

State Office of Administrative Hearings



Cathleen Parsley
Chief Administrative Law Judge

May 11, 2010

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

**Re: SOAH Docket No. 582-09-6111; TCEQ Docket No.2009-0324-UCR;
Application under Water Code Section 13.255 from the City of Karnes City
to decertify a portion of Certificate of Convenience and Necessity No. 10570
from El Oso Water Supply Corporation in Karnes 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 **June 1, 2010**. Any replies to exceptions or briefs must be filed in the same manner no later than **June 11, 2010**.

This matter has been designated **TCEQ Docket No. 2009-0324-UCR; SOAH Docket No. 582-09-6111**. 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,

A handwritten signature in cursive script that reads "Sharon Cloninger".

Sharon Cloninger
Administrative Law Judge

SC/lh
Enclosures
cc: Mailing List

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AGENCY: Environmental Quality, Texas Commission on (TCEQ)
STYLE/CASE: CITY OF KARNES CITY
SOAH DOCKET NUMBER: 582-09-6111
REFERRING AGENCY CASE: 2009-0324-UCR

STATE OFFICE OF ADMINISTRATIVE
HEARINGS

ADMINISTRATIVE LAW JUDGE
ALJ SHARON CLONINGER

REPRESENTATIVE / ADDRESS

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TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

xc: Docket Clerk, State Office of Administrative Hearings

SOAH DOCKET NO. 582-09-6111
DOCKET NO. 2009-0324-UCR

APPLICATION UNDER WATER CODE	§	BEFORE THE STATE OFFICE
SECTION 13.255 FROM THE CITY OF	§	
KARNES CITY TO DECERTIFY A	§	
PORTION OF CERTIFICATE OF	§	
CONVENIENCE AND NECESSITY	§	OF
NO. 10570 FROM EL OSO WATER	§	
SUPPLY CORPORATION	§	
IN KARNES COUNTY	§	ADMINISTRATIVE HEARINGS

PROPOSAL FOR DECISION

The City of Karnes City (City) has applied to decertify a portion of Certificate of Convenience and Necessity (CNN) No. 10570 from El Oso Water Supply Corporation (El Oso). El Oso challenges the authority of the Texas Commission on Environmental Quality (TCEQ or Commission) to consider the single certification application of the City. El Oso claims the Commission may not consider the application because the certification at issue was the subject of a dismissal with prejudice in a 1994 order (1994 Order) issued by the Texas Natural Resources Conservation Commission (the TCEQ's predecessor). Specifically, El Oso disputes whether the 60-acre tract (Tract) that was the subject of the City's TEX. WATER CODE ANN. § 13.255 (Section 13.255) application and the 1994 Order—issued at the request of the City and El Oso after they reached a written settlement agreement—may be reconsidered for decertification under the City's current Section 13.255 application.

In Order No. 8, issued March 5, 2010, the Administrative Law Judge (ALJ) sustained El Oso's jurisdictional challenge after determining that the Commission is not authorized by statute to reconsider the 1994 Order. The ALJ further ruled that the changed circumstances claimed by the City are inadequate to support its argument that *res judicata* does not apply to the 1994 Order.

I. PROCEDURAL HISTORY

The City notified El Oso on May 15, 2008, of its intent to file a Section 13.255 application for single certification to provide water service to all of the territory within its corporate limits currently served by El Oso under CCN No. 10570.¹ In the ensuing 180 days, the City and El Oso did not agree to revise their 1994 agreement related to the Tract. At the October 28, 2009 preliminary hearing, the parties informed the ALJ that they had reached a settlement as to all acreage listed in the City's application except for the Tract. Accordingly, an unopposed oral motion to remand to the Executive Director (ED) the portion of the application unrelated to the Tract was granted on the record.

On December 21, 2009, in response to El Oso's challenge to TCEQ's jurisdiction, the City submitted its Brief in Support of its Application for Single Certification. The City asked the ALJ to take official notice of the Proposal for Decision and Order issued In the Matter of the Complaint of North Collin Water Supply Corporation against the City of Melissa, Texas (SOAH Docket No. 582-02-3110; TCEQ Docket No. 2002-0232-UCR). The ALJ took the requested official notice.²

On January 13, 2010, the ED and El Oso submitted replies to the City's brief. On February 2, 2010, the City filed its response to the replies. On March 1, 2010, the parties presented oral argument on the issue. Order No. 8 sustaining El Oso's jurisdictional challenge was issued March 5, 2010.

¹ See August 21, 2008 letter from the City to the Texas Water Development Board, attached to City's Reply Brief.

² The ALJ agrees with the ED that the PFD contains an excellent discussion of Section 13.255, but finds that the facts underlying the discussion are not on point as far as the issue at hand. See ED Brief at 4.

II. DISCUSSION

In this case of first impression,³ the issue to be decided is whether the Commission may disturb the 1994 Order and consider the City's application for single certification of the Tract, or in the alternative, consider the City's application as a new one unrelated to the 1994 Order, because of changed circumstances.

A. Background Surrounding 1994 Order

Since issuance of the 1994 Order, Bluebonnet Nursing and Rehabilitation (Bluebonnet) and the Karnes Correctional Center (Correctional Center) have been built on the Tract. Both are currently El Oso's water customers and both have requested water service from the City.⁴

When the City sought single certification of the Tract in 1994—specifically to serve Bluebonnet, which was under construction—the water available to it under its agreement with El Oso, who supplied the City with water, was insufficient to meet the Commission's minimum design requirements for the anticipated number of connections. Under Section 13.255(m), the Commission could not grant single certification to a municipality that could not meet minimum design standards.⁵ The City attempted to augment its water supply by drilling wells. When the augmentation efforts were unsuccessful, the City did not withdraw its application without prejudice as permitted by Section 13.255(h).⁶

³ According to the ED, parties to a Section 13.255 agreement have never before sought to re-open the matter, particularly one dismissed with prejudice. ED Brief at 3-4.

⁴ City exhibits 4, 5, and 7 at 3-9.

⁵ Section 13.255(m) states that the Commission shall deny an application for single certification by a municipality that fails to demonstrate compliance with the Commission's minimum requirements for public drinking water systems.

⁶ Under Section 13.255(h), a municipality may dismiss an application for single certification without prejudice at any time before a judgment becomes final provided the municipality has not taken physical possession of the retail public utility's property or made payment for such a right.

Instead, the City entered into the written settlement agreement with El Oso that underlies the 1994 Order. A term of the agreement is that El Oso would not seek reimbursement of \$50,000 in legal fees incurred opposing the City's single certification application in exchange for the City's agreement that its application to provide water service to the Tract would be dismissed with prejudice.

Ronald J. Freeman, the City's attorney involved in the settlement agreement, explained, "El Oso was not willing to allow the City to withdraw its application unless the City paid El Oso its attorney fees and other expenses."⁷ Section 2a of the Compromise and Settlement Agreement provided that the proceeding to remove the Tract from El Oso's certified area would be dismissed with prejudice. The dismissal with prejudice provision from the Compromise and Settlement Agreement was incorporated by the Commission in the 1994 Order.⁸

Since 1994, the City has supplemented its water supply by drilling a well near Falls City and leasing an additional well. The City's water supply is now more than adequate under TCEQ requirements to supply Bluebonnet, the Correctional Center, and other customers within the Tract.⁹

B. Section 13.255 and the Underlying Legislative Bill Analysis

1. Section 13.255

The Commission's authority to consider a city's application for single certification in its incorporated limits is found in Section 13.255. In relevant part, Section 13.255(a) states:

⁷ Pre-filed Testimony of Ronald J. Freeman, City's Ex. 6, at 2.

⁸ See Compromise and Settlement Agreement, City Ex. 2.

⁹ City's Reply Brief at 2-3; pre-filed testimony of Raul H. Garcia, City Ex. 3; and pre-filed testimony of Mayor Don Tymrak, City Ex. 7 at 3-7.

In the event that an area is incorporated or annexed by a municipality, either before or after the effective date of this section, the municipality and retail public utility that provides water or sewer service to all or part of the area pursuant to a certificate of convenience and necessity may agree in writing that all or part of the area may be served by a municipally owned utility, by a franchised utility, or by the retail public utility. . . . The agreement may provide for single or dual certification of all or part of the area, for the purchase of facilities or property, *and for such other additional terms that the parties may agree on. . . .* The executed agreement shall be filed with the commission, and *the commission, upon receipt of the agreement, shall incorporate the terms of the agreement into the respective certificates of convenience and necessity of the parties to the agreement.*¹⁰
[Emphasis added.]

Under subsections (b) and (c) of Section 13.255, if the written agreement provided for in Subsection (a) is not reached within 180 days after the municipality notifies the retail public utility in writing of its intent to provide service to the incorporated area, the municipality shall file an application for single certification with the Commission prior to providing service to the area. The Commission shall grant single certification to the municipality.¹¹

2. H. B. 2035 analysis

Section 13.255 was enacted in 1987 in H.B. 2035. The one-page bill analysis summarizes the purpose of the law as follows:

As proposed, H.B. 2035 allows a city to initiate action to provide utility services to an annexed area. This bill provides for just compensation to a retail public utility that loses property to a city under such action. This bill exempts a municipally-owned utility from the requirement of obtaining a certificate of public convenience and necessity.

¹⁰ See also 30 TEX. ADMIN. CODE (TAC) § 291.120(a).

¹¹ See also 30 TAC § 291.120(b) and (c).

The bill analysis states that Section 13.255 allows a municipality and retail public utility to agree in writing about providing utility service to an incorporated or annexed area.¹²

C. ALJ's Analysis

1. 1994 Order is Valid

The ALJ finds that the 1994 Order is a valid order of the Commission that cannot be disturbed under the express provisions of Section 13.255. When parties such as the City and El Oso reach a settlement, Section 13.255(a) requires the Commission to "incorporate the terms of the agreement into the respective certificates of convenience and necessity of the parties to the agreement." Section 13.255 does not give the Commission authority to modify agreements reached under Section 13.255(a), either at the time the agreements are presented or after CCNs incorporating the terms of an agreement have been issued. The Commission properly issued the 1994 Order and has no authority to reconsider the incorporated terms.

2. Changed Conditions Do Not Warrant Disturbing 1994 Order

But the City claims that it does not seek to re-open the 1994 proceeding; rather, the City states its new Section 13.255 application is based on events occurring after the 1994 application was dismissed.¹³ The City argues that the Texas Supreme Court has repeatedly ruled that a judgment or dismissal with prejudice is *res judicata* only of present and not of future conditions.¹⁴ As far as the ALJ can determine from the pleadings, the primary changed condition relied on by the City is that it now has the capability to provide water service to the Tract in

¹² ED's Brief at 3. Staff further notes that the Commission adopted 30 TAC § 291.120 effective January 5, 2006, to implement Section 13.255.

¹³ City's Reply Brief at 1.

¹⁴ The City cites, among other cases, *City of Lubbock v. Stubbs*, 327 S.W.2d 411, 414(1959).

accordance with TCEQ drinking water standards.¹⁵ Also, the Corrections Center, which seeks City water service, was not constructed until 1995.¹⁶

The ED notes there are no Commission standards as to what constitutes a material change in conditions that would warrant reconsideration of a valid Commission order regarding CCN service areas.¹⁷ Therefore, the ALJ looks to case law for guidance. In *Westheimer Indep. School Dist. v. Brockett*, 567 S.W.2d 780, 787 (Tex. 1978), the Texas Supreme Court held that a “material change of conditions” should be narrowly construed, providing a basis for review in limited circumstances only. The court recognized that “there are aspects of administrative orders which must be treated with flexibility, rather than with the binding effects of *res judicata*.” But the court went on to explain, “[W]henever possible, the courts should support the finality of administrative orders in keeping with the public policy favoring an end to litigation, whether it be in the administrative or judicial process. Continued litigation of issues or piecemeal litigation should be discouraged. Therefore, to constitute material changes of conditions, the allegations must reflect that the changes have intervened since the rendition of the order and *must not constitute issues which might have been raised in the prior hearing* had adequate and diligent research been conducted to discover such facts.” [Emphasis added.]

The only material change in this case—which involves the identical parties and Tract as the 1994 case—is that the City is now able to meet TCEQ requirements for providing water service. When, in 1994, it became apparent that the City could not adequately provide water service, it could have exercised its option under Section 13.255(h) to dismiss its application without prejudice. Instead, to avoid reimbursing EL Oso the \$50,000 in legal fees the retail public utility had incurred in opposing the application, the City entered into a written agreement

¹⁵ Pre-filed testimony of Mayor Don Tymrak, City Ex. 7, at 6, 9-13 and 15. The ALJ notes that the fact that Bluebonnet seeks to switch its water service to the City is not a changed condition. Bluebonnet wanted City water service in 1994, which is why the City filed its first application.

¹⁶ Pre-filed testimony of Mayor Don Tymrak, City Ex. 7, at 9.

¹⁷ ED Brief at 9.

with El Oso; the parties asked the Commission to dismiss with prejudice the issue of provision of water service to the Tract.

The ALJ finds that the City's current ability to provide water service in the Tract is an issue that could easily have been foreseen. The City and El Oso could have included a term in their written settlement agreement allowing the City to re-apply for single certification once its water supply met TCEQ requirements. Or the parties could have agreed that the issue of providing water service to the Tract would be dismissed without prejudice. While it is true that the written agreement contains a provision that the City will pay El Oso \$50,000 in liquidated damages for breach of the agreement should it ever re-apply for single certification of the Tract,¹⁸ the ALJ does not agree with the City's argument that the aforementioned language is evidence that the parties anticipated that the City would someday re-file its Section 13.255 application, and therefore, El Oso has waived any jurisdictional objection to the re-filing.¹⁹ The very language "breach of this Agreement" indicates to the ALJ that El Oso, at least, had no intention of waiving any objection to a future Section 13.255 filing by the City to serve the Tract. The ALJ further notes that the "breach of Agreement" provision was not incorporated by the Commission in the 1994 Order.²⁰

3. The City Did Not Barter Away Its Powers

In addition, the ALJ is not persuaded by the City's assertion that the 1994 City Council bartered away the City's Section 13.255 governmental powers by agreeing to dismissal with prejudice in its settlement with El Oso. The former City Council was exercising one of the governmental powers accorded municipalities under Section 13.255: the opportunity to enter into a written settlement agreement that must be incorporated into its CCN. The 1994 Order does not forever bar the City from proceeding with a Section 13.255 application as to other areas within

¹⁸ Compromise and Settlement Agreement, City Ex. 2 at 3.

¹⁹ City Brief at 5.

²⁰ City Ex. 1.

its incorporated limits. Indeed, at the preliminary hearing in this very matter, the Section 13.255 agreement between the City and El Oso as to all service areas in the application except for the Tract resulted in bifurcation of this proceeding and a remand to the ED.

D. ALJ's Conclusion and Recommendation

The ALJ agrees with the ED's argument that "[t]he dismissal with prejudice in 1994 was at the request of the parties, both sophisticated, both represented by counsel. There is no evidence of obvious mistakes of law regarding the 1994 Order, nor is there evidence of fraud or other fault on the part of either party. The City did not raise timely objections to the 1994 Order, which remains valid."²¹ The ALJ further finds that the changed condition claimed by the City—that it now has an adequate water supply to serve the Tract—is one that could have been foreseen by the parties and addressed in their written settlement agreement, so does not constitute a "material change of condition" under *Westheimer Indep. School Dist. v. Brockette* that would warrant the Commission's reconsideration of which utility should provide water service to the Tract.

For the aforementioned reasons, the ALJ recommends that the Commission find that the 1994 Order may not be disturbed.

SIGNED May 11, 2010.


SHARON CLONINGER
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

²¹ ED Brief at 7.

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY



**AN ORDER Concerning the Application
Under Water Code Section 13.255 from
THE CITY OF KARNES CITY
To Decertify a Portion of Certificate of Convenience and Necessity No. 10570
From El Oso Water Supply Corporation in Karnes County
TCEQ DOCKET NO. 2009-0234-UCR
SOAH DOCKET NO. 582-09-6111**

On _____, the Texas Commission on Environmental Quality (Commission or TCEQ) considered the application of the City of Karnes City (City) to Decertify a Portion of Certificate of Convenience and Necessity (CCN) No. 10570 from El Oso Water Supply Corporation (El Oso) in Karnes County. A Proposal for Decision (PFD) was presented by Sharon Cloninger, Administrative Law Judge (ALJ) with the State Office of Administrative Hearings (SOAH).

The following are parties to the proceeding: the City, El Oso, and the Executive Director (ED) of the TCEQ.

After considering the Proposal for Decision, the Commission makes the following Findings of Fact and Conclusions of Law.

I. FINDINGS OF FACT

1. The City notified El Oso on May 15, 2008, of its intent to file a an application (Application) for single certification to provide water service to all of the territory within its corporate limits currently served by El Oso under CCN No. 10570.

2. In the ensuing 180 days, the City and El Oso did not agree to revise their 1994 agreement related to a 60-acre tract (Tract) within El Oso's CCN area.
3. On July 20, 2009, TCEQ referred the case to SOAH.
4. At the October 28, 2009 preliminary hearing, the parties informed the ALJ that they had reached an agreement as to all acreage listed in the Application except for the Tract and the oral motion to remand to the ED the portion of the Application unrelated to the Tract was granted on the record.
5. At the preliminary hearing, El Oso challenged the jurisdiction of the Commission to consider the Application as to the Tract.
6. On December 21, 2009, in response to El Oso's challenge to the Commission's jurisdiction, the City submitted its Brief in Support of its Application for Single Certification.
7. On January 13, 2010, El Oso and the ED submitted replies to the City's brief.
8. On February 2, 2010, the City filed its response to the replies.
9. On March 1, 2010, the parties presented oral argument on the issue of the Commission's jurisdiction to consider the Application as to the Tract.
10. On March 5, 2010, the ALJ sustained El Oso's jurisdictional objection, finding that the Commission could not reconsider water service to the Tract unless the City and El Oso reached a new agreement and requested a new CCN incorporating that agreement.
11. The Tract was the subject of the City's application for decertification that was dismissed with prejudice by the Commission in a 1994 order (1994 Order).
12. The 1994 Order dismissing the City's application with prejudice was issued at the request of the City and El Oso after they reached a written settlement agreement that El Oso would provide water service to the Tract.

13. On March 5, 2010, the ALJ sustained El Oso's jurisdictional objection.

II. CONCLUSIONS OF LAW

1. Under TEX. WATER CODE ANN. § 13.255, the Commission has jurisdiction over the Application.
2. Under TEX. WATER CODE ANN. § 13.255(a), the Commission has no authority to overturn or reconsider its 1994 Order unless the City and El Oso reach an agreement requesting revision of the terms of the 1994 Order.
3. SOAH has jurisdiction over matters related to the hearing in this matter, including the authority to issue a Proposal for Decision with Findings of Fact and Conclusions of Law, pursuant to TEX. GOV'T CODE ANN. ch. 2003, but has no jurisdiction to hold a hearing on aspects of the Application related to the 1994 Order.

NOW, THEREFORE, IT IS ORDERED BY THE TEXAS COMMISSION ON ENVIRONMENTAL QUALITY, IN ACCORDANCE WITH THESE FINDINGS OF FACT AND CONCLUSIONS OF LAW, THAT:

1. The Commission does not have jurisdiction to overturn or reconsider its 1994 Order.
2. All other motions, requests for entry of specific Findings of Fact or Conclusions of Law, and any other requests for general or specific relief, if not expressly granted herein, are hereby denied.
3. 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.
4. The Commission's Chief Clerk shall forward a copy of this Order to the City and El Oso.

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

ISSUED:

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

**Brian W. Shaw, Ph. D., Chairman
For the Commission**