

Texas Justices OK Electric Companies' Pollution Exemptions

By **Michelle Casady**

Law360 (May 3, 2019, 10:41 PM EDT) -- The Texas Supreme Court on Friday determined that the Texas Commission on Environmental Quality did not have the authority to deny a property tax exemption for electric companies that operate heat recovery steam generators, which are devices the Legislature has deemed “pollution control property.”

The state's high court issued opinions in two cases that asked it to determine whether the commission overreached in denying the exemptions sought by nine electric companies. Brazos Electric Power Cooperative and eight other power plants argued that under Subsection K of Texas Tax Code Section 11.31, which outlines properties the Legislature has already determined are pollution-control properties and which includes heat recovery steam generators, or HRSGs, they should be provided at least a proportional exemption for pollution control.

The TCEQ had argued the electric companies' applications didn't meet the requirements for a pollution-control property exemption because HRSGs don't remove pollutants from the combustion process, but instead “make production equipment more efficient.” Five of the applications failed to show that their HRSGs were adhering to any environmental rule for which a pollution-control exemption could be given, and three did not provide a reasonable methodology for determining the pollution-control proportion of the HRSGs, the TCEQ argued.

But the Texas Supreme Court disagreed, holding that the Legislature had removed from the TCEQ's purview any ability to determine whether the HRSGs qualify as pollution-control property because the lawmakers already determined that they do and are therefore entitled to a tax exemption. That means TCEQ's “sole responsibility” is to decide what portion of the property is “purely productive,” and what proportion is for pollution control.

“But it may not determine that the pollution control proportion is zero or negative — the Legislature took 'zero' off the table when it instructed the [TCEQ] executive director to determine that k-list property is pollution control property, meaning it is used at least 'partly' for pollution control,” the court wrote.

The Texas Supreme Court also noted, however, that the Legislature does allow TCEQ to determine that some equipment should be removed from the list, but that the agency has declined so far to exercise that authority. It remanded the case to TCEQ to make a determination on the amount of the tax exemption the companies are entitled to.

Melissa M. Davis of Thompson & Knight LLP, who represents Brazos Electric, said she was pleased with the ruling in favor of her client, describing the process of overturning the administrative ruling from TCEQ against it as a “ long uphill battle.” She expressed skepticism that the TCEQ will chose to exercise its authority to remove HRSGs from the list of equipment that qualifies for an exemption.

“I really think one of the reasons they haven't done that is because they have to show that the equipment isn't environmentally beneficial,” she said. “And that's going to be hard to do because that's by their nature what they do — reduce pollution through increased efficiency.”

Nine energy companies initially appealed exemption denials from the commission, with Brazos' appeal going through the El Paso appeals court and the remaining eight staying in Austin. The two cases rose to the high court after the El Paso and Austin appeals courts split on the question of whether the TCEQ's denial of the property tax exemption was correct.

The Austin appeals court ruled that Section 11.31 is unambiguous in saying heat recovery steam generators are eligible for a pollution-control property tax exemption. Conversely, the El Paso appeals court said the commission's determination rejecting applications for property tax exemptions on heat recovery steam generators was appropriate.

The eight other companies challenging the tax exemption denial are Freestone Power Generation LLC, Freeport Energy Center LLC, Brazos Valley Energy LLC, Tenaska Gateway Partners Ltd., Ennis Power Co. LLC, Wise Power Co. LLC, Midlothian Energy LLC and Hays Energy LLC.

Counsel for TCEQ and the other eight electric companies did not immediately return messages seeking comment Friday.

Brazos Electric Power Cooperative is represented by Melissa M. Davis, Emily A. Fitzgerald and Nathan K. Palmer of Thompson & Knight LLP and Christopher D. Smith of Smith Jolin LLP.

Freestone, Freeport and Brazos are represented by Susan A. Kidwell, Elizabeth E. Mack and Geoffrey R. Polma of Locke Lord LLP. Tenaska is represented by Thomas A. Countryman and Edward Kliewer III of Norton Rose Fulbright. Ennis, Wise, Midlothian and Hays are represented by Kevin D. Collins and Whitney L. Swift of Bracewell LLP.

The Texas Commission on Environmental Quality is represented by Daniel C. Wiseman and Amy Davis of the Texas Attorney General's Office.

The cases are Texas Commission on Environmental Quality et al. v. Brazos Valley Energy LLC et al., case number 18-0128, and Brazos Electric Power Cooperative Inc v. Texas Commission on Environmental Quality et al., case number 17-1003, in the Supreme Court of Texas.

--Additional reporting by Philip Rosenstein. Editing by Peter Rozovsky.