State Office of Administrative Hearings

Cathleen Parsley
Chief Administrative Law Judge

July 13, 2010

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

Re: SOAH Docket Nos. 582-08-3825 and 582-09-3548
TCEQ Docket Nos. 2008-0955-UCR and 2009-0350-UCR
In Re: Application of the City of Alton to Amend Certificate of Convenience and Necessity No. 20809 in Hidalgo County and Application of the City of Mission to Amend Certificate of Convenience and Necessity No. 20768 in Hidalgo County

Dear Mr. Trobman:

The above-referenced matter will be considered by the Texas Commission on Environmental Quality on a date and time to be determined by the Chief Clerk's Office in Room 201S of Building E, 12118 N. Interstate 35, Austin, Texas.

Enclosed are copies of the Proposal for Decision and Order that have been recommended to the Commission for approval. Any party may file exceptions or briefs by filing the documents with the Chief Clerk of the Texas Commission on Environmental Quality no later than August 2, 2010. Any replies to exceptions or briefs must be filed in the same manner no later than August 12, 2010.

This matter has been designated **TCEQ Docket Nos. 2008-0955-UCR and 2009-0350-UCR; SOAH Docket Nos. 582-08-3825 and 582-09-3548**. All documents to be filed must clearly reference these assigned docket numbers. All exceptions, briefs and replies along with certification of service to the above parties shall be filed with the Chief Clerk of the TCEQ electronically at http://www10.tceq.state.tx.us/epic/efilings/ or by filing an original and seven copies with the Chief Clerk of the TCEQ. Failure to provide copies may be grounds for withholding consideration of the pleadings.

Sincerely,

Craig R. Bennett
Administrative Law Judge

CRB/ls
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STYLE/CASE: **CITY OF ALTON**

SOAH DOCKET NUMBER: **582-08-3825**

REFERRING AGENCY CASE: **2008-0955-UCR**

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Note: CONSOLIDATED WITH DOCKET NO. 582-09-3548
xc: Docket Clerk, State Office of Administrative Hearings

SOAH DOCKET NOS. 582-08-3825 and 582-09-3548
TCEQ DOCKET NOS. 2008-0955-UCR and 2009-0350-UCR

APPLICATION OF THE CITY OF ALTON TO AMEND CERTIFICATE OF CONVENIENCE AND NECESSITY NO. 20809 IN HIDALGO COUNTY	§	BEFORE THE STATE OFFICE
APPLICATION OF THE CITY OF MISSION TO AMEND CERTIFICATE OF CONVENIENCE AND NECESSITY NO. 20768 IN HIDALGO COUNTY	§	OF
	§	ADMINISTRATIVE HEARINGS

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TCEQ DOCKET NOS. 2008-0955-UCR and 2009-0350-UCR

APPLICATION OF THE CITY OF ALTON TO AMEND CERTIFICATE OF CONVENIENCE AND NECESSITY NO. 20809 IN HIDALGO COUNTY	§	**BEFORE THE STATE OFFICE**
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	§	**ADMINISTRATIVE HEARINGS**

PROPOSAL FOR DECISION

I. INTRODUCTION

The City of Alton (Alton) and the City of Mission (Mission) have each filed a separate application with the Texas Commission on Environmental Quality (TCEQ or Commission) to amend their existing sewer certificates of convenience and necessity (CCN). In their applications, they each seek certification to the same area in Hidalgo County. Because the Commission does not permit dual certification, the two applications were consolidated for a hearing and the issuance of a single proposal for decision (PFD), which the Commission may then consider in deciding which city should be certificated for the requested area.

Both Mission and the Executive Director (ED) of the Commission recommend that Mission be certificated for the area. In contrast, Alton asserts it should be certificated for the area. After considering the evidence and arguments, the Administrative Law Judge (ALJ) recommends that the Commission approve Mission's application and allow it to amend its CCN to include the requested area. Primarily, the ALJ's recommendation is based upon findings that (1) Mission is more financially stable; (2) Mission has its own water treatment facilities; and (3) the requested area is in the ETJ of Mission. To a great extent, all of the other factors considered and addressed in this PFD are neutral or only slightly favor one applicant over the other. If the Commission accepts this recommendation and certificates the area to Mission, then Alton's application should be denied.

II. PROCEDURAL HISTORY, NOTICE, AND JURISDICTION

On January 31, 2008, Alton filed its initial application for amendment of its CCN to include a proposed utility service area located approximately 2.4 miles west of downtown Alton. The proposed service area is classified as "economically distressed" and is generally bounded on the north by FM 2221 (Mile 7 North Road); on the west by Bentsen Palm Boulevard; on the south by an irrigation canal between Basham Subdivision No. 37 and Basham No. 34; and on the east by La Homa Road. The total area sought to be served by Alton was 819 acres, and included approximately 453 customers. The Commission initially rejected Alton's application for filing because of deficiencies. However, the deficiencies were remedied by March 7, 2008, and the application was accepted. Thereafter, notice of the application was provided to all affected persons.

Upon receiving notice of Alton's request to amend its CCN, Mission timely protested the application and the matter was referred to the State Office of Administrative Hearings (SOAH) for an evidentiary hearing. A preliminary hearing was conducted on August 25, 2008, at which parties were named and a procedural schedule was adopted. However, on or about November 17, 2008, Mission filed a competing application to amend its CCN to include the proposed service area sought by Alton. Mission then asked for an abatement of the proceedings to allow its application to be processed by TCEQ and then sent to SOAH so the two cases could be consolidated for hearing. The ALJ granted the requested abatement.

On or about April 8, 2009, the TCEQ referred Mission's application to SOAH. A joint preliminary hearing/prehearing conference was then conducted in both cases on July 14, 2009, at which time the two cases were consolidated for hearing. The contested case hearing was held on February 23-26, 2010. The record closed on May 14, 2010, after written closing arguments and reply briefs were filed by the parties. There are no contested issues of notice or jurisdiction, so those matters are set forth in the findings of fact and conclusions of law in the proposed order attached to this PFD.

III. APPLICABLE LAW

The Texas Water Code and the Commission's rules specifically provide the standards for awarding a CCN when two retail public utilities are seeking certification to the same economically-distressed area. First, TEX. WATER CODE § 13.246(f) provides:

> If two or more retail public utilities or water supply or sewer service corporations apply for a certificate of public convenience and necessity to provide water or sewer utility service to an uncertificated area located in an economically distressed area and otherwise meet the requirements for obtaining a new certificate, the commission shall grant the certificate to the retail public utility or water supply or sewer service corporation that is more capable financially, managerially, and technically of providing continuous and adequate service.

Moreover, TEX. WATER CODE § 13.241(e) provides that the Commission "by rule shall develop a standardized method for determining under Section 13.246(f) which of two or more retail public utilities . . . is more capable financially, managerially, and technically of providing continuous and adequate service." Pursuant to this statutory directive, the Commission has adopted such rules.

In 30 TEX. ADMIN. CODE § 291.102(g), the Commission has established the factors to consider when deciding between two retail public utilities seeking certification in an economically-distressed area. In particular, the Commission incorporates the general factors in 30 TEX. ADMIN. CODE § 291.102(a)-(f), and then also has set out additional considerations in subsection (g). For purposes of this case, the parties have agreed that the following factors from 30 TEX. ADMIN. CODE § 291.102 are relevant to the outcome of this case (and have briefed them accordingly):

- The financial, managerial, and technical capabilities of the applicants - 30 TAC § 291.102(a)
- Whether service in the requested area is inadequate - 30 TAC § 291.102(d)(1)
- Whether there is a need for service in the requested area – 30 TAC § 291.102(d)(2)

- The effect of granting the CCN on the recipient, landowners, and other retail public utilities - 30 TAC § 291.102(d)(3)
- Ability of the applicants to provide adequate service - 30 TAC § 291.102(d)(4)
- Feasibility of obtaining service from an adjacent retail public utility - 30 TAC § 291.102(d)(5)
- Financial ability of the applicants to pay for the facilities necessary to provide continuous and adequate service - 30 TAC § 291.102(d)(6)
- Environmental integrity - 30 TAC § 291.102(d)(7)
- Probable improvement of service or lowering of cost to consumers in the requested area - 30 TAC § 291.102(d)(8)
- Effect on land in the requested area - 30 TAC § 291.102(d)(9)
- Whether the CCN is necessary for the service, accommodation, convenience, or safety of the public - 30 TAC § 291.102(c)
- Comparative assessment of the applicants' financial, managerial, and technical capabilities - 30 TAC § 291.102(g).

Each of these factors set out in the Commission's rules is addressed separately below, including the parties' arguments and the ALJ's analysis.

However, it should be noted that the issues set out above frequently overlap. For example, the financial abilities of the applicants are relevant under at least three separate factors set out in the Commission's rules. So as to not make the PFD repetitive, if an issue is already addressed elsewhere in the PFD, that section is referenced without repeating the discussion or underlying facts. For at least a couple of issues, there is no new discussion at all, but simply a reference to a prior section.

IV. DISCUSSION

A. Description of the Requested Area and the Two Systems

Before addressing the statutory factors, it is important to briefly describe the proposed utility service area (the requested area) and the two municipal systems vying to provide service to it.

1. The Requested Area

The requested area is located in Hidalgo County, Texas, and—as noted previously—is generally bounded on the north by FM 2221 (Mile 7 North Road); on the west by Bentsen Palm Boulevard; on the south by an irrigation canal between Basham Subdivision No. 37 and Basham No. 34; and on the east by La Homa Road.[1] The total area sought to be served ranges between 819 and 845 acres (Mission seeks certification over a slightly larger area than does Alton). The requested area is located approximately 2.4 miles west of downtown Alton, outside of its city limits and its extra-territorial jurisdiction (ETJ). It is approximately 5.2 miles from downtown Mission and is located within Mission's ETJ. The requested area is immediately adjacent to the certificated service areas of both Alton and Mission.

The requested area is classified as "economically-distressed" and includes between 453 and 722 potential customers (the parties provide different estimates of potential customers due, in whole or in part, to the slightly larger area sought by Mission). Water service is provided to the requested area by the Sharyland Water Supply Corporation. The area contains many substandard lots and colonias.[2]

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[1] Attached to this PFD are two maps, marked as Attachments A and B, showing the general location of the requested area in relation to Mission and Alton, and showing the requested area in relation to existing CCN territories. These maps are taken from Mission Ex. 4.

[2] Tr. at 23 and 163-164.

2. City of Alton's System

Alton currently provides sewer service to approximately 2,800 connections,[3] and has an interlocal agreement under which it obtains wastewater treatment services from the City of McAllen (McAllen). The wastewater collection system is owned by Alton, and transports sewage through collection lines to 10 wastewater lift stations and a 36-inch trunk line that connects to a main lift station. There, the sewage is metered by McAllen, pumped into McAllen's collection system, and transported to McAllen's North Wastewater Treatment Plant for treatment.[4] Under the interlocal agreement, McAllen is obligated and has the current capacity to accept all existing sewage from Alton, in addition to what would be expected from the requested area if Alton's CCN is amended.

Alton currently has approximately 1.023 million gallons per day (MGD) purchased sewage capacity from McAllen. But, it has the ability to expand its purchased capacity—up to a total of 1.922 MGD.[5] Further, McAllen is currently expanding its North Wastewater Treatment Plant from 6.0 MGD to 18.0 MGD capacity. McAllen has 60 licensed wastewater operators, and these operators are responsible for the operation and maintenance of Alton's collection system in addition to McAllen's system. Alton's limited public works crews provide only basic inspection and repair services for the system but, otherwise, most services are provided by McAllen.

3. City of Mission's System

Mission fully operates its own wastewater collection and treatment system serving 20,671 connections, with a wastewater treatment plant having an existing capacity of 9.0 MGD.[6] Currently, Mission uses approximately 6.2 MGD of its capacity, leaving roughly 2.8 MGD available for expansion.[7] Mission also employs its own licensed wastewater treatment operators, who have full-

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[3] Tr. at 119. The total population of Alton is slightly less than 10,000 residents. *Id.*

[4] Alton Ex. 2, at 8; Alton Ex. 15, at 4 and 16-17; Alton Ex. 25, at 5; and Alton Ex. 27.

[5] Alton Ex. 2, at 9.

[6] Mission Ex. 4, at 6 and Attachment FLK-2. Mission's has a total population of slightly more than 67,000.

[7] Mission Ex. 4, at 6.

time responsibility for oversight of Mission's system. As of the hearing, Mission had 128 employees in its Public Works Department, 12 of whom work at the wastewater treatment plant.[8] Further, an additional nine of those employees work in maintenance and are responsible for the maintenance of Mission's wastewater treatment system. In addition to serving its own residents, Mission also provides wastewater service to the neighboring communities of Palmhurst and Granjeno.

Having identified the requested area and the two systems seeking to provide service, the ALJ now turns to the various factors identified by statute and the Commission's rules for determining which entity should be certificated. The first and overarching factor is the entities' financial, managerial and technical capabilities. Subsumed within that are the other factors set out in the Commission's rules. All of these are discussed below.

B. Financial, Managerial and Technical Capabilities of the Applicants[9]

As a city of less than 10,000, it is obvious that Alton has more limited resources than Mission, a city of more than 67,000. However, that alone does not mean that Alton is less financially capable than Mission. Rather, the analysis of financial capability is tied more to ongoing expenses and revenues, along with available cash or other funding, that reveal the overall financial health of the municipality.

Alton concedes that prior financial analyses (particularly an audit from 2007-2008) show weaknesses in its financial position, but it contends these weaknesses have been dealt with and, as of today, Alton is financially stable. In particular, that 2008 audit showed that Alton had a reduction in net assets of $872,000, a reduction in cash and cash equivalents of approximately $395,000, and a reduction in net revenues of more than $167,000 between 2007 and 2008.[10] As a result of its reduced revenues, Alton had to draw down its cash accounts by more than $300,000 to cover its

[8] Mission Ex. 7, at 5-6.

[9] Because all parties appear to agree that both Alton and Mission are technically and managerially capable of providing adequate service, the ALJ discusses these elements only briefly in this section.

[10] Tr. at 138; Alton Ex. 14, at 22.

shortfall in revenues. However, Alton contends that this is partially due to poor collection practices for its utility service (namely, at least 300 accounts that were not being billed for service) and that, after an audit of customer accounts and connections, it has corrected those practices and expects its utility revenues to increase by $200,000 going forward.

Alton points to the testimony of its expert witness, Jeff Snowden, who prepared a feasibility study analyzing Alton's ability to provide sewer service to the requested area.[11] In his study, he determined that Alton could financially handle the provision of new service to the requested area and, when coupled with rate increases, such a move would strengthen Alton's financial situation over the next ten years.[12] Mr. Snowden testified that Alton's sewer revenues increased 11.9% per year, on average, for the five-year period starting in 2002.[13] For fiscal year 2008-2009, Alton's sewer expenses were $832,678 and its revenue was $865,038, showing Alton to be financially stable in providing sewer service even without the inclusion of the requested area.[14] Further, the budget projections for 2009-2010 again showed that Alton's revenues were expected to exceed its expenses for sewer service by a significant amount, without the impact of the requested area.[15] Given its low debt service, with a balance of approximately $190,000 on a prior loan from the Texas Water Development Board (TWDB),[16] Alton claims that its financial situation is now very stable.

With its current stability, Alton argues it has the financial ability to fund the expansion and provide service to the requested area. Based on Mr. Snowden's rate analysis, Alton adopted a rate change ordinance that charges higher rates over the next five years. Alton argues its planned rate increase is sufficient to raise revenues to a healthy and sustainable level, and asserts the rates may be further increased in the future if needed. Alton claims part of its Project Strategic Plan included the invitation by TWDB to apply for $5.6 million in 2009 and $3.085 million in 2010 under the CWSRF

[11] Alton Ex. 30.

[12] Alton Ex. 30, at last page (unnumbered).

[13] Tr. at 352.

[14] Alton Ex. 2, at 15; Alton Ex. 12.

[15] Alton Ex. 13.

[16] Alton Ex. 28.

program. Funding from TWDB would be a majority of the funding source for the expansion to the requested area. Alton contends that it was informed by the TWDB that the sewer project for the requested area was a high ranking project and, thus, was likely to get funding; however, the processing of Alton's application for funding cannot proceed until Alton has obtained the CCN for the requested area.[17]

Further, in regard to its managerial and technical capabilities, Alton points to its interlocal agreement with the City of McAllen (McAllen) to treat all of Alton's sewage. Alton insists the two cities work closely to provide service to Alton's customers. This service would extend to the requested area, as the interlocal agreement allows for Alton to expand its system. Because of the interlocal agreement, Alton contends that it actually has better managerial and technical capabilities than Mission, because Alton relies on the much larger McAllen in the actual provision of sewer service. Thus, McAllen's technical and managerial capabilities are essentially Alton's, at least for purposes of the analysis in this case, because McAllen is the entity that will provide the bulk of the actual sewer operational services to the requested area.

Not surprisingly, Mission contends it is the better candidate for the CCN. Mission argues its financial audits from 2008 and 2009 show the city of Mission has the financial ability to provide continuous and adequate service to the proposed area. Mission has met its debt service coverage ratio nine out of the last ten years, and has more than $6 million in its unrestricted fund balance to fund the expansion project to provide service to the requested area. Mission notes that its credit rating is A3,[18] which is upper medium grade. Further, Mission notes that its sewer operations produce a net revenue gain for the city, and that $1.5 million is transferred from the sewer fund to the general fund of Mission on a recurring basis. This shows that Mission's sewer operations are financially stable and could fund expansion into the requested area.[19]

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[17] Tr. at 192-194.

[18] Tr. at 56. The transcript erroneously refers to "83" when it should be "A3." *See* Mission Ex. 6, at 33.

[19] The ALJ does not discuss at length Mission's financial figures here. Rather, they are addressed below in regard to the evidence relied on by the ED and in the ALJ's analysis.

Moreover, Mission's consulting engineer, Fred L. Kurth, testified that Mission has the capability necessary to provide continuous and adequate service to the proposed area. He testified that Mission has provided sanitary sewer service for almost 80 years, as well as expanded its service when needed to meet the demands of its customers. The ED agrees that Mission is financially, managerially, and technically capable of providing service. The ED questions whether Alton is, though, and expresses doubts about the reliability of Alton's audits, due to deficiencies not considered and errors found within the audit. Moreover, the ED notes that Alton relies heavily on grants and loans as part of its funding, whereas Mission has the financial ability to extend service to the proposed area without loans or grants. In its closing arguments, the ED presents the following table comparing Alton and Mission in regard to 2008 financial data (footnotes omitted):[20]

Comparison of 2008 Annual Financial Report Information

	Column A	Column B- Alton	Column C-Mission
1	Total assets	$18.6 million[81]	$239.9 million[82]
2	Long-term debt	4.2 million[83]	$64.4 million[84]
3	Net assets (equity)	14.2 million[85]	$161.9 million[86]
4	Debt equity ratio	All funds: 0.29:1 Utility fund only: 0.0:1 (no debt)[87]	All funds: 0.40:1, Utility fund only: 0.55:1
5	Utility Fund -Net Income/(loss)	$(576,747)[88]	$1,644,148[89]
6	Depreciation	$390,007[90]	$3,895,366[91]
7	Interest and fiscal charges	-0-[92]	$1,762,595[93]
8	Available cash for debt service (line 5 + 6 + 7)	$(186,740)	$6,358,999[94]
9	Required debt service	-0-[95]	$3,842,831[96]
10	Debt service coverage (line 8 divided by line 9)	Negative funds available for debt service; no debt outstanding	1.52:1

Based on the information contained in the table, the ED contends that Mission is clearly in a stronger financial position than Alton. The ED agrees that both Alton and Mission are capable managerially and technically of providing continuous and adequate service to the area. However, the ED disagrees that Alton has shown that it is financially able to provide adequate and continuous service to the requested area.

[20] ED's Closing Arguments, at 10.

Ultimately, the ALJ agrees with the ED's assessment and concludes that both Mission and Alton have the managerial and technical capability to provide adequate service to the requested area, and that Mission has the financial capability to do so. However, the ALJ is concerned that Alton may not have the financial capability to do so.

Although Alton's rate expert provided an analysis showing that Alton could provide service to the requested area, his analysis had numerous deficiencies which cause the ALJ to question his conclusions. For example, he left out part of the capacity payment that Alton is required to make to McAllen in the next few years, thus leaving his annual expenses understated and cash flow projections overstated by approximately $75,000.[21] This would have a significant impact on available cash, even if it does not cause it to become negative. Moreover, his analysis included an assumption that Alton would receive 30% of the funding for the capital improvement project to provide new service from the TWDB, thus requiring Alton to fund the remaining 70%. However, if Alton did not obtain the funding, it would be required to obtain loans for the full 100%, which, as Mr. Snowden acknowledged, would further erode Alton's ending available cash balance.[22] The ALJ is not inclined to rely on grants as a basis for determining Alton's financial capability, because the availability of, and eligibility for, grants is uncertain.[23]

Further, Mr. Snowden'a analysis included a 100% collection rate from sewer customers, but testimony from the City Manager for Alton indicated that its collection rate was approximately 95%.[24] Thus, Mr. Snowden's analysis further overstated projected revenues by approximately $35,000 the first year (and presumably a greater amount for subsequent years that have rate increases).[25] Even the audit information presented by Alton contained inaccuracies that overstated its performance. Among other things, the audit for 2008 understated depreciation (thus understating

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[21] Tr. at 230-232.

[22] Tr. at 242-243.

[23] This may be particularly true in the current economic climate where many state agencies are facing mandatory budget cuts.

[24] Tr. at 131 and 355-356.

[25] Tr. at 356.

expenses) by $351,000.[26] Mr. Snowden acknowledged that, during the period he looked at the financials for Alton, its cash balance had been eroded because its expenses had exceeded its revenues.[27] And, his analysis (that showed Alton's sewer system financial situation being strengthened) included the requested area, with the infrastructure cost being paid for fully by low-interest loans or grants. Thus, it is difficult to assess Alton's current financial situation without the inclusion of the requested area.

All of these concerns lead one to question how stable Alton is financially. Its own auditors raised at least two serious deficiencies from the 2008 audit, including high-risk findings that (1) significant year-end adjustments were necessary for Alton's financial statements to be in accordance with generally accepted accounting principles, and monthly and year-end statements were not an accurate reflection of the actual financial position of the city; and (2) an actual inventory of Alton's capital assets had not been performed recently, thus raising the question of whether the city's reported capital assets reflected its actual assets. Given Alton's past history of sewer revenues not covering expenses, its accounting errors and deficient practices, the optimistic assumptions built into Mr. Snowden's financial analysis and projections—coupled with Alton's small size—cause the ALJ to have doubts about Alton's financial capability to provide adequate and continuous service to the requested area.

The ALJ does not have similar doubts about Mission. Although Mr. Snowden raised questions about Mission's financial projections and its future ability to handle expected projects, the ALJ is not as troubled by those concerns. For example, Mr. Snowden noted that Mission has potential expansion projects costing more than $25 million in the works (including the requested area) and that, in his estimation, it did not have the ability to obtain financing for those projects without dropping below its necessary debt coverage ratio of 1.25 (namely, to obtain financing and be in compliance with the terms of its loans, Mission must have at least $1.25 in excess revenues, after

[26] Tr. at 272.

[27] Tr. at 272-273.

paying expenses, for every $1.00 in debt service owed).[28] But, except for the amount that would be required for serving the requested area, the record does not indicate that any of the proposed projects are required. Other than the service expansion for the requested area, the other two proposed projects are for expansion of Mission's wastewater treatment facilities.[29] Because Mission currently has excess capacity of 2.8 MGD for providing wastewater treatment, those expansion projects appear discretionary and do not cause the ALJ to question Mission's financial position.[30]

Moreover, even with those projects, Mission's free cash would still exceed its debt service, thus allowing it to service its debt even though it would be out of compliance with its debt covenant requirement of a 1.25 ratio.[31] This is different than if Mission would be financially losing money and not able to service its debt. As noted, Mission currently provides more than $1.5 million from its sewer fund to its general fund; thus, its sewer operations are financially strong. And, its city bond rating is healthy. Given all of this, the ALJ has no reason to doubt Mission's financial capability to provide adequate and continuous service to the requested area.[32]

C. Adequacy of Service in the Requested Area and the Need for Service

Currently there is no retail service available in the requested area. The residents in the area are served by septic systems. Some of these septic systems are on substandard lots. Therefore, both Alton and Mission argue the area does not have adequate service.[33] The ED agrees.

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[28] Tr. at 221, 233, and 239-242.

[29] Tr. at 224.

[30] Further, Mr. Snowden made numerous inaccurate or unfair assumptions in his analysis of Mission's ability to handle the proposed projects, which the ALJ does not discuss at this time. To his credit, he acknowledged and corrected for many of these at the hearing. Tr. at 239-241.

[31] Tr. at 241 (using loan assumptions similar to those for Alton).

[32] Because of Mission's long history of providing service, along with the fact that Alton's service is essentially backed by McAllen, the ALJ agrees with the ED that both Alton and McAllen are technically and managerially capable of providing service.

[33] However, Mission also focuses on the service currently provided by Alton. Specifically, Mission argues that Alton is not currently providing adequate sewer service in its entire certified area. The ALJ finds this issue to be irrelevant in regard to this particular criterion.

Given that all parties agree there is not adequate service in the area, the question then becomes whether there is a need for service. The requested area includes three colonias along the Texas-Mexico border.[34] Colonias are residential areas lacking one or more of the basic living necessities, which include wastewater systems meeting state standards. The requested area is also experiencing rapid growth in denser areas. Septic systems will not fit in these denser areas, and therefore, Alton argues, centralized service is needed. Mission agrees service is needed in the proposed area. Mission also points to two requests for service received by it as further evidence that service is needed in the area. The ED agrees that the area lacks existing service and has a need for service. However, the ED disagrees that Mission has received two requests for service. The ED notes that those requests were informal in nature and do not qualify as formal requests for service. But, this does not change the ED's opinion that service is needed for the area.

The ALJ concludes that the record clearly establishes that the requested area does not currently have adequate sewer service and has a need for service. Because the requested area has some more densely-populated sections, namely the colonias, it is different from other rural areas where the landowners may be perfectly content to have septic systems and those systems may be sufficient to meet their needs. The colonias do not have room for septic systems for all residents, and thus do not have the ability to meet the sewer service needs of the residents in a manner that ensures the protection of public health and the environment. Because of these potential health and environmental concerns for this area, the provision of adequate sewer service is a legitimate need as the area continues to grow.

D. Effect of Granting the CCN on the Recipient, Landowners, and Other Retail Public Utilities[35]

Alton argues granting the CCN will affect it in a positive way. The CCN will allow Alton's system to expand in size and therefore allow Alton and its customers to see some cost benefits. The

[34] Tr. at 23 and 163-164.

[35] Mission did not present any argument on this issue; therefore, arguments from only Alton and the ED are discussed.

agreement with McAllen, coupled with its billing agreement with Sharyland Water Supply Corporation, allow for Alton's expansion into the requested area without affecting service to its current customers. The landowners in the area will also be positively affected as septic systems on substandard lots will be decommissioned and centralized sewer service will be offered. Alton contends that landowners of undeveloped land will be able to develop their land more densely, increasing the chance of commercial development—as some businesses require centralized sewer service. Only Mission has protested Alton's CCN application, and no other retail public utility has indicated a willingness to provide service to the requested area. Thus, Alton argues, the only negative effect is on Mission, which would have its CCN application denied if Alton's is granted.

The ED argues both applicants are on equal footing regarding this criterion. The effect on the landowners, if the CCN is granted to either applicant, is access to centralized sewer service. No other retail public utility, other than Alton will be affected if Mission receives the CCN, and only Mission is affected by Alton receiving the CCN.

The ALJ agrees with the ED. It appears that landowners in the area would benefit from either CCN being granted, as they will receive better service through the development of an integrated sewer system for the area. And, because no other entities have opposed either application nor sought to provide service, it appears that the only potential harm would be to the municipality whose application is denied. Thus, this factor supports certification, but is neutral in helping distinguish which CCN amendment should be granted.

E. Ability of Applicant to Provide Adequate Service

As discussed above, Alton owns its own wastewater collection system which transports sewage through a series of collection lines ending at the main lift station where the sewage is metered by McAllen and pumped to McAllen's collection system. Alton's total current purchased capacity in McAllen's treatment plant is 1.023 MGD, with the ability to purchase up to a total of 1.922 MGD in the future. Further, McAllen is in the process of expanding its North Wastewater Treatment Plant from 6.0 MGD to 18.0 MGD, so Alton's ability acquire additional treatment

capacity appears likely. With Alton's current capacity and additional capacity available, Alton argues it is able to provide adequate service to the requested area.

Also as discussed above, Mission owns its own treatment plant, with a current capacity of 9.0 MGD. Mission is only using 6.2 MGD of the 9.0 MGD available. This leaves Mission's standby capacity at 2.8 MGD (in comparison to Alton's current standby capacity of 1.022 MGD). Thus, it is clear that both cities have enough standby capacity to serve the proposed area. While Mission can serve nearly three times as many additional connections as Alton, Alton still has adequate capacity for the proposed area. However, even with this standby capacity, Mission argues that Alton is not currently serving all of its certificated area, thus calling into question the "adequacy" of Alton's current service. Specifically, residents within Alton's city limits located between Moorfield Road and LaHoma Road do not currently have access to sewer service.[36] And, in total, there are approximately nine different pockets within Alton's CCN boundaries that are not currently able to receive sewer service.[37]

Apart from the financial concerns previously discussed above, the ALJ finds that both Alton and Mission could provide adequate service. Mission's ability is direct, as a result of its own treatment plant, while Alton's ability derives from its interlocal agreement with McAllen. Given Mission's excess standby capacity of more than 2.8 MGD, it can take in the requested area and provide service to it. Similarly, Alton's right to purchase additional treatment capacity from McAllen allows it to provide service to the requested area as well. Thus, both entities can provide adequate service. The fact that Alton is not currently providing service to all of its CCN area is not consequential without more details about the reasons for that. The question is whether Alton has the "ability" to provide service, and the ALJ finds that it does, given its excess capacity. However, because Mission owns its own complete treatment system, it has greater control over the provision of service than Alton. Given this, the ALJ finds that, although this factor supports both entities' applications, it slightly favors Mission's application.

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[36] Tr. at 120.

[37] Tr. at 120-121.

F. Feasibility of Obtaining Service from an Adjacent Retail Public Utility

In general, the ALJ construes this factor as relating to the ability of an existing utility to provide service when a new utility is being proposed or a new CCN sought. Thus, it is not as relevant here. However, the parties' arguments go beyond this, so the ALJ addresses such arguments and analyzes them accordingly.

Alton argues Mission did not show any interest or plan for the proposed area prior before Alton filed its CCN application. While Alton took steps to determine the condition of the septic tanks in the proposed area, Mission did not. Alton's planning for the proposed area began in 2007 and includes a process to implement its plan. Mission has not shown that it either planned to provide service to the area before Alton began its efforts, nor that it has any specific plan or process currently in place to do so.

In response, Mission argues its application is not a mere afterthought just because it was submitted after Alton's, but rather Mission is very interested in servicing the area. Mission notes both cities are adjacent to the requested area and, therefore, it is feasible for either to serve the area. Moreover, Mission points to the fact that the requested area is in its ETJ, which gives it another incentive for providing service. The ED states both applicants are equal on this criterion. The feasibility of obtaining service from any other adjacent retail public utilities is unknown.

The ALJ finds that this factor weighs in favor of granting the CCN to either applicant. There is no evidence of any other retail public utility other than Mission or Alton who is willing and able to provide service to the requested area. Both Mission and Alton are adjacent to and best situated to provide service. Thus, they currently appear to be the only retail public utilities interested and able to provide service to the area. Although the requested area is in the ETJ of Mission, Alton has taken the greater initiative in seeking to provide service to it. Alton prepared the information necessary for seeking funding from the Texas Water Development Board (TWDB) to provide service to the area, and filed its CCN application 10 months before Mission. As such, this factor slightly weighs in favor of Alton.

G. Financial Ability of the Applicant

See Section B above, where the financial capabilities of both Alton and Mission are discussed in detail.

H. Environmental Integrity

This factor is essentially a non-issue. Alton argues its practices for the provision of service will improve and protect the environmental integrity of the area. First, Alton has provisions for storm water run-off and constructs its facilities to limit the environmental impact during construction. Second, Alton has a pretreatment ordinance which ensures hazardous pollutants are properly treated and the buildup of grease in the system is minimized. Industrial customers of sewer service would be subject to the requirements of this ordinance. Third, Alton plans to decommission the substandard septic systems and use gravity collection lines. Taken together, Alton argues that these steps maintain the environmental integrity of the proposed area. Mission also plans to decommission substandard septic systems and will use gravity collection systems, arguably eliminating potential backups and overflows of septic tanks (which can create health hazards).

The ED finds both applicants equal on this criterion, noting that the construction necessary for providing service to the requested area will cause a temporary disturbance to the environmental integrity regardless of which applicant receives the CCN. Similarly, both applicants will utilize similar systems to provide service. Thus, environmental integrity provides no basis for distinguishing between the applications of either Alton or Mission.

I. Probable Improvement of Service and Lowering of Cost to Consumers in the Area

Currently there is no centralized sewer service in the proposed area. Either proposed project would bring the first integrated sewer service to the area. The ED finds both applicants equal on this criterion. Granting the CCN to either applicant would lower costs to consumers in the requested area. Expected septic tank costs are higher per month than the rates of either applicant. Specifically,

expected septic tank costs over 20 years is approximately $35 per month.[38] In contrast, a customer using 6,000 gallons per month would pay $21.07 per month under Alton's rate structure, and $23.85 under Mission's rate structure.[39] While Mission's rates to the area would be higher than Alton's rates, the ED argues Alton's rates are not structured appropriately and would have to be raised to be financially viable for ensuring continuous and adequate service.

Given the evidence, the ALJ finds that granting either application would result in the improvement of service and the lowering of costs to consumers. Both Alton and Mission's expected rates would be lower than the anticipated monthly costs for a septic system. Further, a new integrated sewer system would be an improvement over individual septic systems. As far as comparing the two utilities, the ALJ finds that Alton's rates are slightly lower than Mission's, but the ALJ has previously expressed concerns about Alton's financial condition. Even Alton's own consultant opined that Alton should raise its rates by more in the future. Thus, the ALJ finds the relatively small rate differential to be insignificant and both applicants to be equal on this criterion.

J. Effect on Land in the Requested Area

Alton argues the effect will be positive because, as previously stated, Alton will decommission the substandard septic systems, thus eliminating the hazard they create and improving the environmental quality. Alton also argues the ability to develop the undeveloped land more densely is a positive consideration, as it allows the land's potential use to be fully realized. Landowners who want to develop will also have certainty about the availability of centralized sewer service if they want to develop their land without septic systems. These same benefits apply to Mission's proposed development of a sewer system in the requested area. Therefore, the ED asserts that granting the CCN to either applicant would have the same result to the land, and this result would be a net positive. The ALJ agrees. The availability of sewer service is more environmentally protective than individual septic tanks, and provides for greater uses of the land in the area.

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[38] Mission Ex. 4, at 8; Tr. at 105.

[39] ED's *Closing Argument*, at 11-12. If a flat rate is used, Mission's rates are $26, without a gallonage limit.

K. Whether the CCN is Necessary for the Service, Accommodation, Convenience, or Safety of the Public

See Section C above, where the need for service in the requested area is discussed in detail.

L. Comparative Assessment of the Applicants' Financial, Managerial and Technical Capabilities

The ALJ attempted to make a comparative assessment of the financial, managerial, and technical capabilities of Alton and Mission in Section B above. However, the Commission's rules also provide some additional subfactors for consideration in the comparative assessment. These subfactors are discussed below. Where they overlap with prior discussions above, the ALJ simply references the prior section.

1. Infrastructure Adequacy

There is no centralized sewer system in the requested area and no adequate infrastructure. The previous evidence, Alton contends, shows Alton's infrastructure is adequate to provide service to the proposed area and that there is no evidence to show that Mission's infrastructure is more adequate than Alton's. Mission distinguishes itself from Alton by noting that, while both cities own their respective lift stations and collection lines, only Mission owns and operates its own wastewater treatment plant. However, neither city currently has infrastructure in the proposed area. The ED believes both applicants are equal on this criterion, and the ALJ agrees. Both cities would have to build significant infrastructure to serve the requested area, and the anticipated cost to each is relatively similar. Although Mission and Alton will face different challenges in extending their service facilities to the requested area, there are no major impediments to the ability of each to build out the necessary infrastructure. Thus, the cities are equal on this criterion.

2. Technical Knowledge of the Applicants

Alton argues its Interlocal Agreement with McAllen gives Alton the required technical knowledge to provide adequate service. Further, Alton contends, no evidence was presented to show Mission has superior technical knowledge. Alton argues that both the ED's and Mission's positions are counter to the State of Texas' public policy decision to promote regionalization and to encourage smaller entities and cities to connect to larger regional systems like McAllen's. Alton argues it is as technically capable as Mission and equally accountable when comparing the two applicants in a way which is consistent with the promotion of regionalism.

Mission notes that it employs ten licensed wastewater operators and, between these operators, Class A, B, C and D licenses are held. This is distinguished from Alton's Public Works Director who does not hold any license—as either a wastewater operator or collection operator. Mission also points to the testimony of the ED's witness, Kamal Adhikari, who opined that "Mission is more technically capable than Alton." Mission believes this is an accurate statement as Alton does not employ any licensed wastewater operators. Because Mission has trained and licensed operators, and has provided sewer service for roughly 80 years, the ED asserts that Mission has more technical knowledge.

This is a difficult factor to analyze. It is clearly true that Mission has more technical knowledge than Alton. However, the bulk of services to Alton's customers comes from McAllen's licensed staff, and McAllen has a much larger public works department than Mission. Thus, from a practical standpoint, the requested area would receive services from highly qualified technical personnel regardless of whether Alton or Mission is certificated. And, connecting the requested area into McAllen's larger wastewater treatment system is consistent with regionalization policies. Overall, in light of these considerations, the ALJ concludes that Alton and Mission are equal on this factor. However, the Commission may find it more appropriate to only compare Alton's knowledge to Mission's knowledge in evaluating this criterion. If so, Mission clearly has the greater technical knowledge and ability.

3. Ownership Accountability

Alton argues that, while it does not own a treatment plant and is not responsible for the day-to-day operation of most of its sewer facilities, Alton is accountable as an owner of its system to insure the wastewater is properly treated for disposal. Alton notes it does own its own collection system and the legal right to the treatment capacity in McAllen's wastewater treatment plant. Alton argues that any reading of the term "ownership accountability" that values an applicant who has chosen to regionalize less than one that owns its own facilities is not consistent with the legislative policy of regionalization. As such, Alton argues that the Commission should not set a precedent that values cities that own their own facilities over those that use a larger city's facilities.

Mission argues it has ownership accountability as it owns its own wastewater treatment plant. By owning its own plant, Mission asserts it is responsible for the duties associated with maintaining and overseeing the treatment plant. Mission argues because Alton uses McAllen's treatment plant, it relies on McAllen to perform these duties and, accordingly, does not have "ownership accountability." The ED agrees with Mission.

Although the ALJ recognizes the potential inconsistency with regionalization policies, a straightforward reading of the term "ownership accountability" favors Mission, because it does have full ownership and control over its entire wastewater system, including treatment facilities. In contrast, Alton has very limited control, basically extending only to its collection system, but not to any treatment facilities. Thus, this factor favors Mission.

4. Staffing and Organization

Alton argues it is unnecessary to have a large staff for its system because of the agreement with McAllen, whose operators perform the daily oversight and maintenance of the system. Alton's City Manager and Assistant City Manager simply oversee the City's budget and the financial aspects of providing wastewater service. Alton contends that, despite the ED's suggestion that Alton is less capable than Mission because it is smaller in size, there is no evidence to suggest that size alone is

linked to the financial, managerial or technical capability for servicing an area. Alton asserts that, other than evidence of the size of Mission, there is no evidence as to how Mission operates its system, how its system is managed, who makes decisions, or how decisions are made. Because of this, Alton argues that the record provides no basis for finding that Mission is more qualified in regard to staffing and organization.

Mission disagrees, and contrasts Alton's lack of any licensed wastewater operators to Mission's ten licensed operators. Mission notes it employs 128 employees in the public works department, 12 of which are at the treatment plant. Further, Mission has a finance department of eight employees and one Financial Director. Further, in regard to the city governments on the whole, Mission notes that Alton has a total of 43 staff members, while Mission has 627 employees. Mission alleges that these staffing numbers show that Mission is more qualified in regard to staffing and organization. The ED agrees.

Ultimately, the ALJ agrees with the ED that Mission is more qualified when it comes to staffing and organization. Although Alton relies on McAllen for service, the actual overall management of its sewer operations is conducted by Alton's city staff.[40] In this regard, Mission has a distinct advantage, having a much larger financial staff and public works department. While size alone does not guarantee better staffing and organization, in the absence of evidence to the contrary it is an indicator of a greater wealth of knowledge and experience. Because nothing in the record indicates that Mission's staff is incompetent in any way, the ALJ concludes it is reasonable to find that Mission's much larger staff and organization makes it better suited to properly operate and maintain effective sewer service operations.

5. Revenue Sufficiency, Credit Worthiness, Fiscal Management and Controls

For the most part, the financial stability of each city has been addressed above in Section B. However, the ALJ offers some additional analysis here to supplement that discussion.

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[40] Which auditors have found to have past deficiencies in their collection operations—as evidence by the fact that they had 300 accounts receiving service without being billed in the past.

The ED argues Mission is stronger in regard to these criteria. The ED claims that Alton's utility rates are insufficient to cover its utility expenses. Moreover, Mission's creditworthiness (with a currently known and acceptable bond rating) is better than Alton's (which has no known bond rating or other credit ranking). Coupled with other information on the unrestricted fund balance and debt service coverage of both applicants, this leads the ED to find Mission more financially capable.

Alton acknowledges that it does not have a credit rating, but argues that it will still be able to obtain funding to expand its service to the requested area. Alton points out that TWDB has twice invited Alton to apply for funding and Alton has obtained funding from TWDB in the past. Alton asserts that it runs annual audits to ensure controls are in place and maintained. All past accounting deficiencies have been noted and corrected. Alton argues Mission has not performed any financial feasibility analysis to determine its ability to extend service to the area. Alton also claims Mission has not completed a rate study in over ten years.

Alton argues the ED's reliance on a two-year-old audit (from 2007-2008) is misplaced and unreasonable, given the steps Alton has taken to strengthen its financial position and correct past deficiencies. Alton notes that the audit relied on by the ED was completed prior to Alton's rate changes and the inclusion of 300 accounts for collection on its sewer system. Alton argues the deficiencies the ED points to have been addressed to the satisfaction of Alton's auditor and that this information has been ignored by the ED. Alton argues that Mission is lacking the necessary studies and analysis to be able to properly evaluate Mission's financial capabilities.

Mission claims that its financial information shows it to be much more solid than Alton. Mission alleges it has the capacity to fund the expansion project into the proposed area, but also states it intends to investigate funding alternatives to find the most financially cost effective method of bringing service to the area. In support of its creditworthiness, Mission states it has a debt to equity ratio of 0.55-to-1. Part of its fiscal management, Mission states, is a policy of maintaining three months of operating reserves, whereas Alton lacks an emergency fund, as Mr. Garza testified. Further, Mission argues that Alton's rate increases are not enough to meet Alton's expenses. While Mission will benefit from the economies of scale, Alton's contract with McAllen means it is unable

to benefit from any economies of scale because it has to pay McAllen directly for all additional wastewater treatment. Finally, Mission asserts it has stable financial controls because its financial director has been employed by Mission for over ten years.

Ultimately, as discussed previously, the ALJ finds that Mission is more financially stable than Alton. Further, in regard to the particular criteria of revenue sufficiency, creditworthiness, and fiscal management and controls, the ALJ finds that Mission is stronger. First, Mission's bond rating is healthy, whereas Alton has no known credit rating. Second, Mission's sewer operation provide enough revenue to allow it to transfer $1.5 million from its sewer fund to its general operations. At best, Alton has only recently had sufficient revenue to cover its sewer expenses. Third, there are no known accounting concerns with Mission's financial statements, whereas Alton's auditors have noted prior significant deficiencies. All of these factors weigh in favor of Mission.

6. Compliance History

Neither Alton nor Mission has any negative compliance history. Based on this, the ED finds the two applicants to be equal as to this criterion. The ALJ agrees.

7. Planning Reports or Studies by the Applicant to Serve the Proposed Area

Alton claims Mission has no planning report for providing service to the proposed area, whereas Alton has prepared a Project Strategic Plan and Financial Feasibility and Affordability Analysis. Mission claims both cities have planning studies or reports to service the proposed area. While Alton has its Project Strategic Plan, Mission has a preliminary proposed layout of a collection system in the proposed area and how it connects with Mission's existing sanitary sewer collection system. Mission also has a map of its existing sanitary system with a path to the wastewater treatment plant and a cost estimate.[41]

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[41] *See, e.g.*, Mission Ex. 4 and attachments.

The ED finds Alton to be superior on this criterion. Alton has prepared studies and reports on the proposed area while Mission has not submitted any studies or reports into evidence. Although Mission has prepared some plans, Alton has invested much more time and effort into analyzing its ability to provide service and has taken the steps to obtain funding through TWDB for service to the area. It has hired a consultant who prepared rate studies and feasibility studies for the area. It has submitted applications to TWDB and obtained preliminary indications that the project would be eligible for grants and/or loans. It filed its CCN application 10 months prior to Mission. Based on all of this evidence, the ALJ agrees with the ED and concludes that Alton has shown greater efforts in planning to provide service to the requested area than Mission.

V. CONCLUSION

In light of all of the criteria discussed above, the ALJ finds that the factors set out in statute and Commission rules favor granting the CCN amendment application of Mission. Although Alton has shown greater effort in planning for and trying to provide service to the requested area,[42] Mission has shown itself to have more financial ability and greater technical knowledge and ability to provide service. Further, Mission has greater ownership control of its system and greater control over the area in question, since it is in Mission's ETJ. The ED's independent analysis has reached this same conclusion. Consistent with his analysis above, the ALJ recommends that the Commission grant the CCN application of Mission and deny the CCN application of Alton. The findings of fact and conclusions of law supporting the ALJ's recommendations herein are set out in a separate proposed final order that is being sent to the Commission along with this PFD.

SIGNED July 13, 2010.

CRAIG R. BENNETT
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

[42] To the extent the Commission has concerns about Mission's actual intention of providing service to the requested area, it could require Mission to begin the provision of service within a defined period of time or else be subject to decertification, upon application by another retail utility such as Alton. However, this has not been briefed by the parties and the ALJ makes no such recommendation at this time.

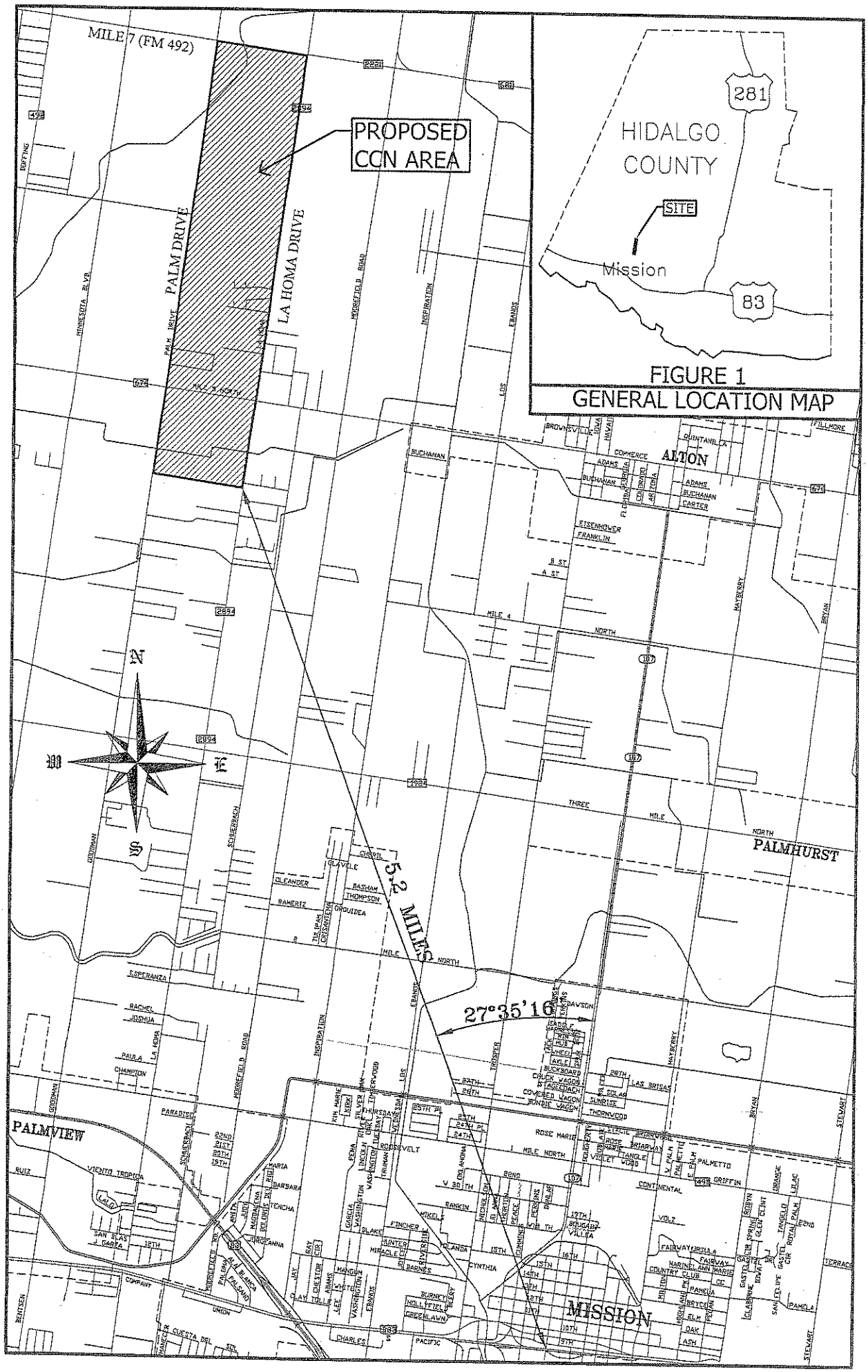
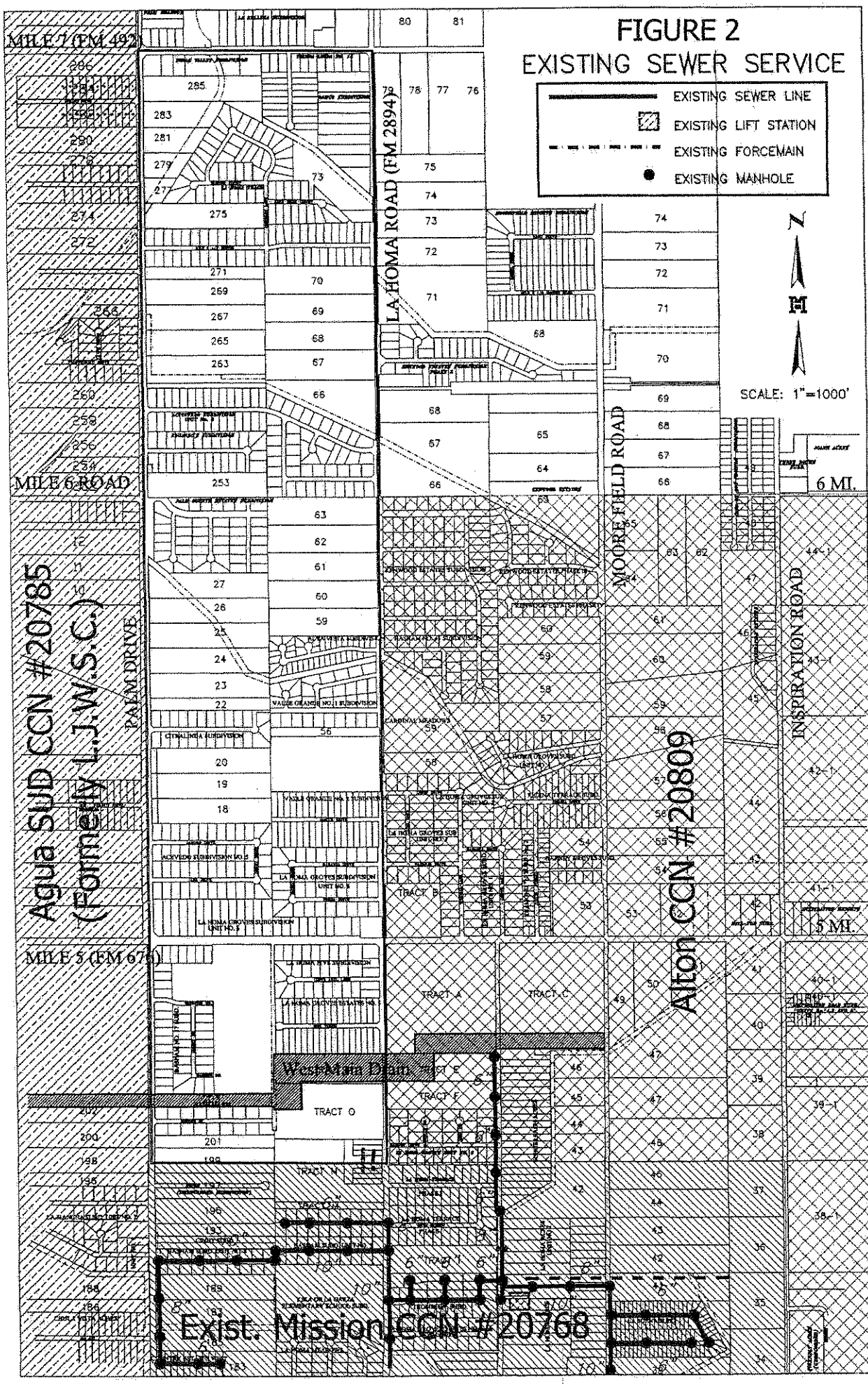


FIGURE 1
GENERAL LOCATION MAP

ATTACHMENT A



ATTACHMENT B

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

AN ORDER granting the Application of the City of Mission to Amend Sewer Certificate of Convenience and Necessity (CCN) No. 20768 in Hidalgo County, Texas; SOAH Docket No. 582-09-3548; TCEQ Docket No. 2009-0350-UCR; and denying the Application of the City of Alton to Amend Sewer Certificate of Convenience and Necessity (CCN) No. 20809 in Hidalgo County, Texas; SOAH Docket No. 582-08-3825; TCEQ Docket No. 2008-0955-UCR

On _____, 2010, the Texas Commission on Environmental Quality (Commission or TCEQ) considered the application of the City of Mission to amend Sewer Certificate of Convenience and Necessity (CCN) No. 20768 in Hidalgo County, Texas. At the same time, the Commission also considered the application of the City of Alton to amend Sewer Certificate of Convenience and Necessity (CCN) No. 20809 in Hidalgo County, Texas.

Craig R. Bennett, an Administrative Law Judge (ALJ) with the State Office of Administrative Hearings (SOAH), conducted preliminary hearings on the applications on August 25, 2008, and on July 14, 2009, and a consolidated contested case hearing on the merits of the dueling applications on February 23-26, 2010. ALJ Bennett prepared a proposal for decision (PFD), which recommended that the Commission approve the application of the City of Mission and deny the application of the City of Alton. The following parties were named and participated in this proceeding: the Executive Director (ED) of the Commission; the City of Mission; and the City of Alton.

After considering the ALJ's Proposal for Decision and the evidence and arguments presented, the Commission makes the following Findings of Fact and Conclusions of Law:

I. FINDINGS OF FACT

Procedural History for Alton's Application

1. The City of Alton (Alton) is a retail public utility holding Sewer Certificate of Convenience and Necessity (CCN) No. 20809 in Hidalgo County, Texas.

2. Alton has applied to the Commission to amend its sewer CCN number 20809 to provide sewer service in Hidalgo County, Texas.

3. Alton's application was initially filed on January 31, 2008, and deemed administratively complete on March 7, 2008.

4. Notice of the application was published in the *Progress Times*, a newspaper of general circulation in Hidalgo County, Texas, on April 4 and 11, 2008.

5. Notice of the application was mailed by Alton on April 4, 2008, to municipalities and neighboring utilities providing similar service within two miles of the area for which certification was sought, and on April 7, 2008, to landowners in the requested area.

6. Notice of the public hearing on the application was mailed on July 24, 2008, by the Chief Clerk of the Commission to Alton and all interested parties.

7. A preliminary hearing was held on August 25, 2008. Designated as parties at the preliminary hearing were Alton; the ED; and the City of Mission (Mission).

Procedural History for Mission's Application

8. Mission is a retail public utility holding Sewer CCN No. 20768 in Hidalgo County, Texas.

9. Mission has applied to the Commission to amend Sewer CCN number 20768 to provide sewer service to the same area in Hidalgo County, Texas, that is the subject of Alton's application.

10. Mission's application was filed on January 31, 2008.

11. Notice of the application was published in *The Monitor*, a newspaper of general circulation in Hidalgo County, Texas, on January 27 and February 3, 2009.

12. Notice of the application was mailed by Mission on January 29, 2009, to municipalities and neighboring utilities providing similar service within two miles of the area for which certification was sought, and to landowners in the requested area.

13. Notice of the public hearing on the application was mailed on June 11, 2009, by the Chief Clerk of the Commission to Mission and all interested parties.

14. A preliminary hearing was held on July 14, 2009. Designated as parties at the preliminary hearing were Mission; the ED; and Alton.

Joint Procedural History

15. On July 14, 2009, the ALJ granted Mission's motion to consolidate its application with the proceeding involving the application by Alton, because Alton and Mission sought CCN amendments for an overlapping area.

16. On July 14, 2009, the parties were given notice of the date, place, and time of the hearing on the merits.

17. The consolidated hearing on the merits in the two dockets was held on February 23-26, 2010. The record closed on May 14, 2010.

Description of the Requested Area

18. The requested area is located in Hidalgo County, Texas, and is generally bounded on the north by FM 2221 (Mile 7 North Road); on the west by Bentsen Palm Boulevard; on the south by an irrigation canal between Basham Subdivision No. 37 and Basham No. 34; and on the east by La Homa Road.

19. The total area sought to be served by Alton is 819 acres, and includes an estimated 453 potential customers.

20. The total area sought to be served by Mission is 845 acres, and includes an estimated 722 potential customers.

21. The requested area is located approximately 2.4 miles west of downtown Alton, outside of its city limits and its extra-territorial jurisdiction (ETJ).

22. The requested area is approximately 5.2 miles from downtown Mission and is located within it's ETJ.

23. The requested area is immediately adjacent to the certificated service areas of both Alton and Mission.

24. Water service is provided to the requested area by the Sharyland Water Supply Corporation.

25. The requested area contains many substandard lots and colonias.

Description of Alton and its Facilities

26. Alton is a municipality with less than 10,000 residents located in Hidalgo County, Texas.

27. Alton provides sewer service to approximately 2,800 customers, and has an interlocal agreement under which it obtains services from the City of McAllen (McAllen).

28. Alton owns its wastewater collection system, and transports sewage through its collection lines to 10 wastewater lift stations and a 36-inch trunk line that connects to a main lift station.

29. At the main lift station, Alton's sewage is metered by McAllen, pumped into McAllen's collection system, and transported to McAllen's North Wastewater Treatment Plant for treatment.

30. Alton currently has approximately 1.023 million gallons per day (MGD) purchased sewage capacity from McAllen, and it has the ability to expand its purchased capacity up to a total of 1.922 MGD.

31. McAllen is currently expanding its North Wastewater Treatment Plant from 6.0 MGD to 18.0 MGD capacity. McAllen has 60 licensed wastewater operators, and these operators are responsible for the operation and maintenance of Alton's collection system in addition to McAllen's system.

32. Alton's public works crews provide only basic inspection and repair services for the system; otherwise, most services are provided by McAllen.

Description of Mission and its Facilities

33. Mission is a municipality with approximately 67,119 residents located in Hidalgo County, Texas.

34. Mission operates its own wastewater system with a wastewater treatment plant capacity of 9.0 MGD. Currently, Mission uses approximately 6.2 MGD of its capacity, leaving roughly 2.8 MGD available for expansion.

35. Mission employs its own licensed wastewater treatment operators, who have full-time responsibility for oversight of Mission's system.

36. Mission has approximately 128 employees in its Public Works Department, 12 of whom work at the wastewater treatment plant. Of those, nine employees work in maintenance and are responsible for the maintenance of Mission's wastewater treatment system.

Financial, Managerial and Technical Capabilities of the Applicants

37. A 2008 audit showed that Alton had a reduction in net assets of $872,000, a reduction in cash and cash equivalents of approximately $395,000, and a reduction in net revenues of more than $167,000 between 2007 and 2008.

38. In part as a result of its reduced revenues, Alton had to draw down its utility fund cash accounts by $395,235 in the 2007-2008 fiscal year.

39. Prior to 2008, there were approximately 300 accounts receiving sewer service that were not being billed for service by Alton. Those accounts have since been added and Alton anticipates its utility revenues to increase by $200,000 going forward.

40. Alton retained consultant Jeff Snowden, who prepared a feasibility study analyzing Alton's ability to provide sewer service to the requested area. Mr. Snowden concluded that Alton could financially handle the provision of new service to the requested area and, when coupled with rate increases, such a move would strengthen Alton's financial situation over the next ten years.

41. The rate analysis by Mr. Snowden has numerous deficiencies.

a. The analysis omitted the full capacity payment that Alton is required to make to McAllen in the next few years, thus leaving annual expenses understated and cash flow projections overstated by approximately $75,000. This would have a significant impact on available cash, even if it does not cause it to become negative.

b. The analysis included an assumption that Alton would receive 30% of the funding for the capital improvement project to provide new service from the Texas Water Development Board (TWDB), thus requiring Alton to fund the remaining 70%. However, if Alton does not obtain the funding, it would be required to obtain loans for the full 100%, which would further erode Alton's ending available cash balance.

c. The analysis included a 100% collection rate from sewer customers, but Alton's collection rate is approximately 95%. Thus, the analysis further overstated projected revenues by approximately $35,000 the first year (and a greater amount for subsequent years that have rate increases).

d. The analysis included the requested area, with the infrastructure cost being paid for fully by low-interest loans or grants. Thus, it is difficult to assess Alton's financial situation without the inclusion of the requested area.

42. Alton's audit for 2008 understated depreciation (thus understating expenses) by $351,000.

43. Alton's auditors raised at least two serious deficiencies from the 2008 audit, including high-risk findings that (1) significant year-end adjustments were necessary for Alton's financial statements to be in accordance with generally accepted accounting principles, and monthly and year-end statements were not an accurate reflection of the actual financial position of the city; and (2) an actual inventory of Alton's capital assets had not been performed recently, thus raising the question of whether the city's reported capital assets reflected its actual assets.

44. Alton's financial statements indicate that, for fiscal year 2008-2009, Alton's sewer expenses were $832,678 and its revenue was $865,038.

45. If its application is granted, Alton's plans are for it to fund the expansion of its system by obtaining 30% of the funding in grants from the TWDB, and then financing the remaining 70% through low interest loans.

46. The processing of Alton's application for funding from TWDB cannot proceed until Alton has obtained the CCN for the requested area.

47. Mission has met its debt service coverage ratio nine out of the last ten years, and has more than $6 million in its unrestricted fund balance to fund the expansion project to provide service to the requested area.

48. Mission's credit rating is A3, which is upper medium grade.

49. Mission's sewer operations produce a net revenue gain for the city, as $1.5 million has been transferred from Mission's sewer fund to its general fund on a recurring basis.

50. Including expansion to the requested area, Mission has potential expansion projects costing more than $25.8 million anticipated or planned, but it does not appear that all of those projects are required.

51. Even if it undertakes approximately $25.8 million in expansion projects, Mission's free cash would still exceed its debt service, thus allowing it to service its debt even though it would be out of compliance with its debt covenant requirement of a 1.25 ratio.

52. Mission has provided adequate and continuous sanitary sewer service for almost 80 years.

53. Mission has the financial capability to provide adequate and continuous service to the requested area.

54. Both Mission and Alton have the managerial and technical capability to provide adequate and continuous service to the requested area.

Adequacy of Service in the Requested Area and the Need for Service

55. Currently there is no retail service available in the requested area.

56. Residents in the requested area are served by septic systems, some of which are on substandard lots.

57. The requested area includes three colonias along the Texas-Mexico border. Colonias are residential areas lacking one or more of the basic living necessities, which include wastewater systems meeting state standards.

58. The requested area is experiencing rapid growth in denser areas. Septic systems may not fit in these denser areas.

59. The colonias do not have room for septic systems for all residents, and thus do not have the ability to meet the sewer service needs of the residents in a manner that ensure the protection of public health and the environment.

60. Current wastewater treatment in the requested area is not adequate.

61. Centralized sewer will be necessary because most of the development will be dense developments that cannot be supported by septic systems.

62. Because of potential health and environmental concerns for the requested area, the provision of adequate sewer service is a legitimate need as the area continues to grow.

Effect of Granting the CCN on the Recipient, Landowners, and Other Retail Public Utilities

63. If the CCN is granted to either Alton or Mission, landowners in the area will be positively affected as septic systems on the substandard lots will be decommissioned and centralized sewer service will be provided.

64. If the CCN is granted to either Alton or Mission, landowners of undeveloped land will be able to develop their land more densely and this will increase chances of commercial development—as some businesses require centralized sewer service.

65. Only Mission has protested Alton's CCN application, and only Alton has protested Mission's CCN application.

66. No other retail public utility has indicated a willingness to provide sewer service to the requested area.

67. No other retail public utility, other than Alton, will be affected if Mission receives the CCN, and only Mission is affected if Alton receives the CCN.

Ability of the Applicants to Provide Adequate Service

68. Mission has historically provided, and is currently providing, adequate sewer service in its CCN territory.

69. Alton is not currently serving all of its certificated area. Specifically, residents within Alton's city limits located between Moorfield Road and LaHoma Road do not currently have access to sewer service. In total, there are approximately nine different pockets within Alton's CCN boundaries that are not currently able to receive sewer service from Alton.

70. Other than as noted above, Alton has historically provided, and is currently providing, adequate sewer service in its CCN territory.

71. Alton and Mission can both provide adequate service to the requested area.

72. Because Mission owns its own complete treatment system, it has greater control over the provision of service than Alton.

The Feasibility of Obtaining Service from an Adjacent Retail Public Utility

73. Alton's planning for providing service to the proposed area began in 2007 and includes a process to implement its plan.

74. Alton prepared the information necessary for seeking funding from the TWDB to provide service to the area, and filed its CCN application 10 months before Mission.

75. Both Alton and Mission are adjacent to the requested area and, therefore, it is feasible for either to serve the area.

76. There is no evidence of any other retail public utility other than Mission or Alton who is willing and able to provide service to the requested area.

77. Mission and Alton currently appear to be the only retail public utilities interested and able to provide service to the area.

Environmental Integrity

78. The environmental integrity of the requested service area will be improved by the provision of a centralized sewer system by either Alton or Mission.

79. Alton has provisions for storm water run-off and constructs its facilities to limit the environmental impact during construction.

80. Alton has a pretreatment ordinance which ensures hazardous pollutants are properly treated and the buildup of grease in the system is minimized. Industrial customers of sewer service would be subject to the requirements of this ordinance.

81. Both Alton and Mission plan to decommission the substandard septic systems and use gravity collection lines, arguably eliminating potential backups and overflows of septic tanks (which can create health hazards).

82. The construction necessary for providing service to the requested area will cause a temporary disturbance to the environmental integrity regardless of which applicant receives the CCN.

83. Both applicants will use substantially similar systems to provide wastewater service to the requested area.

The Probable Improvement of Service or Lowering of Costs to Consumers in the Area

84. Currently there is no centralized sewer service in the requested area, and either proposed project by Alton or Mission would bring the first integrated sewer service to the area.

85. Expected septic tank costs over 20 years is approximately $35 per month.

86. A customer using 6,000 gallons per month would pay $21.07 per month under Alton's proposed rate structure, and $23.85 under Mission's rate structure, if metered. If unmetered, a customer under Mission's rate structure would pay a flat fee of $26.00 regardless of usage.

87. Granting the CCN to either Alton or Mission would lower costs to consumers in the requested area.

88. Granting either Alton's or Mission's application would result in the improvement of service and the lowering of costs to consumers in the requested area.

Effect on Land in the Requested Area

89. The availability of sewer service is more environmentally protective than individual septic tanks, and provides for greater uses of the land in the area.

90. Granting the CCN to either Alton or Mission would have the same positive result to the land.

Comparative Assessment of the Applicants' Financial, Managerial and Technical Capabilities

Infrastructure Adequacy

91. There is no centralized sewer system in the requested area and no adequate infrastructure.

92. Neither Alton nor Mission currently has infrastructure in the proposed area.

93. Both Alton and Mission would have to build significant infrastructure to serve the requested area, and the anticipated cost to each is relatively similar.

94. There are no major impediments to the ability of either Alton or Mission to build out the necessary infrastructure for service to the requested area.

Technical Knowledge of the Applicants

95. Alton relies on its Interlocal Agreement with McAllen to give it the required technical knowledge to provide adequate service.

96. McAllen has many trained and licensed wastewater operators and has a larger public works staff than does Mission.

97. Alton's Public Works Director who does not hold any license—as either a wastewater operator or collection operator—and Alton employs no licensed wastewater operators.

98. Mission employs approximately 10 licensed wastewater operators and, between these operators, Class A, B, C and D licenses are held.

99. Mission has trained and licensed operators and has provided sewer service for roughly 80 years.

Ownership Accountability

100. Alton does not own its own wastewater treatment plant, but does own its own collection system and has a contractual right to treatment capacity in McAllen's wastewater treatment plant.

101. Mission has full ownership and control over its entire wastewater system, including treatment facilities.

Staffing and Organization

102. McAllen's utility staff perform the daily oversight and maintenance of Alton's wastewater treatment system, and Alton's City Manager and Assistant City Manager simply oversee the City's budget and the financial aspects of providing wastewater service.

103. Alton has no licensed wastewater operators, whereas Mission has ten licensed operators.

104. Mission employs 128 employees in the public works department, 12 of which are at the treatment plant.

105. Mission has a finance department of eight employees and one Financial Director.

106. In regard to the city governments on the whole, Alton has a total of 43 staff members, while Mission has 627 employees.

107. Mission's much larger staff and organization makes it better suited to properly operate and maintain effective sewer service operations.

Revenue Sufficiency, Credit Worthiness, Fiscal Management and Controls

108. Alton has no bond rating.

109. Mission's bond rating is A3.

110. Mission's sewer operations provide enough revenue to allow it to transfer $1.5 million from its sewer fund to its general operations.

111. For the few service years prior to 2008, Alton's sewer revenues were generally insufficient to cover its sewer expenses. For 2008-2009, Alton had sufficient revenue to cover its sewer expenses.

112. There are no known significant accounting concerns with Mission's financial statements.

113. Alton's auditors have noted prior significant deficiencies in its audits, as recently as the fiscal year prior to the hearing.

Compliance History

114. Neither Alton nor Mission has any negative compliance history.

Planning Reports or Studies by the Applicant to Serve the Proposed Area

115. Alton has prepared a Project Strategic Plan and Financial Feasibility and Affordability Analysis regarding its ability to provide service to the requested area. Mission has not prepared a similarly extensive report.

116. Alton has invested more time and effort than Mission into analyzing its ability to provide service and has taken the steps to obtain funding through TWDB for service to the area.

117. Alton has submitted applications to TWDB and obtained preliminary indications that the expansion project for service to the requested area would be eligible for grants and/or loans.

118. Alton filed its CCN application 10 months prior to Mission.

CONCLUSIONS OF LAW

1. The Commission has jurisdiction over this case under TEX. WATER CODE ANN. Ch. 13.

2. The State Office of Administrative Hearings (SOAH) has jurisdiction over all matters relating to the conduct of a hearing in this proceeding, including the preparation of a proposal for decision with findings of fact and conclusions of law, pursuant to TEX. GOV'T CODE ANN. Ch. 2003.

3. Alton and Mission each published notice and provided notice to neighboring utilities and affected parties, as well as all landowners in the requested area as required by TEX. WATER CODE ANN. § 13.246 and 30 TEX. ADMIN. CODE §291.106.

4. Parties received proper and timely notice of the hearing. TEX. GOV'T CODE ANN. § 2001.051 and 2001.052.

5. Mission has met all substantive criteria for granting a sewer CCN amendment in Hidalgo County, Texas, as set forth in TEX. WATER CODE ANN. §§ 13.241, 13.244, and 13.246 and 30 TEX. ADMIN. CODE § 291.102.

6. Mission is more financially, managerially, and technically capable than Alton of providing adequate and continuous service to the requested area.

7. Issuing the amended CCN for sewer service to Mission is necessary for the service, accommodation, convenience, or safety of the public.

8. Mission's sewer CCN amendment should be granted for the entire area set out in its application and published notice.

9. In light of the granting of Mission's sewer CCN amendment, Alton's sewer CCN amendment should be denied.

NOW, THEREFORE, BE IT ORDERED BY THE TEXAS COMMISSION ON ENVIRONMENTAL QUALITY THAT:

1. The application of the City of Mission to amend its Certificate of Convenience and Necessity No. 20768 in Hidalgo County, Texas is GRANTED.

2. Certificate of Convenience and Necessity No. 20768 shall include the area described in the application and published notice.

3. The application of the City of Alton to amend its Certificate of Convenience and Necessity No. 20809 in Hidalgo County, Texas is DENIED

4. The Chief Clerk of the Texas Commission on Environmental Quality shall forward a copy of this Order to all parties.

5. The effective date of this Order is the date the Order is final, as provided by 30 TEX. ADMIN. CODE § 80.273 and TEX. GOV'T CODE ANN. § 2001.144.

6. The Executive Director of the Texas Commission on Environmental Quality shall amend the official maps to reflect this decision.

7. If any provision, sentence, clause, or phrase of this Order is for any reason held to be invalid, the invalidity of any portion shall not affect the validity of the remaining portions of the Order

Issue Date:

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

Bryan W. Shaw, Ph.D., Chairman for the Commission