

BILL ANALYSIS

H.B. 3542
By: Phelan
State Affairs
Committee Report (Unamended)

BACKGROUND AND PURPOSE

For some smaller water and wastewater utilities whose system infrastructure is urgently in need of repair or replacement, sale to a larger utility is a welcome opportunity to enable system improvements and ensure continued safe and reliable service for customers. However, concerns have been raised that current state law restricting a utility's ability to recover an investment for such an acquisition inhibits these otherwise mutually beneficial transactions. H.B. 3542 seeks to remove these barriers to investment by establishing an optional alternative valuation appraisal process as part of a voluntary acquisition of a retail public utility or its facilities.

CRIMINAL JUSTICE IMPACT

It is the committee's opinion that this bill does not expressly create a criminal offense, increase the punishment for an existing criminal offense or category of offenses, or change the eligibility of a person for community supervision, parole, or mandatory supervision.

RULEMAKING AUTHORITY

It is the committee's opinion that this bill does not expressly grant any additional rulemaking authority to a state officer, department, agency, or institution.

ANALYSIS

H.B. 3542 amends the Water Code to authorize a Class A utility that is acquiring a retail public utility or facilities of such a utility as the result of a voluntary arm's-length transaction to agree to determine by the following process the fair market value of the selling utility or the facilities to be sold, as applicable:

- the acquiring utility and the selling utility must notify the Public Utility Commission of Texas (PUC) of their intent to determine the fair market value;
- the PUC, not later than the 30th day after the date the PUC receives the notice, must select three utility valuation experts;
- each expert must perform an appraisal in compliance with Uniform Standards of Professional Appraisal Practice, employing the cost, market, and income approaches, to determine the fair market value; and
- the three experts jointly must retain a licensed engineer to conduct an assessment of the tangible assets of the selling utility or the facilities to be sold and each expert must incorporate the assessment into the appraisal under the required cost approach and provide the completed appraisal to the acquiring utility and the selling utility in a reasonable and timely manner.

The bill establishes that, for purposes of the acquisition, the fair market value is the average of the three appraisals.

H.B. 3542 requires the PUC to maintain a list of experts qualified to conduct economic

valuations of utilities for the bill's purposes and requires the three experts to be chosen from that list. The bill provides certain conflict of interest protections with regard to the valuation experts and sets out provisions relating to fees paid to an expert.

H.B. 3542 establishes that, for an acquisition of a selling utility, the selling utility's ratemaking rate base is the lesser of the purchase price negotiated by the acquiring utility and the selling utility or the fair market value. The bill requires that rate base to be incorporated into the acquiring utility's rate base during the utility's next rate base case under proceedings before the PUC.

H.B. 3542 requires an acquiring utility that, with the selling utility, used the process for establishing fair market value set out by the bill to submit certain related information and documentation as attachments to the acquisition application, including, if applicable, a tariff containing a rate equal to the selling utility's existing rates at the time of the acquisition. The bill establishes that a submitted tariff remains in effect until the PUC approves new rates as part of a rate base case proceeding. The bill requires the PUC to issue an order following approval of the application containing the selling utility's determined ratemaking rate base and any additional conditions for the acquisition the PUC requires.

H.B. 3542 establishes that the original sources of funding for any part of a selling utility's water or sewer assets are not relevant to determine the value of the selling utility's assets. The bill requires the selling utility's cost of service to be incorporated into the revenue requirement of the acquiring utility's next rate base case proceeding. The bill establishes that an acquiring utility's post-acquisition improvements accrue on an accounting practice that recognizes the capital costs that are used to finance the construction costs of an improvement to a selling utility's assets by an acquiring utility after the date the cost was incurred until the earlier of the fourth anniversary of the date the asset entered into service or the inclusion of the asset in the acquiring utility's next rate base case. The bill defers depreciation on an acquiring utility's post-acquisition improvements for book and ratemaking purposes.

EFFECTIVE DATE

September 1, 2019.