



although in hindsight it now appears TXU did not have any. TXU enters competition with the opposite of stranded costs—its power generation assets will be worth almost \$3 billion more than their book value. If nothing is done to remedy this excess until 2004, competition will be stifled. These findings by the PUC may be wrong, but for purposes of this mandamus proceeding we must take them as true.<sup>2</sup>

Whether the Legislature foresaw this situation when drafting the statute is unclear, but one thing is certain—it made no specific provision for it. This is not a case, as TXU argues, in which the Legislature prescribed a plan that the PUC refuses to follow. As shown below, not one of the statutory provisions on which the parties rely tells the PUC what to do in this situation. As a result, TXU asserts the PUC can do nothing, at least not for several years.

But state agencies have never been strictly limited to specific statutory provisions. If legislators could foresee every contingency, there would be little need for agencies. Because they cannot, agencies also have whatever implied powers are reasonably necessary to fulfill their regulatory duties.<sup>3</sup>

In the Public Utility Regulatory Act (PURA), the Legislature directed the PUC to deregulate the electric industry in a way that encourages competition.<sup>4</sup> Given its factual findings and this legislative directive, the PUC must do something. Because all parties implicitly agree the statute is ambiguous, and the PUC's interpretation is just as reasonable as any other, no clear legal violation has been shown.

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<sup>2</sup> *Brady v. Fourteenth Court of Appeals*, 795 S.W.2d 712, 714 (Tex. 1990) (holding appellate court may not deal with disputed areas of fact in original mandamus proceeding).

<sup>3</sup> *Pub. Util. Comm'n of Texas v. City Pub. Serv. Bd. of San Antonio*, 53 S.W.3d 310, 315 (Tex. 2001). In addition, the Legislature specifically granted the PUC authority to do anything “necessary and convenient” to the regulation of public utilities. TEX. UTIL. CODE § 14.001.

<sup>4</sup> TEX. UTIL. CODE § 39.001(b)(1).

*Section 39.254*

TXU relies on two sections of the statute. First, it argues PURA section 39.254 gives it a right—indeed a duty—to mitigate the stranded costs it had in 1998. That is not what the section says:

This subchapter provides a number of tools to an electric utility to mitigate stranded costs. Each electric utility that was reported by the commission to have positive "excess costs over market" (ECOM), denoted as the "base case" for the amount of stranded costs before full retail competition in 2002 with respect to its Texas jurisdiction, in the April 1998 Report to the Texas Senate Interim Committee on Electric Utility Restructuring entitled "Potentially Strandable Investment (ECOM) Report: 1998 Update," must use these tools to reduce the net book value of, otherwise referred to as "accelerate" the cost recovery of, its stranded costs each year. Any positive difference under the report required by Section 39.257(b) shall be applied to the net book value of generation assets.<sup>5</sup>

The reference in this section to the 1998 report limits only *who* may use the chapter's tools. Nothing in the section freezes stranded costs at 1998 levels. When the Legislature intended to freeze utility figures at 1998 levels elsewhere in the statute, it did so expressly.<sup>6</sup> It did not do so here.

It is undisputed the 1998 report listed TXU as having stranded costs at that time. So applying section 39.254 to this case, the operative second sentence requires TXU to accelerate recovery of "its stranded costs each year."<sup>7</sup> The ambiguity is in these last five words—which stranded costs? Those that appeared to exist in 1998 or those that appear to exist now?

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<sup>5</sup>*Id.* § 39.254.

<sup>6</sup> *See, e.g.*, TEX. UTIL. CODE § 39.302(5) (limiting "regulatory assets" to those reported by utilities in 1998 Form 10-K); *City of Corpus Christi v. Pub. Util. Comm'n of Texas*, 51 S.W.3d 231, 257 (Tex. 2001) (holding PUC correctly refused to use updated figures for regulatory assets when statute froze them at 1998 levels).

<sup>7</sup> TEX. UTIL. CODE § 39.254.

The PUC chose to use current estimates, and that is certainly the more reasonable construction. There is no reason to require accelerated recovery of stranded costs from previous years that no longer exist. Once its stranded costs were reduced to zero, TXU could not continue mitigation simply because it made more money that way. TXU's counsel conceded at oral argument that if TXU had sold its nuclear power plant in 1999 at book value, it could not continue recovering stranded costs under section 39.254. The same rule should apply when stranded costs disappear not due to a sale but to a rise in gas prices.

Nevertheless, TXU has continued to recover stranded costs in years when, according to the PUC, it had none. Section 39.255 of the statute allows a utility "that does not have stranded costs described in Section 39.254" to use excess revenues to improve transmission, distribution, or air quality facilities.<sup>8</sup> TXU has used its excess revenues for none of these. As a result, section 39.255 requires TXU to return these funds to consumers.<sup>9</sup> That is just what the PUC order does.

TXU argues the Legislature intended to freeze estimated stranded costs at 1998 levels (eventhough the statute never says so) because after the true-up proceeding in 2004 they will become "actual" rather than "estimated." But the true-up is likely to require just as many educated guesses as earlier estimates. Nuclear plants (the main source of stranded costs) rarely swap hands, and never in an open market. In lieu of an objective market price, the plants will be valued at the true-up using stock prices and anticipated income streams.<sup>10</sup> But stock prices reflect many factors other than the auction-value of the plants. And

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<sup>8</sup>*Id.* § 39.255(a).

<sup>9</sup> *Id.* § 39.255(b).

<sup>10</sup>*Id.* § 39.262(h), (i).

it will be impossible to tell whether income stream estimates are accurate until decades from now when the last kilowatt is sold. The Legislature certainly had the power to provide a cut-off date in 2004, after which all calculations would be treated as final. But that merely guarantees they are final; it cannot guarantee they are accurate.

The statute does not freeze stranded cost estimates at 1998 levels. It requires the PUC to update stranded cost estimates now,<sup>11</sup> and nowhere requires it to ignore the results. In a recent case involving the same statute, the same parties, and the same question—whether the PUC should use updated figures when the statute was unclear—this Court deferred to the Commission.<sup>12</sup> To be consistent, the Court must do the same here.<sup>13</sup>

### *Section 39.201*

Second, TXU argues the PUC has taken steps it has no power to take—at least not yet. For reasons both statutory and equitable, TXU dares not argue it can simply keep several billion dollars as a windfall. Instead, it points out that PURA section 39.201(*l*) allows the PUC to take the steps it does here (reversing redirected depreciation and returning excess revenues to consumers by lowering rates) after the

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<sup>11</sup> See *id.* § 39.201(g).

<sup>12</sup> See *TXU Elec. Co. v. Pub. Util. Comm'n of Texas*, 51 S.W.3d 275, 286 (Tex. 2001) (Owen, J., concurring).

<sup>13</sup> TXU points out the PUC did not use updated figures consistently, refusing to update some figures that might have operated to TXU's benefit. It is hard to see why section 39.254 should be read broadly to favor updated figures, and yet section 39.201(h) should be read narrowly to preclude some updates merely because it mandates others. But as TXU admits, this issue is not before the Court in this proceeding.

true-up proceeding some years from now. Because of this express provision, TXU infers a legislative intent to prohibit their use any earlier.

But the Legislature did provide for some rate adjustment in the current proceedings based on updated stranded cost estimates. PURA section 39.201(g) allows the PUC to include a competition transition charge in 2002 rates based on current estimates of stranded costs.<sup>14</sup> TXU argues that, because the PUC's adjustment is a credit to consumers rather than a charge, it has improperly read a "negative competition transition charge" into the statute.

But TXU makes the same inference in its own reading of the statute, without saying so. TXU says section 39.201(l) allows the PUC to remedy overrecovery at the true-up, but that section only applies if "the competition transition charge is larger than is needed to recover any remaining stranded costs." It is undisputed TXU's rates will include *no* competition transition charge, and it will have *no* "remaining stranded costs" if it has overrecovered them. How then can this section apply, if the charge that is "larger than is needed" is zero? Only by reading the statute to imply a negative competition transition charge. There is nothing else zero can be "larger than."

TXU's argument shows all parties agree we must infer somewhere in chapter 39 the equivalent of a negative competition transition charge. The PUC's order has the effect of doing do so in section

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<sup>14</sup> TEX. UTIL. CODE § 39.201(g).

39.201(g); TXU would do so in section 39.201(l). There is no reason why the former is *ultra vires* if the latter is not.<sup>15</sup>

*Section 39.262(a)*

The PUC relies on two other sections of the statute, both of which mandate general duties without providing specific means. First, it argues PURA section 39.262(a) absolutely prohibits any overrecovery of stranded costs:

An electric utility, together with its affiliated retail electric provider and its affiliated transmission and distribution utility, may not be permitted to overrecover stranded costs through the procedures established by this section or through the application of the measures provided by the other sections of this chapter.<sup>16</sup>

TXU argues this section applies only to the true-up proceeding in 2004. But in the last clause of the rule, the Legislature said just the opposite—the section also applies to “the measures provided by the other sections of this chapter,” including the current proceedings. TXU points to the location of this provision in a section titled “True-Up Proceeding.” The Legislature has categorically rejected such reasoning: “the heading of a . . . section does not limit or expand the meaning of a statute.”<sup>17</sup> And the Legislature’s location

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<sup>15</sup> TXU also suggests stranded costs may be recovered at the true-up pursuant to section 39.262(g). But that section applies only if the PUC determines that rates “are larger than needed to recover the transmission and distribution utility’s costs.” It makes no mention of stranded costs, and a transmission and distribution utility’s costs would never be stranded, as it remains a regulated monopoly. Even if it did apply, the section would again require inferring a negative competition transition charge.

<sup>16</sup> *Id.* § 39.262(a).

<sup>17</sup> TEX. GOV’T CODE § 311.024.

of provisions in this statute cannot be conclusive (at least not contrary to the express words) because it is not always consistent.<sup>18</sup> The body of section 39.262(a) says it applies to all parts of chapter 39. Contrary to human anatomy, in statutory construction what's in the body governs, not what's in the head.

The PUC found TXU overrecovered stranded costs, and there is no denying it did so “through the application of the measures provided by the other sections of this chapter” (specifically sections 39.254 and 39.256). Because the statute says this “may not be permitted,” it is hard to argue the statute prohibits the PUC from doing anything about it.

#### *Section 39.001*

Second, the PUC relies on PURA section 39.001(b)(1), in which the Legislature requires it to implement deregulation in a way “that encourages full and fair competition among all providers of electricity.”<sup>19</sup> The PUC found that doing nothing until 2004 might crush competition just as it starts. This is because TXU's overrecovery threatens to cancel a three-year advantage the Legislature provided for new competitors. Until 2005, the Legislature set a floor for TXU's retail rates and designated it the “price to beat.”<sup>20</sup> By reversing overrecovery of stranded costs, the PUC's order pushes down transmission rates until then, and makes it easier for new competitors to do exactly what the price's name suggests.

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<sup>18</sup> For example, section 39.201(l) concerning the tools available at the true-up is located in the section concerning rate-setting for 2002. Conversely, section 39.262(b) concerning annual reports by certain utilities beginning in 2002 is located in the section concerning the true-up beginning in 2004.

<sup>19</sup> TEX. UTIL. CODE § 39.001(b)(1).

<sup>20</sup> *See id.* § 39.202.

But if transmission costs are kept artificially high until after the true-up is completed<sup>21</sup> (as TXU suggests), by that time TXU will no longer be bound to the price to beat.<sup>22</sup> The brief competitive advantage the Legislature intended for new competitors will never exist. Again, given this legislative mandate to encourage competition and an interim plan that prescribed a price advantage for new providers, it is hard to argue the statute requires the PUC to stand by while the “price to beat” becomes a “price that cannot be beat.”

### *The Necessary Implication*

This brief overview of the relevant statutory provisions shows the Legislature could not have been clearer about what the PUC must do—it must promote competition and prohibit overrecovery of stranded costs. But the Legislature could have been clearer about how, at least in the current circumstances. There is no prescribed plan for the current situation; the Legislature prescribed the results it wanted, but left the means and timing unclear.

What should the PUC do when the Legislature gives it a mandate but no express authority to carry it out? The Court answered this question most recently in a case involving the same statute and many of the

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<sup>21</sup> The PUC proceeding at issue here began in March 2000, and a final order was not issued until eighteen months later. Even with this Court’s prompt review by mandamus, numerous issues remain pending in the trial court, and the time needed to complete them and the inevitable appeals is anybody’s guess. It would be wishful thinking to assume the true-up will proceed any faster.

<sup>22</sup> See TEX. UTIL. CODE § 39.202(e).

same parties. In *City of Corpus Christi v. Public Utility Commission of Texas*,<sup>23</sup> several parties challenged a “non-standard true-up” because the statute<sup>24</sup> did not expressly provide for reallocation among consumer classes. This Court rejected the challenge, relying on a more general section<sup>25</sup> allowing adjustments to utility rates (but not reallocation among classes) to ensure funds would be available to pay a utility’s bonds.<sup>26</sup> The Court reasoned that the important purpose in the general policy permitted “minor and essential adjustments” not expressly permitted by the statute.<sup>27</sup>

The same applies here. The statutory adjustments the PUC adopted are minor—they implement powers the PUC clearly has, though arguably not yet. They are also essential if the PUC is to comply with the statute’s mandatory policies in favor of competition and against overrecovery of stranded costs. If the Court was correct when it held the PUC could act by necessary implication to protect the viability of bonds and the interests of bondholders, surely the viability of competition and the interests of consumers deserve no less.

## Conclusion

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<sup>23</sup> 51 S.W.3d 231 (Tex. 2001).

<sup>24</sup> See TEX. UTIL. CODE § 39.253.

<sup>25</sup> See *id.* § 39.307.

<sup>26</sup> *City of Corpus Christi*, 51 S.W.2d at 268.

<sup>27</sup> *Id.* at 268-70.

No one knows the amount of TXU's stranded costs. After an eighteen-month proceeding involving scores of lawyers, experts, and computers, the PUC commissioners determined TXU had no stranded costs, and should not retain \$1.7 billion for several years on the assumption that it did. They may be wrong, but under any theory of legislative delegation, it is their mistake to make.

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Scott Brister  
Justice

OPINION DELIVERED: December 31, 2001