier III formulas added to the TCEQ rules in 2010 to Appellant's application would: (i) contravene the express language of H.B. 3206 and H.B. 3544, which explicitly do not apply to applications filed before January 1, 2009; and (ii) violate the constitutional prohibition against retroactive laws. The

Commission must, therefore, determine Appellant's HSRGs' percentage of exempt use under the pre-2010 Tier IV criteria.

The Executive Director appears to concede this issue. The ED Response acknowledges that "HB 3206 and 3544 do not apply to applications filed prior to January 1, 2009." ED Response, pg. 3. As Appellant submitted its Tier IV use determination application to the Executive Director in March of 2008, the changes made to the formulas pursuant to H.B. 3206 and H.B. 3544—including the elimination of the Tier IV application—do not apply to Appellant's application. The OPIC Response explicitly acknowledges this fact, stating:

> OPIC finds that the rules and statutes in effect when the Appellant submitted its application should be applied. . . . therefore HB 3206 and HB 3544 as well as **the 2012 amendments to Chapter 17 abolishing Tier IV would not apply to this application**.

OPIC Response, pg. 10 (emphasis added).

Therefore, all parties agree that the pre-2010 Tier IV criteria must be applied to Appellant's application. Appellant has demonstrated in both its original Application and its Response to Appeal of the 100% Positive Use Determination, which Appellant incorporated by reference in its Notice of Appeal, that application of Tier IV criteria to Appellant's HRSGs results in a 100% positive use determination.

E. The Executive Director's Negative Use Determination Violates the Texas Constitution's Equal and Uniform Taxation Requirement.[20]

Appellant's Notice of Appeal explained why the Executive Director's negative use determination violated the Texas Constitution's mandate that taxation be equal and uniform. The

[20] This section of the Reply responds to Section III(H) of the ED Response.

ED Response concedes that he has treated two classes of taxpayers differently by issuing 100% positive use determinations with respect to some HRSGs while issuing a 100% negative use determination to Appellant's indistinguishable HRSGs. The ED Response attempts to justify its unequal and non-uniform treatment by characterizing the prior positive use determinations as issued "in error" and "in violation of statutory provisions," observing that the Executive Director made the negative use determination with respect to Appellant's HRSG after that error had been corrected. ED Response, pg. 15.

To support its position, the ED Response relies primarily on *Grocers Supply Co. v. Sharp*, 978 S.W.2d 638 (Tex. App.—Austin 1998, pet. denied). However, *Grocers Supply* considered facts far different from the current appeal, and consequently does not affect the conclusion that a constitutional violation will occur if Appellant is not granted a positive use determination.

Grocers Supply considered the Comptroller's denial of a sales tax refund claim based on the Comptroller's change as of a given date of its policy and interpretation regarding how certain tax rates are computed. The taxpayer alleged a violation of Equal and Uniform Taxation because (i) some taxpayers had already received refunds or the benefit of the favorable rate for pre-policy change years, but (ii) the taxpayer was denied the favorable rate for the same years because its refund claim was processed after the effective date of the change in policy.

Critically, in *Grocers Supply*, the Comptroller's policy change was in direct response to a Texas Supreme Court decision mandating the new policy. *See* 978 S.W.2d at 640, 645. The court characterized the Comptroller's prior, changed policy as an "erroneous interpretation in clear contravention of the legislature's purpose" and in direct conflict with Texas Supreme Court precedent. Therefore, because the policy change "gave the most effect to legislative intent" and the Comptroller's action allowed him "to bring his policy into compliance with the statute," the

uniform application of the policy to all tax issue after a given date was not "irrational or unreasonable." *Id.* at 645. None of these factors applies to the current appeal. At a bare minimum, the inclusion of the HRSGs on the Section 11.31(k) equipment list establishes that TCEQ had ample authority to adopt its longstanding administrative interpretation that the HRSGs qualify for positive use. No case law establishes that HRSGs cannot qualify as pollution control equipment. Thus, the prior HRSG policy that the Executive Director now seeks to change is *not* "erroneous" or "in direct contravention" of the statute and case law, but instead is a valid administrative agency interpretation. This distinction negates the primary basis on which *Grocers Supply* justified the unequal treatment of taxpayers as being constitutional.[21] Accordingly, with respect to the Group 1 taxpayers, who are identically situated to many simultaneous applicants who were granted positive use determinations, no rational basis supports the Executive Director's retroactive differential treatment.

F. The Executive Director Lacked Authority to Change his Position on the Treatment of HRSGs.[22]

(1) Rulemaking Was Necessary to Implement the Change in the Executive Director's Treatment of HRSGs.

[21] The ED Response also suggests that its divergent treatment of identical HRSGs is supported by *First American Title Insurance Co. v. Strayhorn,*169 S.W.3d 298, 306 (Tex.App.—Austin 2005), *aff'd on other grounds sub nom First Am. Title Ins. Co. v. Combs*, 258 S.W.3d 627 (Tex. 2008). However, that case is distinguishable because, first, it concerned differing taxation of foreign vs. domestic insurers, two demonstrably different classes. The current appeal involves indistinguishable HRSGs. Second, the case involved a change in tax computations for 2001 and later years, *see id.* at n. 2, where the Comptroller in 2001 had adopted an administrative rule amendment that supported the change in tax computations. Thus, the case concerned taxpayers being treated equally after an announced policy change—a far cry from the "Group 1" taxpayers, who are treated completely differently from identically situated applicants who submitted applications at the same time as Appellant, long before any attempted policy change.

[22] This section of the Reply responds to Section III(I) of the ED Response.

The Executive Director argues that a formal rulemaking was not necessary to implement the Commission's change in the treatment of HRSG applications, stating that Appellant's negative use determination—along with numerous other simultaneously issued HRSG negative use determinations—was the result of a case-by-case review of each application and that the change in treatment of HRSGs is not a rule of general applicability. The Executive Director's position is undermined by his own ED Response, which states that the Executive Director has changed his interpretation of Section 11.31 as "his understanding has evolved." ED Response, pg. 15.

By his about-face the Executive Director has implemented a new rule of general applicability pursuant to which HRSGs can never qualify for a positive use determination. The Executive Director does not point to any attributes particular to the HRSGs in Appellant's application—or any other application—that render them ineligible for a positive use determination. Furthermore, the Executive Director's decision to issue a single ED Response collectively addressing the many outstanding HRSG determinations demonstrates the lack of any "case-by-case" analysis. Instead, the negative use determination is the result of a new rule defining HRSGs as production equipment that *per se* do not qualify for exemption.

Under the Administrative Procedures Act (the "**APA**") a rule:

(A) means a state agency statement of general applicability that:
  (i) implements, interprets, or prescribes law or policy; or
  (ii) describes the procedure or practice requirements of a state agency;
(B) includes the amendment or repeal of a prior rule; and
(C) does not include a statement regarding only the internal management or organization of a state agency and not affecting private rights or procedures.

TEX. GOV'T CODE § 2001.003(6). A rule must be adopted pursuant to a formal rulemaking under the procedures set forth in the APA, and a rule promulgated without complying with the proper procedures is invalid. *See id.* § 2001.035. An agency's statements of general applicability implementing, interpreting, or prescribing law or policy are therefore invalid unless adopted in compliance with APA procedures.[23]

The Executive Director cites *Texas Mutual Insurance Co. v. Vista Community Medical Center, LLP*, 275 S.W.3d 538 (Tex. App.—Austin 2008, pet. denied), and *Railroad Commission v. WBD Oil & Gas Co.*, 104 S.W.3d 69 (Tex. 2003), in support of his position that the change in treatment of HRSGs is not a rule under the APA. ED Response, pgs. 16-17. Both of those cases are readily distinguishable. In *Texas Mutual*, the court held that a staff report addressing an internal inconsistency regarding the interpretation of an existing rule did not constitute a rule because it was a "statement regarding the agency's internal management that does not affect private rights," it did not change or amend the underlying rule, and it was not a new interpretation of the underlying rule. 275 S.W.3d at 556. The opposite is true in this case: the Executive Director's change in the treatment of HRSGs implements policy, affects the interest of the public, and modifies and/or constitutes a new interpretation of the TCEQ Rules. Just as the Texas Supreme Court held in *El Paso Hospital District v. Texas Health & Human Services Commission*, 247 S.W.3d 709, 714 (Tex. 2008), that a cutoff date for a change in policy affecting all hospitals receiving reimbursement for Medicaid services was a generally applicable statement of policy, the Executive Director's change of position that HRSGs are used for production purposes and can

[23] *See Combs v. Entertainment Publ'ns, Inc.*, 292 S.W.3d 712 (Tex. App.—Austin 2009, no pet.) (holding that the Comptroller's statements in letters were generally applicable and therefore rules under the APA because they indicated "that the Comptroller will uniformly regard brochure-fundraising firms as the sellers and nonprofit entities as the sellers' agents, without regard to the individual factors considered under the Comptroller's previous guidelines").

never receive a positive use determination affects all HRSG facilities and is a generally applicable statement of policy.

In *Railroad Commission v. WBD Oil & Gas Co.*, the Supreme Court held that "field rules" determined by the Railroad Commission were not rules under the meaning of the APA because they are not rules of general applicability. 104 S.W.3d at 79. The Court distinguished field rules "detailing spacing and proration requirements in a specific reservoir and its own peculiar geologic formations" with the Railroad Commission's statewide rules "which govern the entire oil and gas industry for the public good." *Id.* As discussed above, the Executive Director has adopted the position that HRSGs are always used for production and therefore are never entitled to a positive use determination—a rule that appears to apply to all HRSGs and is not dependent on the particular features of the HRSG in question. This rule governs all HRSGs statewide and affects the public good. Thus, unlike the Railroad Commission's field rules, it is a rule of general applicability and therefore subject to the APA.

Finally, the Executive Director violated Section 11.31(l) of the Tax Code by altering his treatment of HRSGs without following the statutorily required rulemaking process for equipment included on the Tax Code Section 11.31(k) list. Section 11.31(l) provides a specific process that the Executive Director must follow in order to remove pollution control equipment from the list of pollution control items. The statute provides:

> The Texas Commission on Environmental Quality **by rule** shall update the list adopted under Subsection (k) at least once every three years. An item may be removed from the list if the commission finds compelling evidence to support the conclusion that the item does not provide pollution control benefits.

TEX. TAX CODE § 11.31(l) (emphasis added). By characterizing HRSGs as solely production equipment, the Executive Director has effectively removed HRSGs from the list of pollution control equipment and therefore updated the list without following the rulemaking process, in violation of Section 11.31(l). Moreover, the statute directs that only "the commission" has the authority "by rule" and based on "compelling evidence" to override the list; here, the Executive Director seeks to accomplish this result by informal, unilateral action.

The Executive Director's elimination of positive use determinations for HRSGs, implemented without a formal rulemaking, violates both the APA and Section 11.31 of the Tax Code. The rule providing that HRSGs are used solely for production and are therefore ineligible for a positive use determinations is accordingly invalid. Appellant's application should be remanded for a positive use determination.

(2) The Commissioners Cannot Disregard the Executive Director's Prior Treatment of HRSGs.

In the course of determining that Appellant's HRSG was initially entitled to a positive use determination, the Executive Director, after due consideration of detailed technical information, made a number of findings, including that the HRSG met or exceeded applicable regulations. The Executive Director now takes the opposite stance, seeking to retract those prior findings and have the Commissioners treat them as null and void. However, the Commissioners cannot simply disregard the Executive Director's prior findings and allow him to change his mind. Rather, the Commissioners must give evidentiary weight to those prior findings, as they constitute statements contrary to the position that the Executive Director is now taking. *See City of El Paso v. Public Utility Comm'n of Texas*, 839 S.W.2d 895, 907 (Tex.App.–Austin 1992), *aff'd in part, rev'd in*

part on other grounds, 883 S.W.2d 179 (Tex. 1994) (finding that "some evidentiary weight" must be given to a "declaration contrary to a party's position on a disputed issue."). *City of El Paso* involved a statement made by a party during an administrative proceeding regarding an issue on which the party took a contrary position in subsequent litigation, making clear that the standard requirements of Texas evidence law apply to statements made in administrative proceedings. *See id.* Accordingly, the Commissioner must factor the Executive Director's prior findings into their decision and cannot treat them as if they never occurred.

G. Appellant Timely Appealed the Negative Use Determinations for its Steam Turbines.[24]

The Executive Director argues that appeal of the negative use determination for the steam turbines is untimely because it was not filed within twenty days of receiving the notice of the use determination. ED Response, pg. 17. There was no reason to appeal the determination in 2008 because Appellant had been granted 100% Positive Use Determination for the HRSGs, making the negative determination on the steam turbine irrelevant. Circumstances dramatically changed when the Executive Director committed his about-face and changed the 100% positive use determination to a negative use determination. That revised ruling restarted the appellate clock on the entire decision. It is a well-established principle that modification of a ruling restarts the time period for filing an appeal. *See, e.g.*, TEX. R. CIV. P. 329b(h) ("If a judgment is modified, corrected or reformed in any respect, the time for appeal shall run from the time the modified, corrected, or reformed judgment is signed . . ."); *Arkoma Basin Exploration Co., Inc. v. FMF Associates*, 249 S.W.3d 380 (Tex. 2008) (cross-appeal was timely because the original judgment was modified by remittitur).

[24] This section of the Reply responds to Section III(J) of the ED Response.

Further, the Executive Director requested a remand of "the application," and the application encompasses the request for a positive use determination for the steam turbines. The steam turbine request was therefore remanded to the Executive Director along with the rest of the application and should have been addressed in the Executive Director's determination. The Executive Director's Response asserts that only the HRSG portions of the application were before the Commission and thus subject to remand by the General Counsel. ED Response, pg. 18. However, Appellant's response to the appraisal district's appeal, which properly raised the issue of the negative use determination for the steam turbines, was before the Commission in connection with the appraisal district's appeal. The steam turbine issue was therefore subject to remand.

III. Conclusion

The Texas Legislature by statute has dictated that HRSGs are pollution control equipment and has assigned to the TCEQ the task of assessing the amount of positive use. The Executive Director and OPIC impermissibly seek a broader role for the TCEQ and attempt to supersede the Legislature's will by flatly denying HRSGs' classification as pollution control equipment. Even if, somehow, some way, the Executive Director has authority to assess whether HRSGs control pollution, the Executive Director and OPIC's attempts to completely deny the HRSGs' status as pollution control equipment because it is "production equipment" or "avoided emissions equipment" is unsupported by fact or law. As well, the Executive Director's process for reversing longstanding TCEQ policy on the HRSGs has disregarded multiple procedures and protections required by the Tax Code, the APA, the applicable administrative rules, and the Texas Constitution. For any of these reasons individually, and for all of these reasons collectively, we

respectfully request that the Commissioners remand Appellant's application for a positive use determination.

Respectfully submitted,

LOCKE LORD LLP

ELIZABETH E. MACK
State Bar No. 12761050
GEOFFREY R. POLMA
State Bar No. 16105280
2200 Ross Ave., Suite 2200
Dallas, Texas 75201
emack@lockelord.com
(214) 740-8598
(214) 756-8598 (fax)

COUNSEL FOR FREESTONE POWER GENERATION, LLC

Dated: October 30, 2012

By: _____
Elizabeth E. Mack