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SOAH DOCKET NO. 473-14-5139.WS

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APPEAL OF WATER AND SEWER §  
RATES CHARGE BY THE TOWN OF §  
WOODLOCH CCN NOS. 12312 §  
AND 20141 §

BEFORE THE STATE OFFICE  
PUBLIC UTILITY COMMISSION  
FILING CLERK

ADMINISTRATIVE HEARINGS

**TOWN OF WOODLOCH'S INITIAL BRIEF**

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TO THE HONORABLE HUNTER BURKHALTER, ADMINISTRATIVE LAW JUDGE ("ALJ"), STATE OFFICE OF ADMINISTRATIVE HEARINGS ("SOAH"):

The Town of Woodloch ("Woodloch" or "Town") files this Initial Brief in the above referenced proceeding. For the reasons set forth below, Woodloch has met its burden of proof and has shown that it is entitled to the entirety of the water and sewer rates it established by act of the Town Council on January 18, 2013. It has also proven that its rate-case expense surcharge established by Council action on June 10, 2014 is reasonable and justified and should also be approved.

## **I. PROCEDURAL HISTORY**

This case has had a long and complex procedural history. The initial rate setting by the Town Council occurred in a Town Council meeting on January 18, 2013 following several months of calculations and deliberations by the Town going back to the beginning of 2012. (Woodloch Exh. 1 at 18-19; Woodloch Exh. 7 at 246-254). The Out-of-City (“OOC”) customers filed their appeal with the Texas Commission on Environmental Quality (“TCEQ”) on April 19, 2013. That appeal was accepted by the TCEQ on May 20, 2013 following a determination that the appeal was signed by at least 10% of the OOC customers. During the 83rd Legislative Regular Session, HB 1600 and SB 567 were passed and ultimately enacted into law. HB 1600 and SB 567 transferred jurisdiction over water and sewer utility rates from the TCEQ to the Public Utility Commission of Texas (“PUC”) effective September 1, 2014. On May 20, 2013, TCEQ referred the matter to the State Office of Administrative Hearings for a contested case hearing (“CCH”) and a preliminary hearing was held on August 20, 2013. A mediation session was scheduled in Houston, Texas for December 2013 but was never actually held. Settlement negotiations between the parties continued during the Spring of 2014. On June 19, 2014, a mediation session was held in Conroe, Texas. On June 27, 2014, Woodloch filed a Motion to Abate Proceedings, requesting the matter be abated until after September 1, 2014 so that the transfer of jurisdiction could occur prior to the CCH on the matter. That motion was granted by the ALJ in his Order No. 5.

On June 10, 2014, the Town Council adopted its Rate Case Expense Surcharge. On July 3, 2014, the OOC customers’ appeal was received by the TCEQ. On January 30, 2015, the PUC Commission considered the OOC customers’ appeal in Open Meeting. On February 4, 2015, the PUC Commission issued its Preliminary Order referring that action to a CCH in PUC Docket No. 43720; SOAH Docket No. 473-15-1710.WS. On March 16, 2015, Woodloch filed a Motion

recommending that SOAH Docket No. 473-15-1710.WS be consolidated with the underlying rate case (SOAH Docket 473-14-5139.WS). That motion was granted by the ALJ in his Order No. 13. An evidentiary hearing date of June 2-4, 2015 was set by the ALJ and the evidentiary hearing held on June 2 and 3, 2015 in Austin, Texas.

## **II. BACKGROUND**

### **A. Historic Background**

The Town of Woodloch is a small incorporated municipality in southern Montgomery County, Texas. It has approximately 72 residential homes and a population of approximately 250 persons. (Woodloch Exh. 1 at 5) It has no retail or commercial development within its city limits. (Woodloch Exh. 1 at 5) The average home valuation is approximately \$70,000 and it receives only about \$38,000 per year in ad valorem taxes from those homes. (Woodloch Exh. 1 at 5) The Town also receives a small amount of revenue, approximately \$14,000 from licensing fees from its cable and telephone provider. (Woodloch Exh. 1 at 5) In total, Woodloch's typical revenue from these sources is approximately \$52,000/year. Id.

The Town owns its water and sewer utility which provides service not only to the Town's citizens, but also to approximately 174 customers who do not reside within the Town's boundary. (Woodloch Exh. 1 at 12-13) The OOC customers became customers of the Town's utility as a result of a request for assistance from the then Texas Natural Resource Conservation Commission when Consumer's Water Corporation, a private investor-owned utility became insolvent in 1989. (Woodloch Exh. 1 at 11) As a result of that consolidation Woodloch now has a total of approximately 245 water and sewer utility customers.<sup>1</sup> (Woodloch Exh. 1 at 12-13) The Town has struggled with maintaining the engineering and financial integrity of this

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<sup>1</sup> The exact total varies from month-to-month based on customers voluntarily and involuntarily leaving and rejoining the system.

combined system since the assimilation of the former Consumer's Water Corporation into its system due to the poor physical condition of the infrastructure and the financial limitations of the communities that it serves. (Woodloch Exh. 4 at 8)

Over the years it has been able to gain funding through state and federal utility loan and grant programs accessible because of the under-privileged nature of the Town and the OOC customers. (Woodloch Exh. 1 at 12) This has allowed it to operate and provide minimally adequate service to its customers, but has not been enough to address the infrastructure upgrades necessary for long-term viability of the utility. (Woodloch Exh. 1 at 9) As a result, there has been a continuing deterioration of the infrastructure and the consequent increased need for replacement of worn-out system components. (Woodloch Exh. 4 at 11) At the time of the Town Council's rate-setting action which is the subject of the dispute in this matter, the record shows that the Town needed to replace its entire wastewater treatment plant, replace or refurbish much of its water distribution and sewage collection lines, and replace both pressure tanks in its water system and its water storage tank. (Woodloch Exh. 4 at 14-15) Additionally, the utility has historically had high maintenance costs due to the high incidents of abuse and vandalism in the OOC area of the utility. (Woodloch Exh. 4 at 12; Woodloch Exh. 1 at 9) In 2012 the Town Council made several moves to address these issues, including: (a) applying for a Texas Water Development Board ("TWDB") loan in the amount of approximately \$2.7 million dollars with a 70% loan forgiveness for upgrades to its sewer system; (b) preparing to purchase an electronic water meter reading system at a cost of \$52,500; and (c) preparing for the replacement of the dilapidated water system ground storage tank at a cost of approximately \$130,000. (Woodloch Exh. 1 at 14; Woodloch Exh. 25 at 6) The loans for the meter system and the storage tank were finalized in 2013, shortly after January the rate-setting, but the loan for the sewer system

upgrades was never funded by TWDB due to its uncertainty about the Town's financial ability to repay the loan because of the OOC customers' challenge of the Town's rates in this docket. (Woodloch Exh. 1 at 14) Compounding the difficulty of the situation, the Town, when faced with mounting rate-case expenses, was forced to adopt a surcharge to pay rate-case expenses. That too was challenged by the OOC customers in a separate act which has now been consolidated with the underlying appeal of the Town's rates. (Woodloch Exh. 1 at 16) These events have combined to put the Town in the difficult and precarious position of having to literally fight for its financial life and future in this rate case.

### **B. Legal Background**

This appeal has been pursued under authority of Tex. Water Code Sec. 13.043. Subsection (e) states that the "utility commission shall hear the appeal de novo and shall fix in its final order the rates the governing body should have fixed...". It further states that the "utility commission may consider only the information that was available to the governing body at the time the governing body made its decision and evidence of reasonable expenses incurred ...in the appeal proceedings. (Tex. Water Code § 13.043(e) (West Supp. 2014)) Additionally, Tex. Water Code § 13.043(j) states that "rates shall not be unreasonably preferential, prejudicial, or discriminatory but shall be sufficient, equitable, and consistent in application to each class of customers. The utility commission shall use a methodology that preserves the financial integrity of the retail public utility. (Tex. Water Code § 13.043(j) (West Supp. 2014)) Tex. Water Code § 13.002 (19) (West Supp. 2014) defines retail public utility to include a "municipality." Applicable PUC regulations mirror these statutory requirements 16 Tex. Admin. Code § 24.41 (2015). Precedent shows that the PUC has held that it is "limited to considering matters that could have been considered by the city council in setting....rates, except that it may also consider matters not available to the council for the limited purpose of helping it to understand matters

that were available to the council.” (Attachment 1 See issue No. 2 page 4) It is important to understand that the ALJ, and ultimately the PUC Commissioners, are not limited to considering only information actually used for the Town’s decision, but can also consider other items if they were available at the time and could have been considered by the Town Council, as well as later items under the limitation discussed above.

### **III. REVENUE REQUIREMENT**

The evidentiary record in this matter supports an overall revenue requirement for the Town’s water and sewer utility of \$344,174 per year. (Woodloch Exh. 10 at 11) This is the annual requirement for the entire water and sewer utility system, including the in-city and the out-of-city customers based on the information available to the Woodloch Council at the time of the rate-setting, January 18, 2013. (Woodloch Exh. 10 at 7-9; Woodloch Exh. 12)

The main components of this revenue requirement are (A) operation and maintenance (“O&M”) expenses; (B) debt service on existing, and known and measurable, anticipated capital expenditures; (C) a debt coverage ratio of 1.75 times that debt service amount (Woodloch Exh. 10 at 12; Woodloch Exh. 12); and (D) regulatory fees and costs to pay for compliance with Lone Star Groundwater District requirements.

#### **A. Operation and Maintenance (“O&M”) Expenses**

The water distribution system is composed of a 94,000 gallon ground storage tank, an aeration tower, 2 pressure tanks, 3 miles of distribution lines, 2 water supply wells, and 11 fire hydrants. (Woodloch Exh. 1 at 10) The sewer system is composed of a 120,000 gallon-per-day treatment plant, 9,500 linear feet of line in the collection system, and 5 lift stations (4 exclusionary out-of-city and 1 shared by both). (Woodloch Exh. 1 at 8) There are direct O&M expenses related to these components that are well-documented over the 20+ year life of the

system since the absorption of the Consumers CCN area, which is now the OOC portion of the overall system. Additionally, there are O&M expenses related to salaries, insurance, fees to state and local governments, engineering costs, contract operator expenses. The record of this matter identifies these ongoing costs and supports the reasonableness of that component of the cost-of-service. (Woodloch Exh.1 at 8-9 and 13; Woodloch Exh. 7 at 39-43; Woodloch Exh. 12; Woodloch Exh. 14)

The testimonies of Woodloch Mayor Diane Lincoln, City Engineer Michael Mathena, and rate analyst Angela Rubottom support the necessity and reasonableness of the Town's O&M expenses. Mayor Lincoln testified regarding the Town's historic expenses. Ms. Rubottom stated that the Town has a long-established system of categorizing and separating Town expenses from Utility expenses, and a system of assigning direct expenses of the out-of-city system maintenance and in-city customers maintenance on an invoice-by-invoice basis. (Tr. at 172-176 (June 2, 2015)) It also shows that common system expenses are generally assigned to in-city and OOC customers at a per-capita rate unless specific reasons warrant different treatment. (Woodloch Exh. 14; Woodloch Exh. 17) The O&M accounts used to categorize expenses are based on the line-item account standard set forth in the Texas Comptroller's Budgeting Manual for Texas Cities. (Tr. at 79-80) The expenses are also scrutinized in required annual audits. Combined, the utility O&M expenses items totaled \$217,262 based on 2011-2012 actuals. (Woodloch Exh. 12) Those total O&M expenses were broken down \$167,960 for OOC customers and \$49,302 for in-city. Based on the 2012-2013 budget (which was available and considered as part of the rate-setting) O&M utility expenses were projected to be \$195,247, split \$40,055 in-city and \$155,372 OOC. Id.



## **B. Debt Service**

The Town, at the time of adoption of the rates, carried no existing debts, but had made application for 3 loans that were then and still are critical to the future viability of the system. The Town had applied for a \$52,500 loan for the purchase and installation of an electronic water metering system that would reduce meter-reading expenses and provide critical feedback on water usage within the system which is important in the Town's Groundwater Reduction Plan. (Woodloch Exh. 7 at 45-62) The record in this case documents that the Council not only planned for this expense as part of its rate-setting, but also shows that the lender needed the Town's established rates to support the repayment of this loan before funding the loan. (Woodloch Exh. 7 at 246-254) The loan was, in fact, funded soon after the adoption of the rates. (Woodloch Exh. 7 at 46-62) The meter-reading system is in use and monthly payments of \$701.78 per month are being made by the Town to repay that loan. (Woodloch Exh. 25 at 6) The fact that the loan was funded shortly after the rate was adopted reflects the reality of the how such funding is provided in the real world and does not negate the reasonableness of the Town's action or its inclusion in the rate-setting. (Woodloch Exh. 25 at 5-6) To exclude that expense from the Town's revenue requirement would be to ignore a significant debt actually considered by the Council at the time of the rate-setting.

Another major item actually known and considered by the Council as part of its rate is the new ground storage tank purchased by the Town through a loan from Woodforest National Bank. (Woodloch Exh. 7 at 63-79) Woodloch's water system includes two ground storage tanks, however, one tank is offline and in need of demolition. (Woodloch Exh. 4 at 9) This new storage tank is an integral and necessary part of the water distribution system. The Town had been advised by its contract operator that the existing tank was in dire need of replacement because the existing tank was at risk of imminent failure. (Woodloch Exh. 8) The debt service

related to the loan which funded the storage tank was a major consideration at the time of the rate-setting and a known and measurable cost of approximately \$130,000 was discussed at Council meetings leading up to the January 2013 rate adoption. (Woodloch Exh. 7 at 246-255) Once the rate was adopted, the Bank agreed to the loan and the storage tank was constructed and put in service. (Woodloch Exh. 25 at 6) That tank is currently part of the system and monthly payments of \$2,410.96 (\$28,931.52/year) are being made by the Town funded by its increased rates. (Woodloch Exh. 25 at 6)

Finally, the Town applied in 2012 for a loan/grant combination from the Texas Water Development Board ("TWDB") to fund the much-needed improvements to the wastewater system, including a new treatment plant, refurbishment of the collection lines and the lift stations. (Woodloch Exh. 1 at 8-9; Woodloch Exh. 4 at 16-17) The Town Engineer assisted the Town in making application to TWDB, and the project was approved by that agency. The Town knew and considered the debt service for the loan portion of that approval in its rate-setting. (Woodloch Exh. 7 at 246-255) The TWDB loan/grant package was to be \$2,699,500 with approximately \$1,889,500 of forgiveness and the remaining carrying debt service of approximately \$48,000 annually for 25 years. (Woodloch Exh. 10 at 16; Woodloch Exh. 12 at 24) Unfortunately, before the grant and loan could be funded, this challenge to the rates was filed and TWDB funding withdrawn (after the rates were adopted) due to the uncertainty surrounding the Town's ability to repay the loan caused by the rate challenge. (Woodloch Exh. 1 at 14; Woodloch Exh. 10 at 9) However, at the time of the rate-setting, the Town knew and considered that debt-service amount as part of the rate-setting. The anticipated annual payments on that loan were included in the adopted rate. The Town has subsequently reapplied for that loan. (Woodloch Exh. 1 at 14-15)

Together these debt service items amount to \$86,041 annually. (Woodloch Exh. 12)

**C. Fees**

The Town has included in its rates 2 surcharges for fees related to the costs of compliance with the Lone Star Groundwater District (“District”) requirements. First, the District required Woodloch to participate in its mandatory 30% groundwater reduction program (“GRP”) to conserve groundwater in the Montgomery County area. (Tr. at 51-52 (June 2, 2015)) This required the Town to either join in with the San Jacinto River Authority (“SJRA”) to participate in its GRP, or to come up with a plan of its own that could be approved by the District. Id. Initially, the Town considered joining the SJRA GRP and adopted a surcharge to pass through the cost of preparing for and joining that plan. (Tr. at 52-57 (June 2, 2015)) Then the Town, upon finding the constructs of joining the SJRA plan to be a poor fit, was able to work with Bleyl Engineering to develop and submit a plan to the District to attain the 30% reduction through their own Town GRP. (Tr. at 78 (June 2, 2015)) At that time, the Town was not certain that the District would approve the Town’s GRP. If the District had not approved the Town’s GRP, the Town would have had to join the San Jacinto River Authority’s contract and would have had to pay fines, fees and penalties for missing the deadline for its GRP. (Tr. at 54 (June 2, 2015)) Fortunately, the Town’s GRP was approved by the District. (Tr. at 78 (June 2, 2015)) As the Town continues to have to deal with the groundwater protection program of the District, the Town continues to incur costs associated with filing updated plans to the District, and reserving money in case the Town exceeds (i.e., overuse) its allotment of water. (Tr. at 78 (June 2, 2015)) The Town’s GRP also has to be updated annually, which is a recurring cost item for Woodloch (Tr. at 16 (June 2, 2015); Tr. at 51-52 (June 2, 2015)). The \$0.90 per 1000 gallons per month “SJRA” surcharge on the Town’s tariff is to pay for the development and ongoing costs of this groundwater reduction plan (“GRP”) and to build up a reserve within the utility to pay penalties

to District should the utility's GRP fail to produce the required 30% reduction. (Tr. at 52-56 (June 2, 2015)) It is paid by both in-city and OOC customers. (Woodloch Exh. 3) This surcharge has a legitimate purpose. It pays for GRP costs and provides a reasonable reserve for potential fines or the purchase of credits should the utility customers be unable to meet the 30% reduction requirement through their self-policed conservation plan. (Tr. at 54-56 (June 2, 2015))

The other surcharge, labeled "Lone Star Groundwater Conservation District" on the Utility Tariff is a pass-through fee that funds the Town Utilities' fee to the District for its water supply contract. It is also paid by both in-city and OOC customers at the flat rate of \$1 per customer per month. The District charges the Town a rate of 6¢ per 1000 gallons of permitted water based on a fixed 36 million permitted gallons per year. (Woodloch Exh. 3; Tr. at 83, Tr. 51-53; Id.) This surcharge is a legitimate and reasonable method of assigning that cost to all utility customers.

The corresponding expense items to these two fees were lumped together under the Town's "Unfunded Mandates" line item and the funds collected by the surcharges were never used for non-utility expenses. (Tr. at 162-163 (June 2, 2015)) There have been occasions when those fund revenues dollars were used to pay for emergency items due to the inadequacy of the utility's earlier rate structure to build a reserve for that purpose, but that simply highlights the need for the rate increase so that revenue from those fees can be used for their original purpose. (Tr. at 168-169 (June 2, 2015)) The unfortunate labeling of the "SJRA" surcharge and the expense item of "Unfunded Mandates" should not take away from the two fees legitimate need and the propriety of the uses those funds have been put to.

#### **D. Debt Coverage Ratio**

The Town has experienced numerous unanticipated operational problems over the history of the system. There have been vandalism, water well break-downs and system failures that the

Town has had to pay to correct, often through the use of non-utility revenues such as ad valorem taxes. (Woodloch Exh. 1 at 9-10) The Town has also used its tax revenues to pay for costs and fees associated with the loans and grants it has sought or received over the years. (Woodloch Exh. 1 at 18) These issues also factored into the decision of the Town at the time of the rate-setting. In order to provide reserves for such future items, it is reasonable and justified for the rates to be adequate to build in an additional amount to accumulate for the likely future needs of the Utility. Rate expert Angela Rubottom testified that an appropriate method to use in determining the reserve is a debt-coverage multiplier. It is a method that is commonly used in the utility business, and is based on the debt-service amount of the Town. (Woodloch Exh. 10 at 6) Based on Ms. Rubottom overall analysis, the amount she testified would be appropriate was 1.75 times the Town's anticipated debt at the time of the rate-setting. (Woodloch Exh. 10 at 12) That would include the meter loan, the storage tank loan and the TWDB loan. This debt service ratio would create an additional income of approximately \$65,000 per year that would be a "safety-net" to respond to future unexpected repairs and capital items, and cover increased O&M expenses and service any debt that would be incurred to resolve system issues not addressed by the TWDB funds. (Woodloch Exh.10 at 13) It is also critical for the Utility's financial integrity, discussed further below herein.

#### **E. Revenue Requirement Summary**

Taken together, these four components make up the Town's utility revenue requirement of approximately \$344,000 per year. (Woodloch Exh. 10 at 11) Rubottom's testimony shows that the adopted rates of the Town for its combined water and sewer utility from both the in-city and OOC customers would be approximately \$351,000 per year. (Woodloch Exh. 12) Clearly the adopted rates are just, reasonable and necessary for the ongoing future of the utility and its customers.

#### IV. RATE DESIGN

At the Town Council meeting on January 18, 2013, the Council adopted rates that, based on the long term experience of the Town, the verified poor condition of the system, the known and measurable expenses of the utility and the anticipated loans to fund needed capital improvements, properly assigned costs of the water and the sewer expenses to the in-city and OOC customers fairly and reasonably. (Woodloch Exh. 10 at 13-14)

The evidence shows that the adopted rates for OOC customers are reasonable, fair and not discriminatory. When combined with the in-city rates, the total revenue anticipated from the rate tariff will create utility revenues of approximately \$351,740 per year. (Woodloch Exh. 12) This includes the water and the sewer rates for both in-city and OOC-customers. The basic service rates established by the Council in January 2013 are as follows:

##### BASIC SERVICE

	<i>Inside City Limits</i>	<i>Outside City Limits</i>
<b><i>Residential</i></b>		
Water (min 2000gal).....	29.50.....	59.00
2001 – 14999 .....	\$2.40/1000gal.....	\$4.80/1000gal
15000 – 24999 .....	\$2.95/1000gal.....	\$5.90/1000gal
25000 – 34999 .....	\$3.50/1000gal.....	\$7.00/1000gal
35000 – 44999 .....	\$4.00/1000gal.....	\$8.00/1000gal
45000 – Over .....	\$7.00/1000gal.....	\$14.00/1000gal
Sewer .....	\$30.00.....	\$60.00
Garbage .....	\$15.00 plus tax.....	Service Not Provided
Lone Star Groundwater Conservation Dist .....	\$1.00.....	\$1.00
San Jacinto River Authority.....	\$.90/1000gal.....	\$.90/1000gal

This combined water and sewer system was two entirely separate systems until the TNRCC approached the Town and requested that it take on the Consumer's Water Corporation's system in 1994. This was not something the Town sought on its own and only agreed to it after being assured that the TNRCC would provide assistance and funding to the combined utility system as needed. Unfortunately that assistance never materialized. (Woodloch Exh. 1 at 11)

After the merger, it became apparent that the Consumer's Water Corporation system was in poor condition and would incur a much higher per-capita cost for operation and maintenance than the Town had experienced with its own system. (Woodloch Exh. 1 at 12) The infiltration and inflow from the OOC areas cause increased costs of repair and maintenance for those components. (Woodloch Exh. 4 at 11-12) The wastewater treatment plant, as previously discussed was purchased to accommodate the overall system and would not have been purchased but not for the combination of the two separate systems in 1994. The system has 4 of its 5 lift stations outside the city boundaries and those serve only the OOC customers. (Woodloch Exh. 4 at 12) The fifth lift station serves both in-city and OOC customers. (Tr. at 60-61 (June 2, 2015)) These lift stations have had vandalism incidents at a much higher rate over the years, than has the lone in-city lift station. Emergency repairs have also occurred at a higher per-customer rate than the in-city areas. (Tr. at 118-120 (June 2, 2015)) Additionally, a wastewater treatment plant had to be purchased to provide capacity to treat the higher volumes of wastewater. The Town purchased a used WWTP, which, 20 years later is in such poor condition that it needs to be replaced. (Woodloch Exh. 4 at 8) Were it not for the combining of the two systems, that unit would not have been purchased and the utility would only have one lift station, not five. (Woodloch Exh. 1 at 7-8)

The water system has approximately 3 miles of distribution system. (Woodloch Exh. 1 at 10) Two out of three linear feet of water and sewer lines reside in the OOC service area. (Woodloch Exh. 1 at 17) Though operated as one system, the fact is that, if it were not for the historic combining of the Town system and the Consumer's Water Corporation's system in 1994, the Town system would be much smaller and less difficult to operate and maintain. The additional complexity of the combined system creates a need for redundancy of components,

such as the pressure tanks, additional issues with leakage losses and other maintenance that it would not otherwise have. Historically the Town has a disproportionate number of issues with the OOC service area in that regard. (Woodloch Exh. 1 at 17-18)

The facts are that the cost of service is significantly higher per customer to serve OOC as compared to in-city customers. The difference exceeds what the rates previous to the adoption of the 2013 rates reflected. The unit cost differential is 1.7 times the OOC cost compared to the in-city amounts. (Woodloch Exh. 10 at 13-14; Woodloch Exh. 12) The FY 2012-2013 budget unit cost of service for outside Town customer is \$138 per OOC customer per month. *Id.* The adopted rates produce an average annual revenue of \$146.00 per OOC customer per month. Based on the past and expected future unit cost of providing service to OOC customers, the adopted OOC rates are reasonable. The adopted rates for the in-city customers produce an average annual revenue of \$72.51 per in-city customer per month. The ratio of the OOC unit cost of service to the inside Town average annual cost per customer is at least 1.7 times. (Tr. at 161-167) The adopted rates for the OOC customers will result in an average monthly revenue to the Utility of approximately \$146.00 per OOC customer. (Woodloch Exh. 10 at 13-14 and Tr. at 168-172 (June 2, 2015)) Finally, a comparison of OOC rate differentials for surrounding areas was conducted by the Town. (Woodloch Exh. 16) Exhibit 16 shows that other area municipal utilities differentials range from 1.2-1.8 times higher for OOC customers compared to in-city customers.

Finally, the Town has had to use its tax and other non-utility revenues to prop up the utility on numerous occasions over the years. (Woodloch Exh. 1 at 17-18) For instance, the Town tax revenues of approximately \$10,000 were used to pay the utility's portion of a CDBG grant. *Id.*



For all these reasons, the Town is justified in assigning a 2.0/1 overall rate differential between the OOC and the in-city customers. *Id.* That differential is based upon legitimate factors and is not unreasonable or discriminatory.

## **V. RATE CASE EXPENSES**

The evidence in the record shows that the rate case expenses through 5/31/2015 were over \$200,000. This is a high amount for such a small utility customer base. However, it has been proven to be reasonable and necessary in this case. As such, Woodloch is statutorily entitled to recover its reasonable rate case expenses. Each of the attorneys and consultants submitted their invoices with details regarding their billing and testified under oath that their bills were for actions in support of this rate appeal. Attorney Norton's bills represent the vast majority of the total amount. (Woodloch Exh. 22; Woodloch Exh. 35-37) The evidence shows that he was hired by the Town specifically to represent it in this case. (Woodloch Exh. 20 at 5) His bills, his testimony and the work product submitted in this matter over the course of the legal proceeding support the hours incurred on behalf of Woodloch in this matter. *Id.* No one disputed any material part of his billings. His rate was shown through his testimony and the testimony of the PUC staff to not be unreasonable in light of his particular experience and skills. (Woodloch Exh. 20 at 3-4) (PUC Prefiled Testimony Leila Guerrero at 13) Mr. Norton is Board Certified in Administrative Law by the Texas Board of Legal Specialization. *Id.* (Woodloch Exh. 21) He has almost 30 years of experience in administrative contested case hearings before the TCEQ and other agencies. *Id.* This includes participation in many water and /or sewer rate proceedings. *Id.*

Marcia Tillman's testimony shows that she has duties as the City Attorney for Woodloch that are not related to this matter. (Woodloch Exh. 18; Woodloch Exh. 31) It also establishes

that she has spent considerable time directly in pursuit of this matter. (Woodloch Exh. 32) She separately accounted for her work as City Attorney and her efforts in this matter. (Id. and Tr. at 187-188 (June 2015)) Her billings in this matter were shown to be reasonable and justified, including her work advising the Town prior to the hiring of Norton and later in both advising and in taking the lead in the preparation of the prefiled testimony for the Mayor and herself. (Woodloch Exh. 18 at 4) There is no credible evidence that casts doubt on that testimony or the exhibits that show her billings in pursuit of this matter.

Similarly, Michael Mathena, the City Engineer for Woodloch submitted his company's billings in pursuit of this matter and supported the reasonableness and validity of those bills through his testimony. (Woodloch Exh. 25-26) The engineering needs and the condition of the utility are the areas of focus in his testimony. Those issues are relevant and material to the matter of this rate increase and no objection to that testimony's relevance was sustained or even raised in this case.

Finally, Angela Rubottom was hired by the Town to forensically review the overall financial status of the Town at the time of the rate-setting according to information available to the Town Council at that time, and based on that review, apply her expertise to assessing the Town's revenue requirements and rates based on the relevant statutory factors. She kept track of her time and tasks and submitted reasonable bills for that work to the Town. (Woodloch Exh. 30) No challenge was made to the validity of her bills or time spent on her tasks and her analysis, including the many detailed spreadsheets and other financial analyses accepted into the record in this case, and form the basis of much of the Town's position in this matter. The PUC witnesses testified that, because she was only hired after the rates were set, her testimony could not be considered by them in their review. (Tr. at 367-372 (June 3, 2015)) They then argued

that her fees should not be included in the Town's rate case expenses. *Id.* This argument defies logic and is contrary to the plain language of the statute and precedent in such matters. (Attachment 1) It cannot form the basis for the exclusion of her legitimately incurred fees being included as a valid rate case expense.

All told, the record supports that the legitimate rate-case expenses that are eligible to be reimbursed through customer charges is approximately \$230,000. (Woodloch Exh. 25 at 4; Woodloch Exh. 26; Woodloch Exh. 27 at 6; Woodloch Exh. 30; Woodloch Exh. 31 at 2-3; Woodloch Exh. 32; and Woodloch Exh. 34-37) The Town elected to begin charging the OOC customers for this cost in August 2014, pursuant to its June 2014 rate action. At that time it began charging \$35/OOC customer/month. That action was, as previously discussed, appealed to the PUC by the OOC customers and ultimately consolidated with the original appeal of the actual utility rates. The record shows that the Town charged only the OOC customers this rate for 9 months<sup>2</sup> (Woodloch Exh. 27 at 3) and then adopted the same \$35 per month surcharge to the in-city customers as well. (Woodloch Exh. 23 at 6; Woodloch Exh. 24C) The testimony shows that it will take approximately 14 months for the OOC customers and 23 months for the in-city customers to pay the existing, proven rate-case expenses on the basis of a pro-rata distribution among all customers. (Woodloch Exh. 27 at 3)<sup>3</sup> This is a fair, reasonable and non-discriminatory outcome.

The PUC staff has argued that no rate case expenses should be assessed in this case because the rates adopted by the Town are not just and reasonable and therefore the rate case expenses cannot be assessed at all. As discussed above, the Town has proven that its rates are

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<sup>2</sup> The testimony shows 8 months, but the in-city surcharge was actually begun on August 2014, 9 months after the OOC customers began being charged.

<sup>3</sup> That payback period was based on a lower rate case expense than was actually incurred through May 31, 2015. Therefore a longer payback period is actually justified.

just and reasonable and not discriminatory, and should be upheld in this appeal. Clearly, if that is true, the rate case expenses incurred in its pursuit are also valid and should be reimbursed.

## **VI. FINANCIAL INTEGRITY OF THE UTILITY**

It is a statutory requirement that the financial integrity of the utility be considered when setting the final rate for the utility. (Tex. Water Code §13.043 (j)) (West Supp. 2014). The only thoughtful analysis in the record regarding the financial integrity of the Town's utility supports the conclusion that a rate which establishes a revenue equal to, or near equal to the \$344,174 per year that the adopted rate produces will protect the financial integrity of the utility. (Woodloch Exh. 10 at 11-12) Angela Rubottom, the most experienced and credible rate expert who testified at the hearing, said that "(t)he Town's financial integrity would not be able to be maintained" if the PUC staff's recommendation in this case were to be adopted. (Woodloch Exh. 27 at 3-5; Woodloch Exh. 29) No one else performed any analysis of the effect of the rates or the surcharge on the utility's financial integrity. No PUC or appellant witness provided any informed opinion on the financial integrity issue. In fact when specifically asked, two of the PUC witnesses stated they had not investigated the issue and had no opinion regarding the effect of their opinions on the financial integrity of Woodloch or its utility. (Tr. at 342-343, Tr. at 383-384 (June 3, 2015)) PUC witness Fred Bednarski testified that 10% of his recommended revenue requirement be added for financial integrity but could provide no basis or analysis to support that recommendation. (Tr. at 283-287, 296-297 (June 3, 2015)) The only position supported by the record in this matter is that the Woodloch requires a rate that produces revenues equal or near its adopted rates to maintain its financial integrity. (Woodloch Exh. 27 at 4; Woodloch Exh. 29; Woodloch Exh. 10 at 10-12) The PUC staff's recommendation would render the utility insolvent. (Id.; Woodloch Exh. 27 at 3-6; Woodloch Exh. 28; Woodloch Exh. 29)

This fact alone, requires that the ALJ and the PUC institute a rate to support that revenue level. To do otherwise would be unsupported and contradictory to the only financial integrity evidence in this record. More importantly, the PUC's recommendation would render the Town's utility insolvent and unable to pay its debts and expenses, much less make the needed capital improvements to its system. This would be to the serious detriment of all of the Utility's customers, both in-city and OOC.

## **VII. CONCLUSION**

For the reasons stated above, the Town of Woodloch respectfully requests that the ALJ rule that the Town's adopted water and sewer utility rates, and the surcharge, are just and reasonable, not discriminatory, and are necessary to protect the financial integrity of the Town and its utility. Woodloch further requests that it be granted any other such relief to which it has proven to be justly entitled.

Respectfully submitted,

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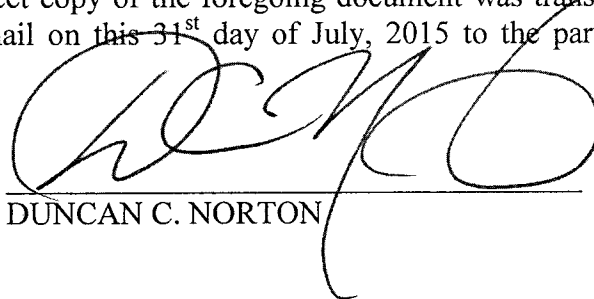
Duncan C. Norton

State Bar No. 15103950

**ATTORNEY FOR TOWN OF WOODLOCH**

## CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing document was transmitted by e-mail, fax and/or regular, first class mail on this 31<sup>st</sup> day of July, 2015 to the parties of record.

  
DUNCAN C. NORTON

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SOAH DOCKET NO. 473-13-0935  
PUC DOCKET NO. 40627

PETITION BY HOMEOWNERS UNITED §  
FOR RATE FAIRNESS TO REVIEW §  
AUSTIN RATE ORDINANCE NO. §  
20120607-055 §

PUBLIC UTILITY COMMISSION

OF TEXAS

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### SUPPLEMENTAL PRELIMINARY ORDER

This Order provides the Commission's determination on threshold legal issues identified by the Commission in its November 9, 2012 briefing order. The petitioners in this docket, Homeowners United for Rate Fairness, ratepayers of Austin Energy who are outside the City of Austin, filed an appeal of the rate ordinance adopted by the Austin City Council in June. This docket was referred to the State Office of Administrative Hearings (SOAH) on November 5, 2012 and the Commission issued its preliminary order in this docket on November 16, 2012. On November 9, parties were requested to submit briefs regarding the 185-day deadline in PURA<sup>1</sup> § 33.054(c) and the known and measurable changes to the test-year that can be considered in this docket. The parties were notified that the Commission would consider a supplemental preliminary order to address the issues briefed. Austin Energy, Commission Staff, Office of Public Utility Counsel, Homeowners United for Rate Fairness, and Data Foundry, Inc. filed responses to the order requesting briefing.

#### I. Supplemental Threshold Legal/Policy Determinations

The following statements of position were reached in consideration of the arguments of the parties:

**Issue No. 1** *Can the 185-day deadline in PURA § 33.054(c) be extended?*

The Commission concludes that the 185-day deadline in PURA § 33.054(c) is mandatory and cannot be extended.

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<sup>1</sup> Public Utility Regulatory Act, TEX. UTIL. CODE ANN. §§ 11.001-66.016 (Vernon 2007 & Supp. 2011) (PURA).

This proceeding involves an appeal of the rates of Austin Energy, a municipally owned utility, and the “Commission *must* enter a final order on or before the 185th day after the date the appeal is perfected or the utility files a rate application.”<sup>2</sup> If the Commission does not enter a final order before the 185th day, “the rates proposed by the [municipal] utility are considered to be approved by the Commission and take effect on the expiration of that period.”<sup>3</sup> When a statute uses the word *must* and includes a penalty for non-compliance, the requirement is mandatory.<sup>4</sup> Thus, the plain language of the provision indicates that the deadline is mandatory and cannot be extended.

The Commission contrasts that requirement with the requirement found in PURA § 36.108 that similarly provides that the proposed rates of the utility are “considered to have been approved” if the Commission (or any other regulatory authority) does not make a final determination before the specified deadline.<sup>5</sup> That approval, however, “is subject to the authority of the regulatory authority to continue a hearing in progress.”<sup>6</sup> In addition, where the Commission inquires into a utility’s rates, if the Commission has not issued a final order (or established temporary rates) by the prescribed deadline, then the rates “automatically become temporary rates”<sup>7</sup> subject to refund or possible surcharge.<sup>8</sup> The lack of any such qualifications to the statutory approval of a municipally owned utility’s rates provided in PURA § 33.054(c) supports the conclusion that the deadline is mandatory and not extendable.

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<sup>2</sup> PURA § 33.054(c).

<sup>3</sup> PURA § 33.054(f).

<sup>4</sup> *TJFA, L.P. v. Texas Com'n on Env'tl. Quality*, 368 S.W.3d 727, 734 (Tex. App.—Austin 2012, pet. denied).

<sup>5</sup> PURA § 36.108(c).

<sup>6</sup> *Id.*

<sup>7</sup> PURA § 36.156.

<sup>8</sup> PURA § 36.155.



In 1989 the legislature amended former PURA § 26(e)<sup>9</sup> to add language requiring the Commission to issue its final order “for proceedings involving the rates of a municipally owned utility, within 185 days from the date on which the appeal is perfected or on which the utility files a rate application as prescribed by Subsection (c) of this section.”<sup>10</sup> This amendment removed rate appeals for municipally owned utilities from the general deadline of 185 days from the date the appeal was perfected. Austin Energy asserts that this amendment also indicates that the 185-day deadline for municipally owned utilities is mandatory and not extendable.<sup>11</sup> Quoting from a bill analysis, Austin Energy states that the legislature was seeking to remedy the reduced time the Commission had to decide such an appeal.<sup>12</sup> Thus, Austin Energy states: “If the legislature intended for the Commission to be able to extend this jurisdiction deadline, no such amendment to PURA would have been necessary.”<sup>13</sup> The Commission agrees that this amendment further supports the conclusion that the 185-day deadline is mandatory and cannot be extended.

Several parties also discuss the fact that the effective date for rates of an investor-owned utility are extended by the utility when appealed and consolidated with rate cases at the Commission.<sup>14</sup> On this point, the Commission just notes that the requirements for those appeals are different than for municipally owned utilities.

Finally, the Commission takes note that Austin Energy requested leave to supplement its rate-filing package on December 12, 2012. It asserted that the unique nature of this case, the

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<sup>9</sup> Public Utility Regulatory Act, 64th Leg., R.S. ch. 721, §26, 1983 TEX. GEN. LAWS 2327, 2337, formerly compiled as TEX. REV. CIV. STAT. art 1446c §26, *repealed by* Public Utility Regulatory Act of 1995, 74th Leg., R.S., ch. 9, § 2, 1995 Tex. Gen. Laws 31, 87.

<sup>10</sup> Act of May 28, 1989, 71st Leg., R.S. ch. 325, § 2, 1989 TEX. GEN. LAWS 1287 (repealed 1995).

<sup>11</sup> Austin Energy’s Brief on Threshold Legal/Policy Issues at 3 (Nov. 28, 2012). (Austin Energy’s Brief).

<sup>12</sup> *Id.* (citation omitted).

<sup>13</sup> *Id.*

<sup>14</sup> Austin Energy’s Brief at 4; Commission Staff’s Brief on Threshold Legal and Policy Issues at 1-2 (Nov. 28, 2012).

lack of prescribed rate-filing-package forms for a municipally owned utility, and uncertainty as to the nature of the review are good cause for the Commission to extend the 90-day filing period in PURA § 33.104 to December 12, 2012.<sup>15</sup> The SOAH administrative law judges (ALJs) assigned to this case granted this motion.<sup>16</sup> The judges recognized that the motion was directed at the Commission, but given that the Commission could not act before its open meeting scheduled for December 13, the judges found it appropriate to rule on the motion. While not properly before the Commission for action, the Commission supports the ALJs' analysis and action. Consequently, the Commission understands that the 185-day deadline will now be measured from December 12, 2012, the date that Austin Energy will file, with permission, its completed rate-filing package.

In summary, PURA does not give the Commission authority to extend the deadline for the effective date of rates in proceedings involving the rates of a municipally owned utility.

**Issue No. 2** *Does the requirement in PURA § 33.054(a) that the Commission use the same test-year presented to the municipality and the requirement in PURA § 33.054(b) that the Commission establish rates the Commission determines the municipality should have set limit the known and measurable changes to those used by the City of Austin to set rates, or otherwise limit known and measurable changes that can be considered in this docket?*

The Commission is limited to considering matters that could have been considered by the city council in setting Austin Energy's rates, except that it may also consider matters not available to the council for the limited purpose of helping it to understand matters that were available to the council.

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<sup>15</sup> Joint Motion for Leave to File Supplemental Direct Testimony and Request for Expedited Ruling (Nov. 21, 2012).

<sup>16</sup> Order No. 2 (Nov. 28, 2012).

As discussed above, this appeal is under PURA § 33.101. Such appeals are subject to de novo review by the Commission based on the test-year presented to the municipality.<sup>17</sup> Furthermore, PURA § 33.054(b) requires the Commission to enter a final order establishing rates that the Commission determines the municipality should have set in the ordinance to which the appeal applies.

OPC argues that because this proceeding is de novo, the Commission must “conduct an independent fact finding” and take evidence and determine all issues “anew.”<sup>18</sup> It further asserts that the Commission must “exercise its own judgment and redetermine each issue of fact and law” and “is to accord absolutely no deference to the City of Austin’s rate ordinance under review.”<sup>19</sup> While the Commission agrees with OPC that it must decide this matter as if the City of Austin had not acted,<sup>20</sup> the Commission also observes that there are limitations on what information the Commission can consider in this appeal.

The Commission must “establish the rates the Commission determines the municipality should have set in the ordinance to which the appeal applies.”<sup>21</sup> The Commission has previously construed similar language in a previous version of PURA. Former PURA § 26(g) directed the Commission to “fix such rates as the municipality should have fixed in the ordinance from which the appeal is taken.”<sup>22</sup> In a prior appeal of Austin Energy’s rates, the hearing’s examiner stated that the Commission had construed this language “to mean that the Commission cannot take into

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<sup>17</sup> PURA § 33.054(a).

<sup>18</sup> Office of Public Utility Counsel’s Response to the Commission’s Order Requesting Briefing on Threshold Legal/Policy Issues at 5 (Nov. 28, 2012). (OPC’s Brief).

<sup>19</sup> *Id.*

<sup>20</sup> See *Petition for Review of Certain Ratemaking Actions of the City of Austin*, Docket No. 6560, Examiner’s Report at 12 P.U.C. Bull. 1311, 1319-1326 (Apr. 25, 1986).

<sup>21</sup> PURA § 33.054(b).

<sup>22</sup> Act of May 29, 1989, 71st Leg., R.S., ch. 1167, § 1 1989 Tex. Gen. Laws 4795, 4798, formerly compiled as TEX. REV. CIV. STAT. art 1446c, *repealed by* Public Utility Regulatory Act of 1995, 74th Leg., R.S., ch. 9, § 2, 1995 Tex. Gen. Laws 31, 87.

account events which occurred after the municipality acted.”<sup>23</sup> After discussing this matter further, the examiner concluded that the “Commission determined it could use any data compilations or reports, even if issued after [the ordinance was passed], for the purpose of determining the conditions in existence as of that date.”<sup>24</sup> Events occurring after the passage of the ordinance were deemed admissible for the limited purpose of “shed[ding] light on what conditions were in existence as of the time the city council acted.”<sup>25</sup>

Therefore, in determining what known and measurable changes are to be considered for its de novo review of the Austin rate ordinance in this docket, the Commission may only consider known and measurable changes that were available to the Austin City Council at the time the ordinance was passed—June 7, 2012. To the extent that there is evidence available to the Commission that was not available at the time the city council made its decision, the evidence would only be admissible for purposes of determining what conditions existed at the time the city council acted.

#### IV. Effect of Supplemental Preliminary Order

The Commission’s discussion and conclusions in this Order regarding threshold legal issues should be considered dispositive of those matters. Questions, if any, regarding threshold legal and policy issues may be certified to the Commission for clarification if the SOAH ALJ determines that such clarification is necessary. The SOAH ALJ, upon his or her own motion or upon the motion of any party, may deviate from the non-dispositive rulings of this Order when circumstances dictate that it is reasonable to do so. Any ruling by the SOAH ALJ that deviates from this Order may be appealed to the Commission. The Commission will not address whether this Order should be modified except upon its own motion or the appeal of a SOAH ALJ’s order. Furthermore, this Order is not subject to motions for rehearing or reconsideration.

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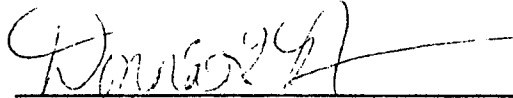
<sup>23</sup> Docket No. 6560, 12 P.U.C. BULL. at 1326 citing *Appeals of Dallas Power and Light Company from Ratemaking Ordinances of the City of Dallas et. al.*, Docket No. 5572, 10 P.U.C. BULL. 1315 (Apr. 12, 1985).

<sup>24</sup> *Id.*, 12 P.U.C. BULL. at 1328.

<sup>25</sup> *Id.*

SIGNED AT AUSTIN, TEXAS the 13<sup>th</sup> day of December 2012.

PUBLIC UTILITY COMMISSION OF TEXAS



DONNA L. NELSON, CHAIRMAN



KENNETH W. ANDERSON, JR., COMMISSIONER

  
ROLANDO PABLOS, COMMISSIONER

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