TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

Protecting Texas by Reducing and Preventing Pollution

March 18, 2024

Laurie Gharis, Chief Clerk
Texas Commission on Environmental Quality
Office of the Chief Clerk (MC – 105)
P.O. Box 13087
Austin, Texas 78711-3087

RE: Ellis Ranch Municipal Utility District No. 1
SOAH Docket No. 582-23-11658; TCEQ Docket No. 2022-1157-DIS

Dear Ms. Gharis:

Enclosed please find a copy of the Executive Director's Exceptions to the Proposal for Decision for the Contested Case Hearing listed above.

If you have any questions, please do not hesitate to call me at (512) 239-4761 or email at kayla.murray@tceq.texas.gov.

Sincerely,

Kayla Murray

Kayla Murray
Staff Attorney
Texas Commission on Environmental Quality
Environmental Law Division

Enclosures

SOAH Docket No. 582-23-11658
TCEQ Docket No. 2022-1157-DIS

Application for the Creation of	**§**	**Before the State Office**
Ellis Ranch	**§**	**Of**
Municipal Utility District No. 1	**§**	**Administrative Hearings**

EXECUTIVE DIRECTOR'S EXCEPTIONS TO THE PROPOSAL FOR DECISION

To the Honorable Commissioners of the Texas Commission on Environmental Quality:

COMES NOW, the Executive Director (ED) of the Texas Commission on Environmental Quality (TCEQ or Commission) and submits these exceptions to the Administrative Law Judges' (ALJs) Proposal for Decision (PFD) and proposed order in the above-captioned matter.

As discussed in detail below, the Executive Director respectfully requests the Commission issue an Order for the creation of Ellis Ranch Municipal Utility District No. 1 as drafted by the Executive Director.

A. INTRODUCTION

On February 26, 2024, the ALJs issued their PFD recommending that the petition to create Ellis Ranch Municipal Utility District No. 1 be denied.[1] The Executive Director respectfully disagrees with the ALJ's decision.

B. LEGAL STANDARD

Texas Water Code § 54.021(a) provides that the Commission shall grant a petition for the creation of a Municipal Utility District (MUD) if the Commission finds that the petition conforms to the requirements of Section 54.015 and that the project is feasible and practicable and is necessary and would be a benefit to the land to be included in the district.

The factors the Commission shall consider in determining if the project is feasible and practicable and if it is necessary and would be a benefit to the land included in the district:

(1) the availability of comparable service from other systems, including but not limited to water districts, municipalities, and regional authorities;

(2) the reasonableness of projected construction costs, tax rates, and water and sewer rates; and

(3) whether or not the district and its system and subsequent development within the district will have an unreasonable effect on the following:

(A) land elevation;
(B) subsidence;

[1] ALJs' Proposal for Decision, page 60.

(C) groundwater level within the region;
(D) recharge capability of a groundwater source;
(E) natural run-off rates and drainage;
(F) water quality; and
(G) total tax assessments on all land located within a district.[2]

C. DISCUSSION

In the PFD, the ALJs found that the Applicant met all of the factors listed above except for: 1) the reasonableness of projected construction costs and tax rates and economic feasibility of the District, 2) the reasonability of the effect on the groundwater level in the region and recharge capability of a groundwater source, and 3) whether Applicant met the requirements in their request for road powers.[3]

1. Projected Construction Costs, Tax Rates, and Economic Feasibility

In its application, the Applicant provided an estimated cost of $48,160,000 for water, wastewater, and drainage construction costs and $19,175,000 for road construction costs.[4] A contingency of 5% was included on construction with these costs. Also in its application materials, the Applicant included a projected tax rate of $0.9941 per $100 of assessed valuation.[5]

The Protestant's expert, Dennis Lozano, testified that the water, wastewater, drainage, and road construction costs are underestimated by approximately 50%.[6] However, Mr. Lozano also testified that he has never worked in Ellis County and did not review any MUDs in Ellis County.[7] Mr. Lozano went on to testify that while he felt the tax rates are within the statutory limits, there was insufficient evidence to determine the economic feasibility of the proposed District.[8] During the hearing, Mr. Lozano testified that for a 5% contingency fee, he'd expect to see a complete set of construction plans.[9]

The Applicant's engineer, Mr. Ken Heroy, testified that the projected construction costs appear reasonable compared to other taxing authorities in the area.[10] In its Reply to Closing Arguments, the Applicant noted that Ellis Ranch MUD No. 2 and Ellis Ranch MUD No. 3 … "will share in the costs of the construction of the wastewater treatment facility for all three districts."[11] The ED's expert witness, Mr. Andrew Paynter, also testified that the projected construction costs appear reasonable.[12]

In their PFD, the ALJs stated that while "experts may disagree as to construction unit prices… a cost difference of 40% to 60%... is alarming."[13] The ALJs also stated that

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[2] Texas Water Code § 54.021(b).
[3] PFD at page 60.
[4] Exhibit ED-AP-4, Table No. 3, page 0037.
[5] *Id.* at Table No. 5, page 0039.
[6] Lozano Prefiled Testimony, page 7, lines 17-20.
[7] PFD page 85, lines 15-17; PFD page 84, lines 18-25; PFD page 85, lines 1-3.
[8] *Id.* at pages 7-8, lines 21-23 and 1-4.
[9] Transcript, page 99.
[10] Heroy Prefiled Testimony, page 15, lines 16-18.
[11] Applicant's Reply to Closing Arguments, page 2.
[12] Paynter Prefiled Testimony, page 8, lines 10-13.
[13] PFD at page 29.

construction costs of approved MUDs that, "…may or may not contribute to the District… has no bearing on the outcome of this case."[14]

The ALJs are correct in that experts will disagree as to construction prices. The discrepancy between the estimated cost by the Applicant and the Protestant does not render the applicant's construction costs unreasonable. As stated in the ED's Closing Argument, the Applicant's projected costs are reasonable when compared to other taxing authorities in the area.[15] This is the appropriate test to use to determine if the applicant's projected costs are reasonable, not an unsupported estimate developed by the Protestant's witness. Furthermore, 30 Texas Administrative Code Section 293.11(d)(5) requires an applicant to submit a *preliminary* [16] engineering report, which is signed and sealed by the Applicant's engineer. And 30 Texas Administrative Code Section 293.11(d), which lists the petition requirements for MUD creations, refers to a statement of the *estimated* [17] project cost. There is nothing in the TCEQ rules or the Texas Water Code which requires a "complete set of plans" or something similar. The projected construction costs will undoubtedly change over time, as they inevitably have in virtually every district creation application that has been submitted to the TCEQ.

The rules regarding construction cost estimates for district creations require "reasonableness" of such costs when an application is initially submitted; in other words, a virtual "snapshot" of proposed construction costs at that time. The ED's position, which has remained the same since the technical memorandum was issued on this application on July 26, 2022, is that the proposed construction costs included in the Applicant's preliminary engineering report are reasonable and as such, TCEQ requirements on this issue are satisfied.

Regarding the contingency, the ALJs opined that the… "evidence demonstrates that Applicant's 5% contingency is insufficient and unreasonable."[18] The ALJs went on to state that a 15% to 25% contingency would be reasonable for the District.[19] The ED is unable to weigh in on what an appropriate contingency percentage is for any district creation application, including the one at hand. The ED relied on the Applicant's engineer to determine the appropriate contingency percentage, and there was nothing in the application materials that indicated to the ED that this contingency percentage was inappropriate.

In addition, the Applicant's combined projected tax rate of $1.00 per $100 assessed valuation is comparable to other districts in the area, as stated in the Technical Memorandum.[20] As is often seen in district creations, the developer can alter their readjustables to insure they stay below the tax rate limit. It should be noted that that limit is only at the time of bond issuance, and the Developer can adjust the timing of the bond sales to stay below the tax rate limits. Since the tax rate is capped at $1.00 per $100 of assessed valuation, the projected financial feasibility calculations in the preliminary engineering report assume that the district would fund a limited amount

[14] *Id.* at page 28.
[15] ED's Closing Argument, page 3.
[16] Emphasis added.
[17] Emphasis added.
[18] PFD at page 29.
[19] *Id.*
[20] Exhibit ED-AP-3, Bates 0026.

of the construction costs through bonds and taxes and any remainder beyond what the district authorizes for bonds could be the developer's responsibility.

As stated in the ED's Response to Closing Arguments, the tax rates for each particular bond issue will be reviewed and justified on its own economic feasibility merits prior to the issuance of any bonds by the district.[21] As such, the ED maintains her position that the tax rate is reasonable, and would support economic feasibility of the project.

Lastly, the ED is not "ignor[ing] the actual District plan as proposed," nor is the ED "disregard[ing] TCEQ's own definition of economic feasibility of a project," as asserted by the ALJs.[22] Rather, the ED contends that the ALJs are not accounting for any change in the total assessed valuation or the interest rates. Based on the information provided, the land values, existing improvements, and projected improvements in the district appear to be sufficient to support a reasonable tax rate for debt service payments for existing and proposed bond indebtedness while maintaining competitive utility rates. In other words, the ED is not ignoring the plan. The ED is basing her approval on the plan as proposed. It should also be noted that the economic feasibility rule that the ALJs point to are for the issuance of bonds. There are no district creation rules that speak to economic feasibility.

2. Groundwater Level and Recharge of a Groundwater Source

The ALJs found that the Applicant failed to meet its burden to show that the proposed development will not have an unreasonable effect on groundwater levels and recharge in the region.[23] The applicant will be receiving water from the CCN holder in the area, Rockett Special Utility District (SUD).[24] The ALJs refer to a recent statement by the Chairman of TCEQ, claiming that the Chairman stated that, while there is no written requirement for a study of groundwater recharge to be conducted by MUD applicants, they must demonstrate that impervious area is typical for the type of development and will not have an unreasonable effect on groundwater levels and recharge capability.[25] The ALJs then assert that "[t]here is no evidence in the record as to whether the amount of impervious cover in the District is typical for this type of development, or as to *what extent* the impervious cover will impact groundwater."[26] As noted in the Proposal for Decision (PFD), the Executive Director and Office of Public Interest Counsel both agreed that Applicant met its burden on these issues.[27]

As stated in the ED's closing arguments and the prefiled testimony of ED's expert Andrew Paynter, the proposed District is anticipated to have little to no effect on the groundwater levels within the region.[28] The ED likewise maintains her position that the District is not expected to have any adverse impact on aquifer recharge.[29] TCEQ relies upon the assertions of the applicant in order to draw its conclusions, and it is not the regular practice of TCEQ to require a showing of whether the amount of

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[21] ED's Response to Closing Arguments, page 1.
[22] PFD at page 30.
[23] *Id.* at page 36.
[24] Exhibit ED-AP-4, page 0021.
[25] PFD at page 36.
[26] *Id.*
[27] *Id.* at page 34.
[28] ED's Closing Argument, page 3; Exhibit ED-AP-4, pages 0042 and 0045.
[29] *Id.*

impervious cover in the District is typical for this type of development, or as to what extent the impervious cover will impact groundwater, because it is not possible to know at this stage what the final amount of impervious cover will be. There is no evidence in the record that the proposed District will have an unreasonable effect on groundwater levels or recharge or that the amount of impervious cover is not typical to this type of development.

Additionally, in this case, water will be provided by another utility district, who has its own requirements for maintaining groundwater levels within the region. The proposed District will not be drawing any groundwater itself. As the Chairman stated in the Commission's open meeting on October 25th, 2023, "Mountain Peak's lawful use of groundwater is not relevant to our inquiry, and the same would be true for this or any other petitioner."[30] The same is true in this case. The applicant will receive their water from Rockett SUD, not wells or any other draw on this property. Therefore, the proposed District is not expected to have any direct impact on groundwater levels or recharge.

Furthermore, the language the ALJs rely on in their PFD is not an accurate recounting of the Chairman's statement. The Chairman simply clarified that the analysis under TWC Section 54.021 should end after considering whether the impervious groundcover is typical of this type of development, and whether it will have an unreasonable effect on groundwater levels in the region.[31] The Commission did not state any new burden that should be placed on MUD applicants. On the contrary, the Commission was seeking to clarify that additional analysis is *not* required, based on their limiting language. Additionally, the applicant in the case the Chairman referenced presented very similar evidence to the case at hand. In fact, the only reference to impervious groundcover in that case was in the Applicant's Closing Brief, which merely stated that the impervious cover would not have a greater effect than any other typical single-family development.[32] There is no evidence in the record that indicates that the development within the proposed MUD is any different from that of other districts in the area. As a result, the inquiry into the effect on groundwater levels and recharge within the region should end there.

The ALJs were correct that the Commission did not place a burden on MUD applicants to obtain a study of groundwater levels and recharge, because the statement regarding studies was in reference to runoff rates and drainage, not groundwater levels and recharge.[33] Even if the statement were referring to groundwater recharge, such an interpretation would seem to support a conclusion that the Chairman was not seeking to place additional burdens on MUD applicants. Finally, the Chairman's next statement confirmed this interpretation, as he said, "I don't think that the legislature intended TCEQ to regulate groundwater through the creation of MUDs."[34] Therefore, the ED respectfully disagrees with the ALJs on the issue of groundwater levels and recharge capabilities and continues to assert that there is no evidence that the proposed District will have an unreasonable effect on either factor.

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[30] SOAH Docket No. 582-22-07138; TCEQ Docket No. 2022-0532-DIS (Commission discussion at open meeting, Oct. 25, 2023).
[31] *Id.*
[32] SOAH Docket No. 582-22-07138 Applicant's Closing Brief, page 12.
[33] *Id.*
[34] *Id.*

3. Road Powers

The ALJs concluded that Applicant's request for road powers did not meet the requirements set forth in Texas Water Code Section 54.234 and 30 Texas Administrative Code Sections 293.11(d)(11) and .202(b) because, as the ALJs claim, Applicant failed to demonstrate that the proposed facilities are financially and economically feasible for the District.[35] Protestant's expert, Mr. Lozano, testified that the estimated costs for roads was based on a high-level valuation.[36] Applicant asserted that it has satisfied its burden by providing a preliminary layout of the roads, detailed cost estimates, and reports on the tax rate allocation for bonds.[37] The ED determined that the Applicant met its burden, and that the applicable requirements for granting road powers with the District creation have been satisfied.[38] The ED continues to hold this view of the issue.

The ALJs seem to have mistakenly assumed that economic feasibility for the District overall weighs into the determination of road powers. The economic feasibility of road powers, however, is considered separately from the overall economic feasibility of the District, and instead, as stated in the statute, the question is what effect the proposed road powers will have on the District. The ALJs acknowledge that the statutory requirements for a preliminary layout, cost analysis and detailed estimate, and analysis of financial and economic feasibility impact have been fulfilled.[39] These factors are all that is required of MUD applicants when requesting road powers. While the ED maintains, as noted above, that the District is economically feasible, this is irrelevant to the issue of road powers, and thus the ED respectfully disagrees with the determination of the ALJs in relation to this issue.

D. CONCLUSION

The ALJs' position in their Proposal for Decision appears to 1) require the ED to weigh in on what an appropriate contingency percentage would be in the MUD creation process, 2) create a new factor for MUD creations that would require applicants to provide additional information on groundwater levels and recharge that is not required by statute, and 3) tie the economic feasibility of a District as a whole to the economic feasibility analysis for road powers. The ED saw no evidence in the application that would lead her to conclude that the contingency percentage was unreasonable, and her analysis ends there.

Similarly, creating additional factors for consideration in the process of MUD creations is the job of the legislature and the Commission, not the judiciary. This is especially true when new factors are seemingly added during the hearing process. An applicant cannot be held to standards that did not exist at the time of the application. If this were allowed, not only would applicants lack clarity on what is required of them in the MUD application process, but the ED's determinations would be essentially pointless as new requirements could be added by an ALJ at the hearing stage, rendering the ED's analysis moot. Additionally, as with many factors present in MUD creation, the factors the ALJs took issue with are estimates that will likely change

[35] PFD at page 58.
[36] *Id.* at page 56.
[37] *Id.*
[38] *Id.* at page 57
[39] *Id.* at page 58.

during the construction process. All statutes, rules, and local law must be complied with in the construction of a MUD; the creation process is a preliminary step that must be fulfilled prior to any construction. Most importantly, there is no authority for these recommendations.

The ED respectfully recommends that the Commission not adopt the ALJs' proposed order. Rather, the ED recommends finding that the Applicant has met all requirements with regard to the applicable statutes and rules and therefore grant the creation of Ellis Ranch MUD No. 1.

Respectfully submitted,

TEXAS COMMISSION ON
ENVIRONMENTAL QUALITY

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ATTORNEYS FOR THE
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CERTIFICATE OF SERVICE

I hereby certify that on this 18th day of March, a true and correct copy of the foregoing document was delivered via electronic mail, facsimile, hand delivery, interagency mail, or by deposit in the U.S. Mail to all persons on the attached mailing list.

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