TCMUD 12's demand for wholesale water service was not anywhere close to the amount specified in the Agreement.[202]

There were comparable provisions in other Wholesale Water Service Agreements transferred or assigned to WTCPUA from LCRA,[203]which evidences that this was not a provision negotiated by TCMUD 12 but that LCRA required this provision be included in all of the contracts with its wholesale customers. WTCPUA's argument that TCMUD 12 is not required to take wholesale water services from the PUA, but rather "it is completely up to TCMUD 12 as to whether to use such capacity"[204] may be based on the following: In the contract amendments entered into by six of WTCPUA's wholesale customers, Section 3.03 of each of the original Wholesale Water Services Agreement (or the comparable provision with a different number) is deleted.[205] Since WTCPUA has imposed other provisions of the standard Contract Amendment (related to rate methodology) on TCMUD 12 even though TCMUD 12 did not accept the Contract Amendment, WTCPUA may believe that it can also ignore the obligations that arise under Section 3.03.c. of TCMUD 12's Wholesale Water Service Agreement. Of course, WTCPUA did not present affirmative evidence that it would not object to TCMUD 12 obtaining wholesale water services elsewhere.

vi. City of Austin is not an Alternative Provider of Wholesale Water Services Available to TCMUD 12

The City of Bee Cave and WTCPUA argue in Briefs that Mr. DiQuinzio should have exerted some effort to seek a service contract with the City of Austin.[206] The City provides no time frame or reference to any rule or statute that would require TCMUD 12 to seek a service contract from the City of Austin, but WTCPUA nonetheless argues that TCMUD 12 had an

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[202] TCMUD 12 Exhibit No. 1 at JAD Exhibit 4, Section 3.03.c.

[203] TCMUD 12 Exhibit No. 8 (Hays County WCID #1) at Section 3.03.b; TCMUD 12 Exhibit No. 11 (Hays County WCID #2) at Section 3.03.b; TCMUD 12 Exhibit No. 14 (Reunion Ranch) at Section 3.03.b; TCMUD 12 Exhibit No. 17 (Senna Hills MUD) at Section 3.03.d; TCMUD 12 Exhibit No. 19 (Lazy Nine MUD) at Section 3.03.c; and TCMUD 12 Exhibit No. 21 (Barton Creek West WSC) at Section 8

[204] WTCPUA Brief at 41-42.

[205] TCMUD 12 Exhibit No. 18 (Hays County WCID #1 Amendment) deletes section 3.03; TCMUD 12 Exhibit No. 10 (Hays County WCID #2 Amendment) deletes and replaces 3.03 w/o any comparable provision; TCMUD 12 Exhibit No. 13 (Reunion Ranch Amendment) deletes Section 3.03; TCMUD 12 Exhibit No. 16 (Senna Hills MUD Amendment) deletes Section 3.03;TCMUD 12 Exhibit No. 18 (Lazy Nine MUD Amendment) deletes Section 3.03; and TCMUD 12 Exhibit No. 20 (Barton Creek West WSC Amendment) deletes Section 8.

[206] Bee Cave Brief at 3; WTCPUA Brief at 49.

obligation to investigate that over a five + year period (January 1, 2009 through March 6, 2014). This is the type of hypothetical alternative dreamed up by the Respondents for cross-examination, and which was completely discredited[207] by Mr. DiQuinzio's unchallenged testimony that the City of Austin is not a viable alternative wholesale water service provider because the City's WTP is "extremely far away" from The Highlands, and The Highlands are not in the City's CCN water service area.[208]

vii. TCMUD 12's Burden of Proof Does Not Extend to Proving Up the Costs and Expenses for Every Hypothetical Alternative Service Provider Suggested by Respondents

WTCPUA advances the unusual argument that TCMUD failed to provide evidence "demonstrating the *costs* of utilizing Lakeway MUD, HCMUD, City of Austin, or any other alternate service provider"[209] and suggests that alternative costs should also include a consideration as to whether TCMUD 12's operating *expenses* could thereby be reduced.[210] This argument is without merit for the simple reason that it rests on the assumptions that the alternatives identified are viable, which TCMUD 12's evidence effectively rebuts; and if the alternatives were viable, it assumes, without proving, that there might be savings to be had in expenses, e.g., O&M. Neither assumption is supported by evidence. As to the operating expense argument, WTCPUA is venturing perilously close to a cost of service analysis – which WTCPUA argues elsewhere must be studiously avoided. TCMUD 12 urges the Administrative Law Judge to give these arguments no weight.

viii. WTCPUA's Confusion About Its Obligation to Provide 3.98 MGD for TCMUD 12

WTCPUA undertakes an unusual but fatally flawed mathematical analysis to arrive at the erroneous conclusion that "TCMUD 12 can only ask WTCPUA to divert, treat, and deliver 1,137,500 gallons of *raw* water per day."[211] WTCPUA's starting point is the Raw Water Contract, under which TCMUD 12 is entitled to 1,680 acre-feet (547,429,680 gallons) of raw

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[207] Tr. at 79.

[208] Tr. at 108.

[209] WTCPUA Brief at 49.

[210] WTCPUA Brief at 53.

[211] WTCPUA Brief at 54 – 55.

water **per annum.**[212] WTCPUA's first error occurs when it divides that gallonage by 365 days (per year) to arrive at approximately 1.5 million gallons **per day**. This is an error because the Raw Water Contract does not place a limit on the **daily** diversion rate, and under normal demand, the daily diversion rate would be expected to fluctuate – sometimes higher, sometimes lower, but not limited to the 1.5 MGD *average* WTCPUA calculates. The limitation in the Raw Water Contract is an annual, not a daily limit as WTCPUA presumes.

The Wholesale Water Service Agreement however does have a maximum diversion or flow rate which is 3.98 million gallons per day, or a peak hourly flow of 414,000 gallons per hour.[213] LCRA committed to provide treated water to TCMUD 12 at those flow rates, and under the Transfer Agreement, that is now WTCPUA's obligation.[214] WTCPUA's argument that it is not obligated to provide to TCMUD 12 3.98 MGD but only 1,137,500 gallons of *raw* water per day is incorrect under the Wholesale Water Services Agreement. WTCPUA's obligation is to divert, transport and treat for TCMUD 12 all water needed and requested up to, but not in excess of a peak hourly flow rate of 414,000 gallons per hour and maximum daily flow rate of 3,980,000 gallons per day. WTCPUA argues that "the truth here is a moving target,"[215] but TCMUD 12 is willing to assume that WTCPUA's error about its obligation to supply a daily flow rate of 3.98 MGD of potable water for TCMUD 12 under the Wholesale Water Service Agreement is an *inadvertent* calculation error and not a purposeful mis-statement of the "truth."

2. Are There Other Disparate Bargaining Power Factors?

(a) The Terms of the Wholesale Water Services Agreement Evidence WTCPUA's *NOT* TCMUD 12's Disparate Bargaining Power

(i) WTCPUA's Unilateral Right to Change the Monthly Charge and Volume Rate

WTCPUA argues that the Wholesale Water Services Contract does *not* allow it to set rates "at any time" or without limitations, citing to Section 4.01 and 4.03.[216] WTCPUA's reliance on Section 4.01 in support of this contention suggests a complete mis-understanding of

[212] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at JAD Exhibit 2 p. 4 of 76.

[213] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at JAD Exhibit 4, Section 3.03.a.

[214] Mr. Rauschuber agrees WTCPUA is *required* to provide wholesale water services to TCMUD 12 up to a maximum daily flow rate of 3,980,000 gallons per day. WTCPUA Exhibit No. 1 at 31:4-5.

[215] WTCPUA Brief at 55 (first full paragraph).

[216] WTCPUA Brief at 16 (first bullet).

the Wholesale Water Services Agreement, because Section 4.01.f. begins with the words: "At any time while this Agreement is in effect, LCRA, subject to applicable law, may modify the Connection Fee, the Monthly Charge and the Volume Rate consistently with the terms of this Agreement . . .". It is unclear given this contention, what, if any, effect WTCPUA as the current seller, gives to the contractual words "At any time."

WTCPUA also claims incorrectly that TCMUD 12 has admitted that WTCPUA does not have the unilateral right to change the rates which are the subject of this Appeal.[217] WTCPUA's reliance on WTCPUA Exhibits 78 and 79 in support of this argument is not persuasive. TCMUD 12's responses to RFIs 4-27 and 4-28 states that under the Transfer Agreement and the Wholesale Services Agreement, WTCPUA has the right to change the Monthly Charge and the Volume Rate in accordance with the Water Services Agreement. As indicated, Section 4.01.f of the Wholesale Water Services Agreement[218] is unequivocal on this point, conferring on the Seller (formerly LCRA and now, WTCPUA) the unilateral right to change the rates at any time.

In the Transfer Agreement, WTCPUA agreed that it would "bill and collect payment from the District in strict accordance with the terms and conditions of the Water Services Contract."[219] Although another provision of the Transfer Agreement prohibits WTCPUA from changing the Connection Fee, WTCPUA exercised its disparate bargaining power by changing the TCMUD 12 Connection Fee, in direct violation of its contractual rights.[220] WTCPUA unilaterally changed a rate (Connection Fee) even when it was expressly prohibited from doing so, and it exercised its unilateral right to change the Monthly Charge and Volume Rate for TCMUD 12 for 2014 in accordance with the express terms of the long-term contract with TCMUD 12.

WTCPUA's unilateral contractual authority to change the rates is the exact situation contemplated when the Public Interest rules were adopted in 1994: "*Over time the seller*

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[217] WTCPUA Brief at 19, fn 36 (last sentence) (citing to WTCPUA Exhibits 78 and 79).

[218] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at 151, JAD Exhibit 4 at page 12 of 27.

[219] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at 169, JAD Exhibit 5, page 3 of 8 (section 3 – last sentence).

[220] TCMUD 12 is *not* challenging WTCPUA's November 1, 2012 change to the Connection Fee. *See,* TCMUD 12 Initial Brief at 37 – 38.

exercises near monopoly power over the purchaser because many agreements allow the seller the unilateral right to adjust the rate."[221]

(ii) ***The Wholesale Water Services Agreement Does Not Bestow Disparate Bargaining Power on TCMUD 12***

The only witness presenting testimony at the hearing who was involved in any way in the Wholesale Water Services Agreement and the Transfer Agreement was Mr. DiQuinzio. Based on his experience, bargaining power exists only if both sides to an agreement or contract have alternatives, and TCMUD 12 has never had alternatives to its Wholesale Water Service Agreement in order to provide potable waters to the Districts' customers in The Highlands. In TCMUD 12's dealings with LCRA, and then with WTCPUA after it took over operations from LCRA, TCMUD 12 had no alternative means of obtaining wholesale water service.[222] PUC Staff argues that "TCMUD 12 had *adequate opportunity* to participate in both the formation of the LCRA Wholesale Agreement and the PUA Transfer Agreement," presumably in support of the position that WTCPUA has not exercised disparate bargaining power.[223]

TCMUD 12, most of WTCPUA's other wholesale customers, as well as WTCPUA itself, purchase raw water under their respective contracts from LCRA because LCRA has the water rights to all the surface water in the Highlands lakes.[224] After TCMUD 12 secured an LCRA Raw Water Contract for 1,680 acre-feet (547,429,680 gallons) of water in September 2008, it began discussions with LCRA, the only wholesale supplier of water services, about how to get the water out of the Lake, transmitted to a WTP, treat it, and then deliver it to The Highlands for ultimate sale to end-use customers.[225] After a delay during which LCRA explored but eventually abandoned constructing a new "Highlands WTP," the Wholesale Water Services Agreement was executed.[226] Under that Agreement, the *quantity* of water to be diverted, treated, and transmitted to The Highlands was established based on the quantities acquired in the Raw Water Contract,

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[221] WTCPUA Exhibit No. 76 at 6228 (top of right column).

[222] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 6: 23 – 25.

[223] PUC Staff Brief at 13. TCMUD 12 states this as a presumption because Staff supports a finding that WTCPUA is a monopoly and therefore it seems unlikely they would dispute that WTCPUA has disparate bargaining power.

[224] *See,* TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at JAD Exhibit 2 (Raw Water Contract); and TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 10:1-12.

[225] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 4:25-27.

[226] TCMUD 12 Exhibit No. 4(DiQuinzio Rebuttal) at 5.

and as reduced by the amount of water treated by Lakeway MUD for Rough Hollow (TCMUD 11).[227] LCRA *told* TCMUD 12 what it would cost for LCRA's wholesale water services and TCMUD 12 was required to prepay connection fees totaling $1.5 million. [228] There is no evidence to refute Mr. DiQuinzio's testimony that the rates reflected in the Wholesale Water Services Agreement were not negotiated.[229]

In 2008-09, when the Wholesale Water Services Agreement was executed, The Highlands was raw land full of cedar and there wasn't a single house and hence no tax base which would have enabled TCMUD 12 to obtain bond financing. A wholesale water services contract was the only way to obtain the potable water necessary to allow The Highlands to be developed, so the Wholesale Agreement had to be in place before the tax base existed to support it.[230] The required prepayment of Connection fees, including the first installment payment of $350,200 (equivalent to 85 LUEs) before there was a single Highlands retail customer or house to pay the Connection Fees, evidences LCRA's disparate bargaining power in establishing the terms of the TCMUD 12 Wholesale Water Services Agreement. The Districts were either going to pay LCRA $1.5 million or The Highlands would not be developed. TCMUD 12 had no alternative to LCRA and hence had no bargaining power to refuse to pre-pay $1.5 million in Connection Fees. That is a provision of the Wholesale Water Services Agreement that clearly benefited LCRA, not TCMUD 12.

TCMUD 12 contends that the focus of the inquiry under P.U.C. Subst. R. 24.133(a)(3)(A) is whether WTCPUA's disparate bargaining power evidences abuse of monopoly power in setting the 2014 rates, and the relative bargaining power of LCRA in 2008 – 2009 should not be relevant to that inquiry. "The question of importance here is whether Suppliers, using the contract they acquired from the LCRA, sought to exploit their market power by changing the computation of a revenue requirement or a rate from one methodology to another and/or whether Suppliers used disparate bargaining power to impose the protested rate

[227] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 5:22 – 6:1.

[228] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 6:1-21.

[229] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 11: 15-21.

[230] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 6:9-21.

change."[231] Nonetheless, if LCRA's bargaining power is considered, the persuasive evidence demonstrates that LCRA had disparate bargaining power which dictated the terms of the Wholesale Water Services Agreement, and TCMUD 12 could only take-it or leave-it. [232]

WTCPUA argues in two separate parts of its Brief that certain discrete sections of the Wholesale Water Services Agreement are "important" to determining: the issue of monopoly;[233] and/or evidence of TCMUD 12's rights under the Agreement that allegedly do not provide WTCPUA bargaining power in providing wholesale water services to TCMUD 12.[234] Comments in WTCPUA's Brief concerning the Raw Water Contract,[235] to which WTCPUA is not a party, are not addressed.

WTCPUA's Brief lists and then provides its interpretation of the selected sections from the Wholesale Water Services Agreement. TCMUD 12 responds to both sections of WTCPUA's Brief by reference to the sections, and explains why WTCPUA's argument is unpersuasive:

1. Sections 3.01.a.and 3.03.a: require WTCPUA to divert, transport and treat water up to a maximum flow rate of 3.98 MGD and an hourly flow rate of 414,000 GPH, or such lesser amount as WTCPUA may be able to supply in an Emergency.[236] WTCPUA also cites to Section 1.03[237]for the proposition that section requires WTCPUA to provide up to 2,125 LUEs to TCMUD 12. Section 1.03 requires WTCPUA to provide wholesale water services for up to 2,125 LUEs *in accordance with the flow limitations and other provisions of this Agreement.* As is clear from Section 3.03 the maximum daily flow rate of 3.98 MGD is *presumed* to be sufficient for up to 2,125 LUEs[238], and it is the flow rate that establishes WTCPUA's obligation, which WTCPUA is confused about, as discussed above in Section B.1.b.(viii).

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[231] TCMUD 12 Exhibit No. 6 (Zarnikau Rebuttal) at 17: 1-5; see also discussion about competition for the field versus competition within the field at 16.

[232] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 6:9-21.

[233] WTCPUA Brief at 15-17

[234] WTCPUA Brief at 57 - 59

[235] For example, WTCPUA Brief at 58: the Raw Water Contract does not require TCMUD 12 to have LCRA/PUA provide wholesale water service.

[236] Not "as much raw water as TCMUD 12 provides" as argued in WTCPUA's Brief at 15. Section 3.01.a. limits WTCPUA's obligation to provide wholesale water service for the raw water TCMUD 12 purchases from LCRA, *in accordance with the terms* of the Agreement.

[237] WTCPUA Brief at 16 (7th bullet).

[238] *See,* Mr. DiQuinzio's explanation on this point at Tr. 587:22 – 588:10.

2. Section 3.03.b [239]requires LCRA to provide elevated storage and pressure as stated in this section. In exchange, TCMUD 12 was required to prepay $1.5 million in Connection Fees under Section 4.01.a.[240] WTCPUA's suggestion that Section 4.01.a "allows TCMUD 12 to phase-in its payment of connection fees"[241] incorrectly implies the payment schedule is a benefit to TCMUD 12, when actually the Connection Fees were a substantial prepayment obligation imposed on TCMUD 12, but not on any other wholesale water service customer.[242]

3. Section 3.03.c and d:[243] As discussed above,[244] Section 3.03.c provides that *only if* WTCPUA is unable to provide additional water *if* and when TCMUD 12's demand exceeds the max day or hourly flow set in 3.03.a, may TCMUD 12 seek water from another source. Section 3.03.d. limits WTCPUA's obligation to provide additional wholesale water services to that which is available *if* TCMUD 12 ever obtains additional raw water from LCRA. Neither provision has ever been exercised because TCMUD 12's demand has never exceeded the contractual maximums under either the LCRA Raw Water Contract or the Wholesale Water Services Agreement.

4. Sections 4.01, including subsection a., d., e., and f. and 4.03[245] Section 4.01 contains the methodology under which WTCPUA agreed to set the rates.[246] As is discussed later in this Brief, WTCPUA changed the rate and revenue methodology set out in the Wholesale Water Services Agreement in setting the Protested Rates, and incorporated those new methodologies in the standard contract amendment accepted by six wholesale customers. Although TCMUD 12 did not agree to the contract amendment

[239] WTCPUA Brief at 16 (8th bullet).

[240] *See,* WTCPUA Exhibit No. 16 (2008 redlined and highlighted versions of the TCMUD 12 Wholesale Water Services Agreement exchanged by TCMUD 12's and LCRA's respective counsel) at TCMUD12-0354.

[241] WTCPUA Brief at 17 (first bullet).

[242] *See,* TCMUD 12 Exhibit Nos. 8, 11, 14, 16, 19 and 21.

[243] WTCPUA Brief at 15 (citing to 3.03.c only) and 59 (citing to 3.03.c. and d. and in an apparent typographical error to 3.03.*e*) claiming TCMUD 12 is not obligated to purchase all of its wholesale water services from WTCPUA.

[244] *See,* Section B.1.b.(v).

[245] WTCPUA Brief at 16 – 17 and 58.

[246] In TCMUD 12's Wholesale Water Services Agreement Sec. 4.01 a.,b. and c. establish the methodology for the Connection Fee; Sec. 4.01.d describes the methodology for the Monthly Charge; and 4.01.e. establishes the methodology for the Volume Rate. Other wholesale water services contracts that were amended contain very similar provisions although they may have different numbers associated with the sections that describe the methodology for setting the rates, as can be seen in TCMUD 12 Exhibits 7-21.

that expressly set out the new methodology that changed the methodology set out in these sections of its Wholesale Water Service Agreement, WTCPUA nonetheless applied its new methodologies in setting the 2014 protested rates. Section 4.03, entitled "LCRA System to be Self-Sufficient" sets out terms for defining Costs of the LCRA System, LCRA's authority to issue debt, and that the wholesale customers will be charged for debt service, including fees. In addition, as discussed in this Brief at subsection 2(a)(i) immediately above, WTCPUA has the unilateral right to set rates consistent with the terms of the Wholesale Water Services Agreement and the Transfer Agreement. That unilateral authority to change the rates and the absence of regulatory oversight allows WTCPUA to simply declare the rates comply with these provisions, and does not provide any protection or "power" for TCMUD 12. Finally, WTCPUA's interpretation that Section 4.01.a "places limitations on [WTCPUA's] ability to change connection fees"[247] by requiring notice" confuses the meaning of the words "notice" and "limitation." That confusion may explain why WTCPUA failed to understand the Transfer Agreement's "limitation" that stripped WTCPUA of its authority to set the Connection Fee for TCMUD 12.

5. Section 4.03 and Recital #6 and Section 1.01:[248] These sections of the Agreement use the standard terms "fair and equitable, reasonable and necessary" to describe the rates that are to be charged. However, since WTCPUA has the unilateral right to set the rates, it is the sole arbiter of what is fair, equitable, just, reasonable, and necessary. As is abundantly clear from the Commission's rule and this docket, WTCPUA will not have to prove its rates set pursuant to the contract are just, reasonable and necessary until the second phase of this hearing. These provisions do not confer bargaining power on TCMUD 12.

6. Section 6.05 is a default provision that includes an acknowledgement that because TCMUD 12 is obligated to provide continuous and adequate service to its retail customers who lack alternative sources for potable water, LCRA may exercise equitable remedies of mandamus and specific performance if TCMUD 12 defaults. WTCPUA's characterization of this provision as simply restricting LCRA's rights to terminate upon TCMUD 12's default[249] is based upon a failure to read the entire provision, or to understand the legal obligations to provide continuous and adequate service, for the protection of captive retail customers.

[247] WTCPUA Brief at 16 (last bullet).

[248] WTCPUA Brief at 16 (2 bullets) and at 58.

[249] WTCPUA Brief at 17.

7. Section 6.06 (Right to Protest Rates) – this provision simply incorporates TCMUD 12's rights under the Water Code, which LCRA/WTCPUA could not have required TCMUD 12 to contractually waive.

8. Section 7.02 (Records) – the right of each party to the contract to inspect books, records, etc. is a standard provision in all the wholesale water services contracts and does not confer any power on either side.

(b) TCMUD 12's Reservation of Capacity Does Not Evidence It Has Disparate Bargaining Power But Represents a Cost that Must be Considered in Examining Alternative Water Service Providers

TCMUD 12 was the only LCRA wholesale water services customer that was required to prepay connection fees and that is why there is a reservation of capacity in its wholesale water services contract. For example, Hays Co WCID #1 Agreement[250] in the last paragraph of Section 4.01.e. confirms that Connection Fees *shall not be paid in advance* of the time a retail customer for the LUE connection signs a retail service agreement for a retail meter to the District's system. Hays County WCID #1 did not pay until the retail customer was there and had service, whereas TCMUD 12 had to pay connection fees before a shovel of dirt had been turned. When properly understood, the facts do not support a finding that TCMUD 12's reservation of capacity was a result of its superior bargaining power, but rather, the upfront payment of $1.5 million was the result of LCRA's greater bargaining power that allowed LCRA to impose an onerous condition on TCMUD 12 for obtaining wholesale water service. The prepayment of $1.5 million in Connection Fees was the equivalent of 364 LUEs, at a time when there were Zero customers in The Highlands.[251] As WTCPUA points out in its Brief, there were only 132 customers in The Highlands as of January 1, 2014.[252]

TCMUD 12 was appropriately concerned about the uncertainties surrounding its right to the capacity in the West Travis County Water System if it were to switch to an alternative supplier (including the alternative of constructing its own WTP and associated equipment).[253]

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[250] TCMUD12 Exhibit No. 8.

[251] TCMUD 12 Exhibit No. 1, at 14:25-26 and JAD Exhibit 4, p. 10 (Section 4.01.c.) ($1,500,000/$4,120 = 364 LUEs).

[252] WTCPUA Brief at 54, citing WTCPUA Exhibit 44.

[253] Tr. 612. Mr. DiQuinzio testified he did not know if TCMUD 12 could sell its investment to a 3rd party.

WTCPUA attempts to dismiss that concern as ill-founded, claiming that the Wholesale Water Services Agreement allows TCMUD 12 to retain its capacity reservation upon termination.[254]

Under cross-examination, Mr. Rauschuber, with apparent great reluctance, admitted that if TCMUD 12 found a hypothetical alternative water service supplier and terminated the Wholesale Water Services Contract, in order to utilize the capacity to which it is entitled under that Contract, it would have to pay WTCPUA for using that capacity. WTCPUA's General Manager would recommend to the Board, that the rate that should be charged to TCMUD 12 under that scenario should be the same rate all other wholesale customers were charged under their contracts – even though TCMUD 12's contract would have been terminated.[255] So, the reserved capacity could be "used" but only by paying some charge. What Mr. Rauschuber does not explain is the practical problem of how TCMUD 12 could obtain all of its water services from another provider and still use the capacity of the PUA System. Given that common sense problem, and Mr. Rauschuber's expectation that WTCPUA would charge TCMUD 12 under the terms of a Contract that had terminated, it is imminently reasonable for TCMUD 12 to have concluded that leaving the WTCPUA system could result in stranding of its $1.5M investment.

WTCPUA's brief contains two more very unusual arguments. First, it refers to TCMUD 12's $1.5 million payment under the Wholesale Water Service Agreement as "the *alleged* investment amount."[256] This is unusual since the amount is explicitly spelled out in the Wholesale Water Service Agreement, and that sum of money was required to be transferred to WTCPUA under the terms of the Installment Purchase Agreement with LCRA. WTCPUA's use of the word "alleged" leaves one to wonder if WTCPUA knows what its obligations are under its numerous contracts. Second, WTCPUA declares that TCMUD 12 could sell its investment to a "third party", and then argues that under the Wholesale Water Services Agreement, TCMUD 12 may assign its rights to TCMUD 11 or 13 without LCRA's (presumably meaning WTCPUA's) consent,[257] and therefore the $1.5 million investment would not be stranded. Again, WTCPUA appears to not understand the express terms of the Wholesale Water Services Agreement under which TCMUD 12 is acting on behalf of TCMUD 11 and 13 as well as itself, and that the three

[254] WTCPUA Brief at 34-35 and 51 - 52.

[255] Tr. 492-495.

[256] WTCPUA Brief at 52 (3rd line of first full paragraph).

[257] WTCPUA Brief at 52 (last sentence of first full paragraph and second paragraph).

Districts are a *single* water system. Therefore the hypothetical sale of capacity from TCMUD 12 to TCMUD 11 or 13 suggested by WTCPUA ignores the reality of the single water system, and could never be a sale to a "third party."

The evidence supports a conclusion that TCMUD 12's probable loss of its $1.5M investment would be a significant cost that should be considered in determining if there is a viable, reasonable cost alternative water service supplier for The Highlands.

(c) The Terms of the Transfer Agreement Do Not Evidence TCMUD 12 Has Disparate Bargaining Power

TCMUD 12 never had a dispute with LCRA about how it set the wholesale water rates under the terms of the Wholesale Water Services Agreement. However, when LCRA decided to sell the West Travis County Water and Wastewater System and WTCPUA acquired it, TCMUD 12 approached the Transfer Agreement with some trepidation because WTCPUA had paid too high a price for the West Travis County System,[258] and TCMUD 12 wanted to ensure the rates were going to be set in accordance with its contractual rights under the Wholesale Water Services Agreement.[259]

TCMUD 12's concerns guided its approach to the discussions about the Transfer Agreement. The provisions of the Transfer Agreement that provided "protections" for TCMUD 12, included receiving full credit of the paid connection fees, and conditioning the transfer on WTCPUA successfully closing on the sale in 2019.[260] The latter simply ensured that if WTCPUA fails to satisfy the terms of the Installment Purchase, which may yet happen, TCMUD 12 and its retail customers would not be left stranded without potable water but instead could rely on its rights to obtain wholesale water service from LCRA. As for receiving full credit for the connection fees, that was "belts and suspenders" since the Wholesale Water Services Agreement governed TCMUD 12's right to that credit.[261] In other words, these were not "new" protections but rather existing rights related to the connection fees TCMUD 12 had already paid.

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[258] TCMUD 12's concerns about the high price paid by WTCPUA for the West Travis County Water and Wastewater System unfortunately bore fruit, and resulted in an acquisition premium that was one of several changes incorporated into the 2014 Rate methodology. TCMUD 12 Exhibit No. 2 (Joyce Direct) at 24:14-22.

[259] TCMUD 12 Exhibit No. 4 (DiQuinzio Rebuttal) at 12:19 – 28; and TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at 13:6-9.

[260] Tr. 87; cited by WTCPUA Brief at 27 and PUC Staff Brief at 13.

[261] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at JAD Exhibit 5 p. 2-3(Transfer Agreement).

Finally, the Transfer Agreement provides that LCRA may delegate to WTCPUA the authority to collect the Connection Fees and to set and collect the Monthly Charges and Volume Rates (collectively "Water Services Contract Fees.")[262] It was LCRA who stated its desire in the Transfer Agreement to delegate to the WTCPUA the authority to "collect" Connection Fees, in contrast to its authority to "set and collect" the Water Services Contract Fees. TCMUD 12 and WTCPUA agreed to LCRA's expressed desire. While the limitation in the Transfer Agreement on WTCPUA's ability to "set" the Connection Fee could arguably have been a benefit to TCMUD 12, it was not a provision *negotiated* by TCMUD 12; and ultimately, WTCPUA ignored the restriction and changed the Connection Fee charged to TCMUD 12 anyway. Hence, WTCPUA's setting of the Connection Fee in spite of the provision to the contrary in the Transfer Agreement evidences WTCPUA's ability to control the price charged to TCMUD 12.

(d) The Wholesale Customer Committee meetings did not bestow bargaining power on TCMUD 12

The fact that WTCPUA convened wholesale customer meetings does not persuasively demonstrate that they did not exercise disparate bargaining power in setting the 2014 rates. Holding a meeting does not equate with making any concessions or modifications based upon the feedback given by the wholesale customers.

PUC Staff argues that TCMUD 12's attendance at some but not all wholesale customer meetings does not support TCMUD 12's claim that it was not offered the opportunity to participate in the ratemaking process.[263] TCMUD 12's claim is not that it was not offered the opportunity to attend meetings, but rather, that WTCPUA's wholesale customer meetings provided no opportunity for meaningful input to the new rates and rate methodology that WTCPUA formulated for setting the 2014 rates.

Mr. Jay Joyce attended most of the meetings on behalf of TCMUD 12 where anything of substance was discussed, and reported to Mr. DiQuinzio that WTCPUA was unwilling to engage in any meaningful dialogue or exchange of ideas related to the new rates, including the new rate methodology.[264] The WTCPUA did not provide concrete information on the new rates prior to

[262] *Id.* at JAD Exhibit 5 p. 3 (para. 3)

[263] PUC Staff Brief at 14.

[264] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at 16:9–23.

the last meeting in May, and later notified the wholesale customers in mid-October the rates change would be up for consideration at its November 21, 2013 meeting a little over a month later:

> ...[D]uring the spring of 2013, TCMUD 12 participated in some of the wholesale water customer meetings held by WTCPUA and voiced several concerns about the rate methodology being considered. However, no agreement or consensus was reached among the parties regarding the method for WTCPUA's rates for wholesale customers before the WTCPUA halted the meetings in May 2013. Although WTCPUA indicated the wholesale customer meetings would resume in August 2013, no additional meetings were held and no communications between WTCPUA and TCMUD 12 occurred until an email from WTCPUA's attorney was sent to TCMUD 12 on October 15, 2013, which notified us that the WTCPUA Board intended to consider action to change wholesale water rates at its November 21, 2013 meeting.[265]

Another example of the lack of meaningful opportunity for discussion is evident from Mr. Joyce's notes from the second to last wholesale committee meeting on May 6, 2013. Ms. Heddin told the wholesale customers in attendance at the May 6, 2013 meeting that the calculations she was presenting would be reviewed by the WTCPUA Board at their May 23, 2013 meeting with plans to finalize the rates at their June 6, 2013 meeting.[266] A few days later, on May 14, 2013, she emailed the wholesale customers the "draft contract amendment" that reflected the new wholesale rate methodology,[267] and that new methodology went unchanged through its adoption by the WTCPUA Board on November 21, 2013.[268] When the rates were not finalized at the WTCPUA's June 6, 2013 meeting, Mr. DiQuinzio asked Mr. Rauschuber whether the wholesale rate process was complete. Mr. Rauschuber informed Mr. DiQuinzio that "Development of wholesale rates is on-going and as such, not complete. We are in the refinement and contract amendment phases."[269] As we now know, the wholesale rate methodology was completed in May, and was not "on-going" as Mr. Rauschuber claimed. TCMUD 12 did not have a meaningful opportunity for input to the rate setting methodology, or

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[265] TCMUD 12 Exhibit No. 3 (Joyce Direct) at 24:5–14.

[266] WTCPUA Exhibit No. 54, page 108, 2nd para.

[267] WTCPUA Exhibit No. 1 (Rauschuber) at Exhibit P.

[268] WTCPUA Exhibit No. 1 (Rauschuber) at Exhibit Q.

[269] TCMUD Exhibit No. 2 (Joyce Direct), JJJ Exhibit 11, at page 45 of 81.

the rates and WTCPUA's wholesale customer meetings did not bestow bargaining power on TCMUD 12.

(e) WTCPUA's Contract Amendment Offer Evidences WTCPUA's Disparate Bargaining Power

PUC Staff argues that WTCPUA's offer to its wholesale customers to amend their contracts by reducing customers' maximum reserved capacity, indicates that TCMUD 12 "has some level of control over the rates it is charged."[270] To be found persuasive as evidence of TCMUD 12's bargaining power, that argument requires ignoring the following evidence concerning WTCPUA's Contract Amendment offer.[271]

First, while WTCPUA[272] apparently convinced the PUC Staff that the Contract Amendment was intended to simply lower the wholesale customer's bill,[273] the true import of the offered Amendment is evident from the uncontroverted evidence that the vast majority of its provisions deleted the provisions in the Wholesale Water Services Agreement that established the methodology for setting the Monthly Charge[274] and the Volume Rate[275] and replaced them with new provisions that describe WTCPUA's new methodologies for setting the 2014 Rates. WTCPUA's standard Contract Amendment offer incorporated its new methodologies into the wholesale customer's contract for wholesale water service and removed the existing rate methodology provisions in the Wholesale Water Services Agreement that LCRA used to set the wholesale rates from the inception of the Agreement, and which was also the methodology used by WTCPUA in its decision setting rates for 2013 (the Previous Rate).

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[270] PUC Staff Brief at 13 – 14.

[271] TCMUD 12 Exhibit No. 23 at HC 0775 – 0778, and 0782; and WTCPUA Exhibit No. 1 (Rauschuber Direct) at 209 – 214, Attachment Q (WTCPUA Nov. 21, 2013 Resolution Authorizing Negotiation and Execution of Form Amendments).

[272] WTCPUA Exhibit No. 1 (Rauschuber) at 25: 6-14 ("WTCPUA Board of Directors provided the wholesale customers with the opportunity to amend their wholesale contracts with the WTCPUA to revise their quantity of wholesale water treatment capacity and living unit equivalent uptake schedule. * * * In other words, WTCPUA gave its wholesale customers an opportunity to reduce or increase their contractual obligation with WTCPUA, which would consequently impact their rates as well.")

[273] PUC Staff Brief at 13-14

[274] TCMUD 12 Exhibit No. 1 (DiQuinzio) at JAD Exhibit 4, Wholesale Water Services Agreement, Section 4.01.d; and WTCPUA Exhibit No. 1 (Rauschuber Direct) at 212–213, Attachment Q, draft Contract Amendment para. 3 (including (x), (Schedule B), and (xx)).

[275] TCMUD 12 Exhibit No. 1 (DiQuinzio) at JAD Exhibit 4, Wholesale Water Services Agreement, Section 4.01.e; and WTCPUA Exhibit No. 1 (Rauschuber Direct) at 212–213, Attachment Q, draft Contract Amendment para. 3 (including (xxx)).

Second, the standard Contract Amendment offered by WTCPUA to TCMUD 12, would have lowered TCMUD 12's Monthly Charge only if TCMUD 12 reduced its "Maximum Day Reservation." Max Day Reservation is a new term proposed by WTCPUA (and set out in the standard contract amendment) but was intended to change what is referred to in Section 3.03.a. of the Wholesale Water Services Agreement as the maximum daily flow rate of 3,980,000. That "offer" was problematic for TCMUD 12 for several reasons. First, TCMUD 12 is a very young district, and to voluntarily give up water rights during the worst drought in the history of Texas, would have been foolish. Second, since The Highlands is growing and expects to need the full capacity commitment under the Wholesale Water Services Agreement in 7 – 10 years, or by 2022 – 2025[276] which would equivalent to about 1,640 single-family retail water connections, or roughly 2,125 LUEs[277] (which is the number of LUEs that were assumed could be served with the maximum daily flow rate of 3,980,000 gallons per day (GPD) capacity under the Wholesale Water Services Agreement) so giving up the ability to serve all customers at build out would have been extremely short-sighted. Finally, if TCMUD 12 had lowered its Max Day as suggested by WTCPUA, there was no guarantee that WTCPUA would allow The Highlands' "Max Reservation" to increase when the need arose.[278] This is confirmed by the contract amendments executed by Hays County MUDs # 1 and 2, for example, which states that the peak daily flow rate and quantity of water delivered may be increased only if capacity is "available in the PUA system."[279]

So, even though neither the Wholesale Water Services Agreement nor the Transfer Agreement required WTCPUA to "give TCMUD 12 an opportunity to reduce" its 3.98 MGD capacity reservation,[280] that wasn't viewed as a positive "opportunity" for TCMUD 12. On the other hand, WTCPUA's contract amendment "offer" would have resulted in a significant benefit to WTCPUA. Since the Transfer Agreement required WTCPUA to "bill and collect payment from the District in strict accordance with the terms and conditions of the Water Services

[276] WTCPUA Exhibit No. 53.

[277] WTCPUA Exhibit No. 51 (1,640 retail water service connections) and WTCPUA Exhibit No. 52 (close to 2,125 LUEs).

[278] Tr. 90-91, and 587-589.

[279] *See,* TCMUD 12 Exhibit No. 7 at WTCPUA 00003864 (paragraph 5) and Exhibit No. 10.

[280] Tr. at 75.

Contract"[281] WTCPUA's offered Amendment would have contractually changed those rate-setting terms and conditions *before* WTCPUA closed on the purchase of the System. As it turned out, TCMUD 12's ability to decline WTCPUA's offer to amend its wholesale water services contract did not stop WTCPUA from imposing on TCMUD 12 the new methodology spelled out in the standard contract amendment for the Monthly Charge and Volume Rate. So, while the "choice" to say "no"[282] allowed TCMUD 12 to maintain its contractual maximum daily flow rate of 3,980,000 gallons per day, the significance of TCMUD 12's declining the offer to amend the "Max Reservation" was greatly overshadowed by WTCPUA unilaterally changing the methodology for determining the Wholesale Water Monthly Charge and Volume Rate when it set the 2014 Rates.

Third, from an economist's perspective, the Suppliers' offering an option to reduce the quantity sold to a buyer has nothing to do with WTCPUA's market position. For example, if the sole supplier of weekly garbage pickup and processing services in a neighborhood was going to double the price of weekly service but offered to discount its price by 25% for every-other-week pickup, the consumer would get a lower service option and the garbage provider would still be exercising monopoly power. Since TCMUD 12 needs the capacity it contracted for, the offer by WTCPUA to reduce the quantity of water does not represent an opportunity of value to TCMUD 12 and does not indicate a change to WTCPUA's market power.[283]

Respondents argue that the offer to the wholesale customers to amend their contracts was an "opportunity to renegotiate." The evidence however supports finding it was a take it or leave proposition.[284] The fact that six wholesale customers signed on, does not prove that they thought it was an "okay-enough deal" as Mr. Haley suggested, or if they "just felt like they didn't have any choice."[285] Only Dr. Zarnikau examined the offer and presented an opinion concerning the offer, and that was the contract amendment offer does not support a finding that TCMUD 12 was given bargaining power or that WTCPUA was not abusing its monopoly power.

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[281] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at JAD Exhibit 5, p. 3 of 8 (para. 3 – last sentence).

[282] Tr. at 36.

[283] TCMUD 12 Exhibit No. 6 (Zarnikau Rebuttal) at 21: 16- 22:8.

[284] TCMUD 12 Exhibit No. 23 at HC 0782.

[285] Tr. 268.

If parties enter into negotiations freely and have similar bargaining strength and the result is a signed contract and all parties are happy, there would be no abuse of bargaining power. But if a customer really has no alternatives but needs the service and nonetheless signs the Contract, the acceptance of the contract does not mean the customer has bargaining power.[286] The fact that the wholesale customers had no power to negotiate the terms of the Contract Amendment, even when WTCPUA's legal counsel agreed that a provision did not apply to wholesale customers, is evidence of WTCPUA's exercise of its disparate bargaining power.[287]

3. Conclusion: If there was disparate bargaining power, does the protested rate evidence WTCPUA'S abuse of monopoly power?

WTCPUA's conclusion is that even if it has disparate bargaining power, the protested rates do not evidence abuse of monopoly power because the Protested Rates resulted in lower rates for 2014.[288] As explained above,[289] this theory is unsupported by citation to statute, rule or precedent, and neither PUC SUBST. R. 24.133 nor the Preamble to the predecessor rule contain any language that supports the argument that a decreased or lower rate prevents a finding that the seller abused its monopoly power. The Protested Rates resulted from a change to the methodology for calculating revenue requirement and rates and the offered form Amendment to the Wholesale Water Services Agreement explicitly modified the methodology by deleted provisions of the original Agreement and replacing or adding provisions that set out the new methodology. TCMUD 12 did not accept the contract amendment, did not agree with Ms. Heddin's new methodology and yet the new methodology was imposed upon TCMUD 12 through the 2014 Protested Rates. In light of that undisputed evidence, WTCPUA's argument that the protested rates were negotiated[290] fails. Under the wholesale water services agreement, WTCPUA had the unilateral right to change the Monthly Charge and Volume Rate "at any time", contrary to WTCPUA's argument.[291] TCMUD 12's ability to say "No" to the contract amendment did not detract from WTCPUA's disparate bargaining power as evidenced by the

[286] Tr. 269-270.

[287] See, TCMUD 12 Initial Brief at 41-42. TCMUD 12 Exhibit No. 23 at HC 0782.

[288] WTCPUA Brief at 59 -60.

[289] *See,* Section IV of TCMUD 12's Reply Brief.

[290] WTCPUA Brief at 61.

[291] WTCPUA Brief at 61.

fact that the new methodology reflected in the form contract amendment was nonetheless imposed on TCMUD 12. WTCPUA's offer to provide a lower quantity of service to reduce the monthly charge similarly was not an offer that would have benefited TCMUD 12 and did not change WTCPUA's status as a monopoly. Finally, the fact that WTCPUA convened wholesale customer meetings does not persuasively demonstrate that they did not exercise disparate bargaining power in setting the 2014 rates. Holding a meeting does not equate with making any concessions or modifications based upon the feedback given by the wholesale customers and the persuasive evidence in this record demonstrates that WTCPUA decided on the new rate methodology early in the process and that methodology did not change – regardless of the number of meetings it held.

PUC Staff's conclusion that even if TCMUD 12 had few options for obtaining wholesale water service other than from WTCPUA, TCMUD 12 has not proved that WTCPUA acted in any manner to limit those options, citing to page 70 of the *Corsicana* PFD. Staff's reliance on the conclusion in *Corsicana* is mis-placed because the facts are readily distinguishable. The reference to the fact that the Seller in that case (Corsicana) did not attempt to exercise power to limit the Purchasers' (NCWR's) options referred to a claim by the NCWR that Corsicana had interfered with some Ratepayers attempt to buy water from TRWD. The ALJ rejected that argument, finding instead that TRWD chose not to supply water to the Ratepayers for reasons of its own.[292]

TCMUD 12 is not claiming WTCPUA exercised its monopoly power by interfering with alternative options for obtaining wholesale water services. TCMUD 12's claim is, and the evidence presented supports a finding that, there were no viable alternative providers, and the cost of any hypothetical alternatives would be prohibitive, including the fact that TCMUD 12 would still have to pay WTCPUA a Monthly Charge even if an alternative provider materialized and if TCMUD 12 wanted to use its reserved capacity in PUA's Water System, it would also have to pay some undetermined rate for that use.[293]

WTCPUA's monopoly power is evident from its control the prices charged and the supply of water services sold to TCMUD 12, and is reflected in the disparately greater

[292] *Corsicana* pfd at 28.

[293] These facts are comparable to the facts explained in the *Corsicana* PFD at p. 27.

bargaining power that flows from the long-term Wholesale Water Services contract and TCMUD 12's lack of viable alternative means of obtaining wholesale water services sufficient to provide potable water to the retail customers of The Highlands. TCMUD 12 had little *effective* involvement in WTCPUA's establishment of the Protested Rates, which included the onerous change to methodology for calculating the revenue requirement and rates that are protested here. WTCPUA's exercise of its disparate bargaining power was an abuse of monopoly power.

C. Methodology for Computation of Revenue Requirement and Rate (P.U.C. SUBST. R. 24.133(a)(3)(C)).

The WTCPUA argues that a change from the Cash Needs Basis to the Utility Basis, or vice versa is required for there to be a change in methodology.[294] Staff's position is that the methodology used to compute the revenue requirement and rates at issue in this proceeding did not change, as the WTCPUA used the cash basis method in both this proceeding and the prior rate change.[295] Hays County's argument is based on the same analysis[296] as is Bee Cave's argument.[297]

None of these parties, however, address the fact that this argument – that a change from the cash basis to the utility basis is the only change that may be considered a change in methodology – has been considered and rejected more than once.[298] In the *Corsicana* case, the Seller, City of Corsicana, made the same argument that the Respondents and Staff have made here – that evidence of a change between the Cash Basis and the Utility Basis for determining revenue requirement would be necessary to find that Corsicana changed its revenue requirement or rate methodology.[299] Even the legal underpinnings of the arguments in this case and the *Corsicana* case are the same. WTCPUA witness Jack Stowe claims that P.U.C. SUBST. R. 24.135(b) limits the change of methodology discussion to changes between the cash basis and the utility basis.[300] Corsicana based its argument on the same rule.[301] In

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[294] WTCPUA Brief at 66–67.

[295] Staff Brief at at 15–16 and 18.

[296] Hays County Brief at 13–14.

[297] Bee Cave Brief at 7–8.

[298] See, TCMUD 12 Initial Brief at 44–46.

[299] *Corsicana* PFD at 51 and TCMUD Exhibit No. 5, 15:5 – 16:11.

[300] WTCPUA Exhibit No. 3, at 23: 21 - 24: 7.

addition to the rule, Corsicana also cited to the McAllen and Multi-County cases to support its position. The ALJ rejected all of Corsicana's arguments, including the claim that P.U.C. SUBST. R. 24.135(b) limits the change of methodology discussion to changes between the cash basis and the utility basis. He concluded that the Public Interest rule does not limit changes between the Cash Basis and the Utility Basis as the only methodological changes that would show abuse of monopoly power:

> However, nowhere in those cases [*McAllen* and *Multi-County*] did the Commission conclude that switches between the Cash and Utility Bases were the only methodological changes that might indicate monopoly abuse. Nor did the Commission cite 30 TAC§ 291.135 as the source of, much less a limitation on, the meaning of the word "methodology" as used in 30 TAC § 291.133(a)(3)(C). Additionally, nothing in the preamble to the adoption of the wholesale-service rules indicates that the Commission intended to narrowly construe 30 TAC § 291.133(a)(3)(C) as advocated by the ED and Corsicana.[302]

Even if the Respondents and Staff were not aware that this argument had been squarely addressed in the *Corsicana* PFD (which is unlikely given that all but Bee Cave cited to the *Corsicana* PFD in its brief), they should have been aware of the ALJ's prior rulings in *this* case which also rejected that argument. The ALJ in this case addressed this issue when ruling on WTCPUA's Motion for Summary Disposition:

> Reading § 24.133(a)(3)(C) in context, the Administrative Law Judge (ALJ) agrees with District 12 that changes in computation methodologies that could adversely affect the public interest are not legally limited to changes between the cash and utility bases for calculating cost of service, and consequently revenue requirement and rates.[303]

Accordingly, changes between the Cash and Utility Bases are *not* the only methodological changes that might indicate monopoly abuse.

The next argument WTCPUA makes in this section of its Brief is that "the terms 'revenue requirement' and 'cost of service' are not synonymous; they have separate and distinct meanings."[304] Noticeably, WTCPUA does not cite to any statues, regulations, or previous cases

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[301] *Corsicana* PFD at 55, citations omitted.

[302] *Id.*

[303] SOAH Order No. 13 (Mar. 24, 2015) at 2.

[304] WTCPUA Brief at 66.

to support this assertion. The lack of any citations is understandable. In the context of the PUC Water Rules generally, and the Public Interest rule specifically, there are no clear distinctions between the definitions of *revenue requirements* and *cost of service*. This was acknowledged by ALJ in the *Corsicana* PFD which stated that the terms "cost of service" and "revenue requirement" are synonymous.[305] The terms have also been used interchangeably in other cases such as in the *San Saba*[306] and the *Chisholm Trail*[307] cases.[308]

1. Did WTCPUA change the methodology for the computation of the revenue requirement?

WTCPUA does not address the evidence presented on this issue directly, but instead tries to skirt the issue by claiming that Jay Joyce's testimony and exhibits were an impermissible cost of service analysis. WTCPUA's claim is that Mr. Joyce addresses cost allocation issues and not WTCPUA's revenue requirement or rate methodologies.[309] The foundation of WTCPUA's argument is that "the cost of service analysis is distinct from the computation of the revenue requirement." However, because "revenue requirement" and "cost of service" are used interchangeably, as discussed immediately above, WTCPUA's attempt to summarily dismiss Mr. Joyce's testimony should be rejected.

As acknowledged in the *Corsicana* PFD, many different methodologies for determining revenue requirement are discussed at length in the Preamble, "including the Cash Basis, Utility Basis, and methodologies that the parties have agreed on in their contract." The Wholesale Water Services Agreement, which establishes WTCPUA's rate-setting authority and the methodology for calculating TCMUD 12's rates, provides in part that costs attributable to the provision of *retail* water service shall *not* be included in TCMUD 12's rates.[310] And yet, WTCPUA changed the methodology of allocating repair and maintenance costs from "retail-

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[305] *Corsicana* PFD at 51.

[306] *In Re: Application of North San Saba Water Supply Corporation to Change its Water Rates Under Certificate of Convenience and Necessity No. 11227 in San Saba County*, TCEQ Docket No. 2008-1481-UCR; SOAH Docket No. 582-09-0660, Proposal for Decision at 4-5 (March 25, 2010).

[307] *Petition Requesting Review of Chisholm Trail Special Utility District's Special District's Rate Increase Pursuant to Texas Water Code Section 13.043*; SOAH Docket No. 582-05-0003, TCEQ Docket No. 2004-0979-UCR, Proposal for Decision, Proposed Finding of Fact 19 (February 8, 2006).

[308] TCMUD 12 Exhibit No. 5 (Joyce Rebuttal) at 31:5 – 32:8.

[309] WTCPUA Brief at 67–69.

[310] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct) at JAD Exhibit 4, Wholesale Water Services Agreement at 3–4, Art. I Definitions: Costs of the LCRA System.

only" in FY 2013 to an allocation method referred to as "Common-to-All" where costs area allocated to all water customers, retail *and* wholesale alike, in FY 2014.[311] WTCPUA therefore changed the revenue requirement methodology so that TCMUD 12 and other wholesale customers are now bearing those costs, that previously had been borne only by the retail customers.[312]

Bee Cave characterizes this change as a change in a value of a category already in place rather than a change of methodology.[313] Either Bee Cave is not aware of the provisions of the Wholesale Water Service Agreement, or this is disingenuous obfuscation. WTCPUA changed the methodology it used to compute the value for the Protested Rates from the methodology as stated in the Agreement and as used in computing the Prior Rates.[314] In other words, WTCPUA changed the computation by which this part of its revenue requirement was calculated from one methodology to another. The fact that the Respondents chose to not introduce any evidence on this issue, but instead relied on their argument that the only change to methodology that should be considered is Cash versus Utility basis, does not transform TCMUD 12's evidence on change of methodology into an impermissible cost of service analysis.

Bee Cave also argues that PUC witness Graham illustrated the distinction between a methodology and its components in an example involving depreciation. Ms. Graham testified that the methodology of calculating straight-line depreciation is a set process, and if the service life changed that would be changing a component of the methodology but not necessarily a change in the methodology.[315] Bee Cave's argument, however, does not address that Ms. Graham also acknowledged that a change from straight-line depreciation to accelerated depreciation would more likely be considered a change of methodology.[316] In his testimony, TCMUD 12 witness Joyce describes the changes to the allocation methods e.g., from retail to common to all, as changes to the revenue requirements methodology. These changes to the

[311] TCMUD 12 Exhibit No. 2 (Joyce Direct) at 1:19–13:18, and JJJ Exhibit 6.

[312] Id.

[313] Bee Cave Brief at 8.

[314] TCMUD 12 Exhibit No. 2 (Joyce Direct) at 1:19–13:18, and JJJ Exhibit 6.

[315] Bee Cave Brief at 8, citing Tr. 405 – 406.

[316] Tr. 406.

revenue requirement calculation methodology are equivalent to changing from straight-line to accelerated depreciation.

Staff argues that examining the components to which WTCPUA allocated costs is permissible in determining whether the overarching methodology has changed but reviewing changes in the actual amounts allocated delves into an examination of the cost of service.[317] This argument is premised on Staff's position that the components to the methodology (i.e. operation and maintenance expense, debt service requirements, and capital expenditures which are not debt financed for the cash methodology) are the only components that may be examined[318] and that changes within those components such as changing allocation factor are cost of service arguments.[319]

Staff's argument on this point again rests on a mischaracterization of Mr. Joyce's testimony. Staff cites to a portion of Mr. Joyce's testimony at hearing which Staff asserts Mr. Joyce testified that "changes in allocation of funds between components remaining the same from year to year can evidence a change in methodology in computing rates."[320] What Mr. Joyce testified to, however, was that it is possible to have a change in methodology even if the components don't change if there is a change to ***how*** the costs are allocated.[321] The fact that the allocation values change does not mean that the method for calculating the component has changed. As Mr. Joyce explained, a change in the dollar value "doesn't necessarily mean there was a change in methodology."[322] The rule requires an examination of whether "the seller changed the computation … from one methodology to another."[323] Even though the Account Number (e.g., 16100 for LCRA Raw Water Reservation Fee; 16101 for LCRA Raw Water Used, etc.) appears in both the Previous Year and Current Year revenue requirement methodology, the methodology for determining the value for that Account could have changed.[324] It is the change

[317] Staff Brief at 17.

[318] Staff Brief at fn. 75.

[319] Staff Brief at 16, "However, it is clear that TCMUD12 witness Mr. Joyce's reliance on the difference in allocation between components that stayed the same in both 2013 and 2014 is flawed and an impermissible reliance on cost of service evidence.

[320] Staff Brief at fn 81 and related text.

[321] Tr. 214: 13–19.

[322] Tr. 143:24 – 144:11.

[323] PUC SUBST. R. 24.133(A)(3)(f).

[324] Tr. 144:20 – 145:2, referring to TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-4..

in the computation methodology which evidences abuse. And in this case, the methodology by which the revenue requirement and the rates were computed changed.

For example, Mr. Joyce addresses a raw water loss surcharge in his testimony. In 2013, the "base cost of service" was tied to the historical average day usage.[325] In 2014, the "base cost of service" was computed by taking the average day and applying an 8% water loss factor resulting in an "*adjusted* average day."[326] Regardless of whether the 8% water loss factor is correct or not, this is a change to the methodology used to calculate the revenue requirement from 2013 to 2014.

WTCPUA argues that rejecting Mr. Joyce's interpretation would be consistent with the precedent established in *City of McAllen,* which held that the creation of new accounts designed for operational and cash reserves did *not* mean that the District had changed its revenue requirement or rate setting methodology.[327] In the *McAllen* PFD relied on by WTCPUA, however, the ALJ explained the two new reserve accounts merely formalized a reserve fund that had accumulated for many years and that formalizing that practice did not evidence a change of methodology for calculating rates or revenue requirement.[328] In addition, the two new funds were created months *after* the rate increase was implemented, and therefore the rate change could not have been affected by changes that occurred four months later.[329] In this case, the raw water loss surcharge did not formalize a historical practice or method but rather had an immediate impact on not the revenue requirement calculation and the rate paid by the wholesale customers.

In its Brief, WTCMUD 5 takes the position that "the protested PUA rates were the first PUA wholesale rates based upon an actual revenue requirement for the PUA" and therefore, the PUA changed its revenue requirement when it adopted the protested rates in November 2013.[330] According to WTCMUD 5, the previous WTCPUA rates were not based on *any* revenue requirement, but instead in March 2012, the PUA Board simply adopted the old LCRA rates[331],

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[325] TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-13, page 47, columns 4–6.

[326] TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-14, page 48, columns 4–8.

[327] WTCPUA Brief at 71.

[328] McAllen PFD at 18-19.

[329] Id.

[330] WTCMUD 5, Brief at 9–10.

[331] *Id.,* citing WTCPUA Exhibit 1 (Rauschuber Direct), at 15.

and therefore the WTCPUA methodology became a continuation of the LCRA methodology. But WTCMUD 5 overlooks the fact that the WTCPUA Board also directed Ms. Heddin to conduct a Wholesale Cost of Service and Rate Design Study to set rates for 2013. That Cost of Service Study resulted in her recommendation that in order for the Agency to recover its *projected revenue*, rates for wholesale customers, including the monthly charges and volume rates, needed to increase by 31%.[332] Ultimately, the Board cut that percentage in half, and increased wholesale monthly charges and volume rates by 15.5%. So the 2013 "Previous Rate" was established by a Cost of Service Study.

Characterizing the 2014 rate methodology as the "first" WTCPUA revenue requirement methodology is simply inaccurate. A utility has a "first" revenue requirement and rate methodology only when the utility sets its first rate. It doesn't happen often that there is an entirely new utility that hasn't ever provided service to, or had a revenue requirement it needed to recover through rates charged to its customers, but there is an example with which the PUC is certainly familiar. In Texas as part of the CREZ cases, Cross Texas Transmission (CTT) was *created* as an "electric utility." CTT was granted a new CCN, allowing it to construct a part of the CREZ transmission lines. After it constructed (some of) those transmission lines, CTT returned to the PUC for its first rate case – and that required it to develop its "first" revenue requirement and rate methodology. However, unlike CTT, in 2013 when WTCPUA was setting the 2014 Protested Rates, it was not determining its cost of service for the first time but rather it was changing the LCRA methodology it had expressly adopted in 2012, then changed again for 2013, pursuant to Ms. Heddin's Cost of Service and Rate Design study. Then in 2013 when calculating the revenue requirement and rates for 2014, in Ms. Heddin's own words, her "proposed" methodology changed the methodology under which she had determined WTCPUA's revenue requirement and the wholesale rates for 2013, to calculate WTCPUA's wholesale revenue requirement and rates for 2014. Even if WTCMUD 5's argument is accepted at face value, and WTCPUA's 2014 revenue requirement and rates are new, the methodology used to compute them is nonetheless different from the methodology used previously, so there is a change to the methodology by which the revenue requirement and rates were computed.

[332] WTCPUA Exhibit No. 1 (Rauschuber) Attachment N at page 25.

2. Did WTCPUA change the methodology for the computation of the rate?

WTCPUA claims it did not change the methodology for the computation of the rate because the Prior Rate employs a minimum monthly fee and a flat volume rate methodology and the Protested Rate employs a minimum monthly fee and a flat volume rate methodology.[333]

Similarly, Staff also maintains that WTCPUA did not change the methodology for the computation of the rate subject to this appeal on the grounds that both this rate and the previous rate were calculated using the cash basis method, and that the rate design for both the protested rate and the previous rate included a minimum base rate and a volumetric rate.

And finally, Hays County argues that because the protested rate is charged as a combination of a Monthly Charge and a volumetric rate, the methodology by which the rate is computed did not change.[334]

WTCPUA, Staff and Hays County place undeserved importance on the fact that the Protested Rates include a Monthly Charge and a Volume Rate. The fact that the WTCPUA charges TCMUD 12 a Monthly Charge and a Volume Rate does not evidence that the WTCPUA did not change the methodology by which the Monthly Charge and Volume Rate are computed. The Wholesale Water Services Agreement, Article IV, sets out the rates WTCPUA may charge TCMUD 12 under the Agreement: a "Connection Fee," a "Monthly Charge," and a "Volume Rate."[335] This argument is a classic non-sequitur. The conclusion that "the computation of the Monthly Charge and the Volume Rate did not change in 2014" does not follow logically from the statement that precedes it, to wit: "A Monthly Charge and a Volume Rate were charged to TCMUD 12 by the WTCPUA in 2013." To base a conclusion that the methods by which the Monthly Charge and a Volume Rate were computed did not change on the fact that a Monthly Charge and a Volume Rate were charged in the previous year requires a herculean leap of (invalid) logic. This position drew criticism from even one of the WTCPUA's own participants, who characterized it as a "simpleton statement."[336] The fact that a Monthly Charge and a Volume Rate were charged to TCMUD 12 by the WTCPUA in both 2013 and 2014 shows that

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[333] WTCPUA Brief at71.

[334] Hays County Brief at 14.

[335] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct), JAD Exhibit 4, Article IV.

[336] WTCMUD 5 Brief at 10.

WTCPUA is continuing to charge TCMUD 12 the rates the contract requires them to charge – it does nothing to establish that the computation of those rates has not changed.

In their Briefs, the WTCPUA and Staff adhere to their position that the only changes in methodology that may be considered in a public interest proceeding are changes between the cash basis and the utility basis. The WTCPUA and Staff further claim that any examination beyond a change from the cash basis to the utility basis and vice versa is an impermissible cost of service analysis. Relying on that position, WTCPUA witness Stowe and Staff witness Graham both chose to not address specific evidence put forward by TCMUD 12 witness Joyce, and his testimony therefore stands un-rebutted.

For example, Mr. Joyce pointed out that in 2013 all wholesale water services customers were charged the same uniform Volume Rate per thousand gallons, but in 2014 the same wholesale water services customers are charged widely differing volumetric rates per thousand gallons.[337] Principles of mathematics dictate that this result is possible only if a change to the calculation of the Volume Rate has occurred. WTCPUA attempts to side step this issue by using misdirection: citing to Staff witness Graham's position that such analysis delves too deep into the cost of service.[338] According to Ms. Graham, there would be no way to perform such an analysis of the amounts allocated to each customer to be collected through the variable rates without conducting a review of WTCPUA's cost of service study.[339]

Contrary to Ms. Graham's testimony, and the position taken by the WTCPUA and Staff in their briefs, delving deeply into the cost of service study is not required to determine that the method used to compute the Volume Rate has changed. The changes to the Volume Rate's computation are apparent in the exhibits cited by Ms. Graham. Exhibit JJJ-14is the final analysis used to set the FY 14 volumetric rate for TCMUD 12.[340] At page 53 of 76 of Exhibit JJJ-14 the computation methodology for the Raw Water Surcharge for customers paying WTCPUA for raw water is spelled out:

Raw Water Surcharge Fee = [LCRA raw water cost per thousand gallons/(1-.10 water loss)]/10.

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[337] TCMUD 12 Exhibit No. 2 (Joyce Direct) at 20:22–30.

[338] WTCPUA Brief at 72.

[339] Id., citing to PUC Staff Ex. No. 1 (Graham Direct) at 11–12.

[340] TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-14, page 1 of 76.

At page 52, the column "Plus Raw Water Charge" appears and indicates that the Volumetric Rate computation includes – for the first time ever – a raw water charge. That computation methodology has no counterpart in previous rate studies.[341] The same change to the Volumetric Rate computation methodology is also reflected in Attachment Q to Mr. Rauschuber's direct testimony, which is the Standard Contract Amendment offered to the Wholesale customers.[342] Section 3 of the form amendment reads "3. Section _____ is hereby amended to add new subsections (x) (xx) and (xxx) as follows: * * * (xxx) The Volume Charge shall recover the PUA's expenses associated with operating and maintaining the Regional Facilities, including a systems raw water loss fee per thousand gallons to be calculated as follows: [LCRA Raw Water cost per Thousand Gallons/(1-.l0 water loss)]/10."[343]

Adding the Raw Water Charge to the Volumetric Rate is a *significant* change in methodology because TCMUD 12's Wholesale Water Service Agreement states that the volumetric rate will *not* include any charges for raw water,[344] but the Protested Volumetric Rate charged to TCMUD 12 uses this new methodology to include a raw water loss charge.[345] The method used to calculate TCMUD 12's Volume Rate changed. This conclusion is inescapable and may be arrived at without an analysis of the WTCPUA cost of service study or "analysis of the amounts allocated to each customer."

Staff's Brief also takes the qualified position[346] that the method used to compute the minimum base rate [i.e. the monthly charge] did not change since it was computed in both 2013 and 2014 by using the fixed revenue WTCPUA needed to recover along with a forecasted number of connections."[347] The source of Staff's apparent equivocation originates in Ms. Graham's testimony, where she states "the minimum charge *appears* to be computed for each wholesale customer for FY 2014 as it was for FY 2013 by using the amount of fixed revenue that WTCPUA was trying to recover and a forecasted number of connections."[348] The WTCPUA

[341] TCMUD 12 Exhibit No. 2 (Joyce Direct) at 8:22, 10:19–29.

[342] WTCPUA Exhibit No. 1 (Rauschuber Direct), Attachment Q (Resolution and Form Amendment)

[343] Id. at Section 3.

[344] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct), JAD Exhibit 4 at 12 of 27, Section 4.01(e).

[345] TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-14, pages 52 and 53 of 76.

[346] Staff Brief at 17. Staff statement on this point is not unequivocal as it states "it appears the method…"

[347] Staff Brief at 17 (clarification added).

[348] Staff Exhibit No. 1 (Graham Direct) at 11 (emphasis added) and fn 13, citing JJJ-12 and JJJ-14.

makes a similar argument relying solely on the same equivocal testimony from Staff witness Graham.[349]

As it turns out, Staff was correct to equivocate in its statement that the monthly charge was computed in the same way for FY 2014 and FY 2013. Evidence in the record establishes that the monthly charge for 2014 was, in fact, computed using a different methodology than the Monthly Charge for 2013.

The Previous Monthly Charge (charged in 2013) was calculated using a 3-step process, that incorporated:[350]

1. Calculate Total Wholesale Costs using a Base/Extra Capacity Method to allocate all cost components to the wholesale customers;
2. Calculate Total Wholesale Revenues at Current Rates
3. Calculate Required Rate Increase (step 1 minus step 2 = step 3) and apply the percentage difference to the prior rates.

The Protested Monthly Charge was developed using a 7-step formula or methodology[351] and may be stated as follows:

> {Annual Allocated Debt Service Payment + (25% times coverage * Annual Allocated Debt Service Payment) – (Effective Impact Fee Credit * Annual Debt Service Payments)} / 12 months.

This Monthly Charge Methodology is reflected both in WTCPUA's FY 14 Minimum Bill Analysis for TCMUD 12[352] and in the Offered Contract Amendments[353], as well as in the Contract Amendments accepted by six wholesale customers.[354] One significant change to the methods used to calculate the Monthly Charge in 2013 versus 2014, is that the formula used in 2014 does not give the wholesale customers credit for the "times coverage" paid.[355]

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[349] WTCPUA Brief at 71–72.

[350] TCMUD 12 Exhibit No. 2 (Joyce Direct at 18 – 19).

[351] TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-11, p. 37 of 81.

[352] TCMUD 12 Exhibit No. 2 (Joyce Direct) at Exhibit JJJ-15 page 14 of 16 (Total Annual Minimum Bill =Total Annual Payment + (total Annual Payment * 25% Times Coverage) – (Total Annual Payment * Impact Fee Credit). In order to arrive at the *Monthly* payment, the Annual Payment is divided by 12.

[353] WTCPUA Exhibit No. 1 at Attachment Q.

[354] TCMUD 12 Exhibits 7, 10, 13, 16, 18, 20.

[355] TCMUD Exhibit No. 2 (Joyce Direct), at page 16, Tables JJJ-T3 and JJJ-T4; and Exhibit JJJ-13 (FYE 2013 Budget Planning at Schedule 5A Debt Service Analysis) at page 10 of 56.

In order to fully appreciate the breadth of the change wrought by the new methodology, it is necessary to read the remainder of the lengthy "formula" as set out in the Form Contract Amendment.[356] Importantly, the Wholesale Water Service Amendment inserts a new subpart into section 4.01(b) of the Wholesale Water Services Agreement, incorporating and substantively changing the methodology by which the Monthly Charge is calculated. [357] The Monthly Charge formula used in the contract amendments is the methodology used to set TCMUD 12's Monthly Charge for 2014, even though TCMUD 12 even though TCMUD 12 did not agree to the contract amendment, as is detailed in full in TCMUD 12's Initial Brief at pages 47–60.

Hays County states in its Brief that interpreting a change in allocation factors to mean that a complete change in methodology has occurred would likely trigger public interest factors under 16 TAC 24.133 for most water providers in any given year, particularly in areas of high growth like Central Texas.[358] The City of Bee Cave echoes Hays County on this point, and states in its brief, and in response to the question "Did WTCPUA change the methodology for the computation of the rate?" states: "The analysis of this question is similar to the question about changed methodology for computation of the revenue requirements. There are differences from year to year. The values of components may change, but the methodology does not." Those three sentences are the totality of Bee Cave's brief on this point.

Hays County and Bee Cave both completely fail to address the changes to the methodology reflected in the evidence. TCMUD 12's volume rate and Monthly Charge are being calculated using the new, changed or amended formulas used for the wholesale customers that agreed to those contract amendments.[359] These changes are beyond the simply "customer class allocations" that Mr. Stowe testifies about[360] or the types of things that would occur every year as Ms. Graham suggests. Bee Cave's suggestion that these are merely "differences from year to year" strains credibility.

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[356] *Id.* at page 212 through 213.

[357] WTCPUA Exhibit No. 1 at Attachment Q.

[358] Hays County Brief at 15.

[359] TCMUD 12 Initial Brief at Attachment C.

[360] Tr. 363, 4-16.

WTCPUA cites to the Multi-County decision[361] claiming that decision stands for the propositions that a change in conditions is not a change in methodology, and that a fluctuation within the components making up the revenue requirement is not a change in methodology.[362] In that case, the Upper Leon River Municipal Water District (Upper Leon) supplied water to the City of Hamilton, (Hamilton) who then resold water to Multi-County Water Supply Corporation (MCW). Upper Leon increased the rate paid by Hamilton by 14 cents per thousand gallons.[363] Hamilton passed through the 14 cent per thousand gallons increase to MCW. MCW appealed the increase.[364] The Hamilton City Administrator testified that the only difference between the rates before and after the increase was the addition of the 14 cent increase onto the cost of the treated water, and other than that the methodology used to calculate the rate increases had stayed the same. The ALJ agreed and ruled that there were no changes in methodology.[365] WTCPUA in 2014 did not merely pass through an increase from its wholesale supplier, but rather completely changed the methodology for calculating the Monthly Charge.

3. Conclusion: If there was a change in the methodology for the computation of the revenue requirement or rate, does the Protested Rate evidence WTCPUA's abuse of monopoly power?

The methodology used to compute the revenue requirement, the Monthly Charge and the Volume Rate has changed. The methodology used to compute the Volume Rate was changed to include a raw water loss fee, although the Wholesale Water Service Agreement explicitly states that the Volume Rate does not include any charges for raw water.[366] The methodology used to compute the Monthly Charge was changed in many ways as shown in the Standard or Form Contract Amendment. Through the definitions and methodology described in the contract amendment and applied to TCMUD 12, the WTCPUA is shifting costs that should be recovered

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[361] WTCPUA Brief at 71, fn 258.

[362] WTCPUA specifically cites to page 19 the Multi-County PFD. On that page immediately following the sentence addressing change of conditions referenced by the WTCPUA is the following sentence: Mr. Yanke [the prevailing party's expert witness] testified that a change in methodology would be 'reflective of a change in the basis or approach for determining the revenue requirement *or allocation of costs*.'" WTCPUA's brief is silent on that point.

[363] WTCPUA Brief at Attachment D, at 193.

[364] *Id.*

[365] *Id* at 19, Finding of Fact 57.

[366] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct), JAD Exhibit 4 at 12 of 27, Section 4.01(e).

by the Connection Fee[367] to the Monthly Charge, which constitutes a change in methodology for computing the rates to wholesale customers. Although the WTCPUA is authorized to collect the Connection Fee, it is not authorized to set the Connection Fee.[368] WTCPUA's change of methodology for setting the Monthly Charge to incorporate costs that were previously recovered in the Connection Fee, is a way for the WTCPUA to circumvent that prohibition.[369] In addition, the Monthly Charge, which prior to the 2014 Monthly Charge had been calculated on a historic average day and historic peak day, is now calculated solely on a projected or contractual peak day, i.e. the Max Day Reservation.[370]

As a result of the changes to the ***methodology for computing the Monthly Charge***, it ***uses*** not *actual* LUEs but ***projected*** **LUEs and the Wholesale Customer must pay the resulting Monthly Charge "regardless of whether the District meets the buildout projections used to develop the annual debt payment schedule."**[371] These changes tie the Monthly Charge based on each wholesale customer's "buildout projections" to WTCPUA's debt (bond) schedules, and the Monthly Charge methodology cannot be changed because the Monthly Charges are *the source of revenue* for WTCPUA to pay its bond indebtedness. That is why the wholesale customers are going to be charged the escalating Monthly Charge whether or not their projected LUEs materialize. *These changes to the method of computing the revenue requirement and rate evidence WTCPUA's abuse of monopoly power.*

Bee Cave argues that the protested rates did not give rise to a hue and cry about "unreasonable, unjust or unfair rates" – but that is not the applicable standard in this Public Interest phase of the proceeding. As Mr. Joyce points out in his direct testimony, the rule does

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[367] *Id.* JAD Exhibit 4 at 11 of 27, Section 4.01.c. ("The Connection Fee has been designed to fund or recover all or a part of the Costs of the LCRA System for capital improvements or facility expansions intended to serve 'new development' (as that term is defined in the Texas Impact Fee Law, Chapter 395 of the Texas Local Government Code) in the LCRA Service Area . . . .").

[368] TCMUD 12 Exhibit No. 1 (DiQuinzio Direct), JAD Exhibit 5 at 3 of 8, Section 3; Tr. 40:10–15.

[369] Although, as noted above, WTCPUA ignored the Transfer Agreement's prohibition concerning changing the Connection Fee. But the new methodology applies to all WTCPUA wholesale water services customers and TCMUD 12's Transfer Agreement is the only such agreement in evidence, so it cannot be assumed that other assignments or transfer agreements contained identical prohibitions.

[370] WTPUA Exhibit No. 1 (Raushuber), Attachment P at 206-207 and Attachment Q at 212. *See also*, TCMUD 12 Exhibit Nos.: 7 at WTCPUA00003862; 10 at WTCPUA00003874; 13 at WTCPUA00003854; 16 at WTCPUA00003842; 18 at WTCPUA00003904, and 20 at WCTPUA0006021.

[371] WTPUA Exhibit No. 1 (Raushuber), Attachment P at 207 and Attachment Q at 213. *See also*, TCMUD 12 Exhibit Nos.: 7 at WTCPUA00003863; 10 at WTCPUA00003875; 13 at WTCPUA00003855; 16 at WTCPUA00003843; and 18 at WTCPUA00003906.

not contain any qualifying or threshold language that would require the change in computation of the revenue requirement or rate to be unreasonable, unjust or unfair in order for it to evidence abuse of monopoly power.[372] In addition, the standards proposed by Bee Cave – that the resulting rates be unreasonable, unjust or unfair rates and that expenses be "used and useful" – are all matters which relate to the cost of service phase of the hearing.[373]

The WTCPUA, Staff,[374] Bee Cave, and Hays County all point out that rates the WTCPUA charges TCMUD 12 have decreased. However, the uncontroverted evidence shows that the methodology used by the WTCPUA will result in significantly higher rates than under the previous methodology. This was established by WTCPUA's own documents admitted into evidence at the hearing. In Ms. Heddin's letter to the WTCPUA Board, in which she was "proposing a methodology" for 2014, she recommended that "the Agency assesses a monthly minimum bill schedule that **escalates annually**, recovering the same net present value for the allocated customer costs for wholesale customers who do not have the existing consumption and customer base to reasonably absorb the impact." [375] In her recommendation to the Board, Ms. Heddin also explained that "**this escalating fee . . . would <u>not</u> be subject to amendment** except for instances where the Agency refunds its bonds."[376] Furthermore, the evidence establishes that the increases in the Monthly Charge is intentional and intended to raise the WTPUA's revenues. WTCPUA's 2014 rate study acknowledges that overall, the new methodology will lead to an increase in revenues for the WTCPUA: "Wholesale Water Sale Revenues are budgeted to increase for FY 2014 due to proposed changes in wholesale customer rate and rate structure and projected wholesale customer growth."[377] The resultant impact of the proposed new methodology to the wholesale customers is outlined on Ms. Heddin's Schedule 1.[378] Schedule 1, titled "Comparison of Current Structure versus Proposed Wholesale Billing Structure" and

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[372] TCMUD 12 Exhibit No. 2 (Joyce Direct) at 7, 17–21.

[373] See, *for example*, PUC Subst. Rules 24.12, 24.41(i), 24.45(b); and 24.25.

[374] Staff Brief at 18, Hay County Brief at 4–5, 7 and 15.

[375] TCMUD 12 Exhibit No. 5 (Joyce Rebuttal) at JJJ Exhibit R9 at WTCPUA00012018 (WTCPUA Response to TCMUD 12 RFI RFP 1-5 & 1-7, Letter from Water Resources Management, LLC to WTCPUA Board President Larry Fox dated March 12, 2013), Recommendation No. 2 (emphasis added).

[376] TCMUD 12 Exhibit No. 5 (Joyce Rebuttal) at JJJ Exhibit R9 at WTCPUA00012018 (emphasis in original).

[377] *Id.*, at JJJ Exh. R29 WTCPUA Budget FYE 2014, page 22.

[378] *Id.*, at JJJ Exhibit R9 at WTCPUA00012017.

shows that Ms. Heddin's new rate methodology in comparison to WTCPUA's 2013 rate methodology would have more than doubled (i.e., 118% increase) TCMUD 12's cost.[379] While the rates undeniably decreased for the first year, WTCPUA's own documents are equally unequivocal in proving that the new methodology is intended to and will lead to escalating rates in the future. This is not a hypothetical increase, it is the direct result of the new methodology adopted by WTCPUA beginning in 2014.

It is significant that WTCPUA's methodology results in a decrease the first year, and then begins a steady climb for the next several years. In order to appeal a decision impacting rates under Water Code Chapter 13, the appeal must be filed within 90 days of that decision.[380] The unwary wholesale customers may be lulled into complacency by the first year decrease in rates and not realize the significance of the methodology change until the narrow window to bring an appeal has passed. Any subsequent rate changes based on the same methodology will not be subject to challenge on the basis that the seller changed the methodology used to compute the rates.

Against this backdrop, it is important to consider how the parties arrived at this point. The history of how the changed rates came to be applied to TCMUD 12 is just as important as the significant rate escalation. TCMUD 5 claims that there is no abuse of monopoly power for the PUA to switch from its prior, arbitrary adoption of a rate to a methodology in which there is not any evidence of wrong doing.[381] However, the following chronicle shows that implementation of the new rate methodology as it was applied to TCMUD 12 was, in fact, an abuse of monopoly power.

The new methodology which changed both the Monthly Charge and the Volume Rate was first proposed by Ms. Heddin in her letter to the WTCPUA Board on March 12, 2013.[382] The changes to the Monthly Charge and the Volume Rate were so significant, that the WTCPUA deemed it necessary to try to obtain a contract amendment to ratify the changes to the method in which the Monthly Charge and the Volume Rate were calculated. By May 2013, Ms. Heddin's proposal had been formalized and changes to computation of both the Monthly Rate and the

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[379] *Id.*, at JJJ Exhibit R9 at WTCPUA00012020

[380] TEX. WATER CODE § 13.043(f) and P.U.C. SUBST. R. 24.130(c)

[381] WTCMUD 5 Brief at 11.

[382] TCMUD 12 Exhibit No. 5 (Joyce Rebuttal) at JJJ Exhibit R9.

Volume Rate are seen in the draft contract amendment sent to the wholesale customers on May 14, 2013.[383]

Despite the WTCPUA and its Participating Entities' claims that the WTCPUA engaged in multi-hour meetings with the wholesale customers in which a lot of information was exchanged, those meeting did little to nothing to alter the changes to the rate methodologies. The final contract amendment which was adopted by the WTCPUA Board on November 21, 2013[384] shows that the new methodologies used to compute the Monthly Charge and the Volume Rate had not changed from the first time they were proposed to the time they were adopted by the WTCPUA. Mr. Rauschuber testified at the hearing on the merits that the form agreement adopted by the WTCPUA Board in November 2013 is in essence the same form agreement that was proposed to the wholesale customers in May 2013.[385] Although some of the wholesale customers did enter into an amendment of their Wholesale Water Services Agreement, TCMUD 12 did not. Nevertheless, the WTCPUA used the new computation methods described in the contract amendment to calculate TCMUD 12's Monthly Charge and volume rate. The ability and willingness of the WTCPUA to – and the fact that it actually did – use the new computation methods described in the contract amendment to calculate TCMUD 12's Monthly Charge and Volume Rate, even though TCMUD 12's Wholesale Water Services Agreement was not amended, evidences WTCPUA exercised its disparate bargaining power, which is an abuse of monopoly power.

The WTCPUA puts forward a test for determining whether there has been an abuse of monopoly power in its Brief.[386] The test laid out in WTCPUA's Brief is from Jack Stowe's testimony.[387] There is nothing in Mr. Stowe's testimony or the WTCPUA's Brief to indicate that this test is anything but something Mr. Stowe made up. There are no citations to any statutes, regulations, or prior dockets to support the notion that this test is correct or has been adopted or used by any regulatory body or court in determining whether an abuse of monopoly power has occurred in a wholesale water rate appeal.

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[383] WTCPUA Exhibit No. 1 (Rauschuber Direct), Attachment P (May 14, 2013, email and draft Amendment Form).

[384] *Id.*, Attachment Q.

[385] Tr. at 482:20–483:6.

[386] WTCPUA Brief at 72.

[387] WTCPUA Exhibit No. 2 (Stowe Direct), 19.

TCMUD 12 does not agree that the test is a proper analysis to determine whether an abuse of monopoly power has occurred in a wholesale water rate appeal. For example, the Public Interest Rule does not contain any requirement that the change in methodology be contrary to "the mutually agreed-upon contractual terms and conditions" in order to support the conclusion that it is an abuse of monopoly power. Assuming however, for the limited purpose of argument, that the test proposed by the WTCPUA is the proper analysis, it is interesting to see what happens when he test is applied to this case.

According to WTCPUA witness Stowe, an abuse of monopoly power occurs if "(1) a wholesale water service provider was determined to have monopoly power, (2) the wholesale water service provider changes its revenue requirement or rate methodology, and (3) the unilateral change in methodology is not in compliance with the mutually agreed-upon contractual terms and conditions."[388]

As to the first prong: "a wholesale water service provider was determined to have monopoly power," as shown above. WTCPUA is a monopoly and has exercised considerable market or monopoly power.

The second prong: "the wholesale water service provider changes its revenue requirement or rate methodology." The WTCPUA changed the revenue requirement methodology by allocating certain expenses from "retail only" to "common to all." The WTCPUA changed the volume rate by incorporating a raw water loss fee. The WTCPUA changed the Monthly Charge in numerous ways including: changing the way the Annual Allocated Debt Service Payment was computed; changing how the District's pro-rata share of the PUA's capital costs is calculated; changing how how the Effective Impact Fee Credit is determined; and requiring a wholesale customer to pay Monthly Charge regardless of whether the wholesale customer actually meets the buildout projections used to develop the annual debt payment schedule (actual vs. projected).

The third prong: "the unilateral change in methodology is not in compliance with the mutually agreed-upon contractual terms and conditions." This prong contains two different concepts, each of which is taken up separately.

The first concept is that the changes in methodology must be unilateral. TCMUD 12 did not agree to the changes in methodology. WTCPUA proposed the changes in its proposed amendment to the Wholesale Water Services Agreement and TCMUD 12 did not enter into that

[388] WTCPUA Brief at 72; WTCPUA Exhibit No. 2 (Stowe Direct), 19.

amendment. Despite the fact that TCMUD 12 did not enter into the proposed Wholesale Water Services Agreement, WTCPUA used the methodology set forth in the proposed Wholesale Water Services Agreement to calculate TCMUD 12's Monthly Charge and volume rate. The change to the methodology was unilaterally imposed by the WTCPUA on TCMUD 12 and the rest of the wholesale customers.

The second concept in the third prong is that the change in methodology is not in compliance with the mutually agreed-upon contractual terms and conditions. The revenue requirement is driven by the allocation of certain expenses. Under the Wholesale Water Services Agreement, certain retail expenses may not be considered "costs of the LCRA system" which is then used to develop the Monthly Charge. The WTCPUA took expenses which had been allocated as retail only expenses and changed them to "common to all." As a result, retail expenses that are excluded by the Wholesale Water Services Agreement were included as a "cost of the LCRA [now PUA] system" in the calculation of the Monthly Charge. This is "not in compliance with the mutually agreed-upon contractual terms and conditions" as set forth in the Wholesale Water Services Agreement. The Wholesale Water Services Agreement states that the volume rate shall not include a raw water charge. The unilateral addition of the raw water loss fee to TCMUD 12's volume rate is not in compliance with the mutually agreed-upon contractual terms and conditions as set forth in the Wholesale Water Services Agreement. The numerous changes to the way the Protested Rates, including both the Volume Rate and Monthly Charge are computed are not in compliance with the mutually agreed-upon contractual terms and conditions as set forth in the Wholesale Water Services Agreement. Under the test proposed by the WTCPUA, an abuse of monopoly power has occurred and has been proven in this case.[389]

VIII. TRANSCRIPTION COSTS

WTCPUA notes that the Administrative Procedure Act provides that costs of a transcript ordered by any party ordinarily shall be paid by that party, and states that the costs of the transcript should be borne by each party requesting a copy of the transcript.[390] WTCMUD 5 also recommends that the ALJ should split transcription costs between the parties that ordered a

[389] The use of Mr. Stowe's test as proposed by the WTCPUA is for argument purposes only and in no way reflects TCMUD 12's position on the validity or legality of the test and should be not be considered TCMUD 12's acceptance, endorsement, or recommendation that the test be adopted by the Commission.

[390] WTCPUA Brief at 73.

transcript of the proceeding.[391] TCMUD 12 paid for the cost of the original transcript and copies furnished to the ALJ and PUC ($3,545.36) and requests that *only* that portion of the transcription cost be shared among each party in this case, except the PUC Staff. See, TCMUD 12's Initial Brief at Attachment D.

IX. CONCLUSION AND PRAYER

WTCPUA is a monopoly as a matter of law, as PUC Staff confirms. That it operates as a monopolist in the provision of wholesale water services to TCMUD 12 is confirmed by its dominant position in the wholesale water services market and its ability to control prices and quantities. Under modern economic theory, WTCPUA is a monopoly because it exercises exclusive control over the provision of wholesale water services to The Highlands. WTCPUA satisfies the definitions of monopoly that are appropriate for this Public Interest proceeding, and the fact that it stepped into LCRA's shoes as the provider of water services under the Wholesale Water Services Agreement does not create an exception for WTCPUA as a monopolist. WTCPUA exercises control over the rates and it is irrelevant that power was obtained through a contract. WTCPUA and the Participating Entities contracted with each other to "protect the value of the assets" which are intended to create barriers to new entrants and to prohibit the Participating Entities to become competitors to WTCPUA. The law and every credible expert analysis supports only one finding – WTCPUA is a monopoly under P.U.C. Subst. R. 24.133(a)(3)(A).

As a monopolist, *WTCPUA has disparate bargaining power*. TCMUD 12's long term Wholesale Water Services Agreement means that TCMUD 12 substantially has no alternatives to obtain water service from another provider. When TCMUD 12 entered into the Agreement in 2009 with LCRA, and continuing through 2014, there were no viable alternative wholesale water service providers that could serve The Highlands. Although the Respondents proposed multiple hypothetical alternative suppliers, each alternative presented its own set of impracticalities as explained by TCMUD 12's General Manager. The other parties failed to present any affirmative evidence of an existing or practical new alternative wholesale water service provider and TCMUD 12's evidence to the contrary is persuasive and was not rebutted. Instead Respondents and Staff rely upon speculation and conjecture in their attempt to identify a wholesale water

[391] WTCMUD 5, Brief at 11.

service provider that could serve The Highlands, in a failed attempt to escape the inescapable conclusion that no such alternatives exist. The Wholesale Water Services Agreement, which was transferred to WTCPUA, is a long term contract, that allows WTCPUA "at any time" to set and collect the wholesale Monthly Charge and Volume rate. When there is a long term contract and the seller unilaterally sets the rates, which are then contested, the commission that created the bifurcated process anticipated these facts could support a finding that the Protested Rates are adverse to the public interest. *WTCPUA exercised its disparate bargaining power in setting the protested rates, which evidences its abuse of monopoly power.*

The Respondents and Staff are aligned in their theory of this case: Even if WTCPUA has violated one of the public interest factors, the 2014 rate change should not be found to be adverse to the public interest because the rate change resulted in rates *lower* than those previously charged.[392] However, the theory that a rate change that does not immediately result in a rate increase cannot be adverse to the public interest is not supported by citation to any rule, statute, or precedent, and cannot be reconciled with the plain reading of the Public Interest rule nor is it supported by any discussion in the Preamble. Rather, TEX. WATER CODE § 13.043(f) refers to "a decision of the provider of water service affecting the amount paid for water service" and it is undisputed that WTCPUA's action in November 21, 2013 affected the amount TCMUD 12 pays for water service. Similarly, P.U.C. SUBST. R. 24.133 uses the term "rate," not "increased or higher or larger" rate, and those words cannot be implied. The word "rate" must be interpreted consistent with TEX. WATER CODE § 13.002(17) and P.U.C. SUBST. R. 24.3(38). When the definition of "rate" and each of the defined terms within that definition are properly understood, it is clear that the Commission is charged with determining if WTCPUA's 2014 Wholesale Water Rates, including the "rules, regulations, practices, or contracts affecting" the compensation demanded, *i.e.,* the methodology utilized to set the Protested Rate, adversely affects the public interest.[393]

WTCPUA's exercise of its disparate bargaining power was enabled by the lack of any alternative providers that could have provided wholesale water service to The Highlands. The Respondents here elected to not present any direct evidence of alternative providers, but instead approached the case by creating multiple hypothetical scenarios of alternatives that they

[392] WTCPUA Brief at 13; PUC Staff Brief at 4.

[393] P.U.C. SUBST. R. 24.132(a)

suggested might have been viable. TCMUD 12's General Manager persuasively explained that each hypothetical thrown out by WTCPUA was not viable, was not cost-effective, could not be funded by TCMUD 12, or was based on a complete misunderstanding of the facts. The alternatives proposed by WTCPUA are not reasonable, viable options for The Highlands as indicated in Section VII. B. 1.b., above, which in sum include: (i) The Highlands does not use treated water for irrigation and there is no third party from whom TCMUD 12 could buy raw water for irrigation in order to reduce its demand for wholesale water services; (ii) neither the Lakeway Regional Raw Water Transportation System (which does not include water treatment or distribution facilities connected to The Highlands), nor its owners, LMUD, HCMUD, TCMUD 11 or the Rough Hollow HOA, could provide wholesale water service to The Highlands even if the TCMUD 12 "emergency interconnect" was ever authorized to operate; (iii) TCMUD 12's construction of its own water services system was never a viable alternative for practical and economic reasons and TCMUD 12 does not have the financial wherewithal to undertake that construction; (iv) Section 3.03.c. of the Wholesale Water Services Agreements limits TCMUD 12's ability to acquire water services from a third party; (v) the City of Austin is not an alternative provider of wholesale water services available to TCMUD 12; (vi) in considering alternatives, one factor may be whether the cost of an alternative is reasonable and affordable – which TCMUD 12's construction of its own system was not. However, if hypothetical alternatives are not demonstrably viable or reasonable, the cost of or operating expenses for those hypothetical alternatives is irrelevant; (viii) TCMUD 12 has a contractual right to a daily flow rate of 3.98 MGD of potable water, and that is the quantity of water services that should be used to determine the viability of any hypothetical alternative supplier. *The absence of any viable, reasonable alternative supplier that could provide wholesale water services to The Highlands enabled WTCPUA to exercise its disparately greater bargaining power in setting the Protested Rates and that evidences an abuse of monopoly power.*

Other factors that evidence WTCPUA's disparate bargaining power that enabled it to act contrary to the public interest in setting the Protested Rates, include: (i) WTCPUA has the unilateral right to change the monthly charge and volume rate "at any time" under the express terms of the Wholesale Water Services Agreement; (ii) none of the specific provisions of the Wholesale Water Services Agreement relied upon by WTCPUA support a finding that TCMUD 12 "freely negotiated" those provisions, or that those provisions tipped the balance of power in

favor of TCMUD 12; (iii) the reservation of capacity for which LCRA required TCMUD 12 to prepay will continue to be controlled by WTCPUA even if an alternative provider could be found, and therefore the costs associated with that reserved capacity that would be stranded must be considered when examining the cost of alternative providers; (iv) holding meetings with wholesale customers where no concessions were made did nothing to diminish WTCPUA's disparate bargaining power; and (v) the part of WTCPUA's offer to amend TCMUD 12's Wholesale Water Services Agreement that included the offer to lower WTCPUA's obligation to provide 3.98 MGD of daily flow was not an option that would have benefitted TCMUD 12 but was touted as the primary purpose for the amendment as a subterfuge for the real purpose of the Amendment, which was to contractually bind TCMUD 12 to the new, onerous revenue requirement and rate methodology.

WTCPUA changed the methodology for computing the revenue requirement and the wholesale Volume rate and Monthly Charge. Those methodological changes, and the way they were implemented, demonstrate an abuse of monopoly power. A change in methodology that evidences an abuse of monopoly power is not limited to a change between the Cash Needs versus the Utility Basis, as all the other parties contend. However, because the other parties relied entirely upon their theory that the only change that was relevant was Cash v. Utility Basis, they failed to present any direct evidence to rebut TCMUD 12's direct case which described the methodology changes that were made. In addition, the record is replete with references from WTCPUA's rate analyst and counsel to the new, proposed or changed methodology that was adopted in setting the Protested Rates. It is undisputed that WTCPUA changed, for example, the allocation method from retail-only to common to all, and that is a change to the revenue requirement methodology from the methodology established in the Wholesale Water Services Agreement. These allocation changes do not represent year to year fluctuations, but rather are changes to the methodology itself. The WTCPUA also changed the methodology it used to calculate the Volume Rate and Monthly Charges which are protested by TCMUD 12. WTCPUA changed the methodology for determining the Volume Rate by adding a raw water loss fee, which is a *significant* change in methodology that is detrimental to TCMUD because the Wholesale Water Service Agreement states that the volumetric rate will *not* include any charges for raw water. Changes to the methodology implemented for 2014 are evident from WTCPUA's Rate Analysis workpapers and are also plainly spelled out in the Wholesale Water Service

Amendment offered to TCMUD 12 and other wholesale water services customers. The Monthly Charge formula used in the contract amendments is the methodology used to set TCMUD 12's Monthly Charge for 2014, even though TCMUD 12 did not agree to the contract amendment. Importantly, WTCPUA's own documents acknowledge that these changes in methodology are *designed* to lead to a significant increase in the Monthly Charges because the methodology is tied to WTCPUA's bond series which will be issued in 2013, 2015, and 2019. Furthermore, as a result of WTCPUA's changes to the methodology for computing the Monthly Charge, the wholesale water services customers are going to be charged the escalating Monthly Charge whether or not the customer's *projected* LUEs, that are imbedded in the new Monthly Charge calculation methodology, materialize. The change in methodology from actual historical usage to projected usage, that is not intended to be revised in subsequent years, undoubtedly benefits WTCPUA, but represents a significant harmful change to TCMUD 12. The fact that the WTCPUA sought to ratify these changes through a contract amendment that TCMUD 12 declined to accept and then imposed them on TCMUD 12 anyway evidences WTCPUA's abuse of its monopoly power. In sum, WTCPUA abused its monopoly power by changing the methodology for computing the revenue requirement and the rate charged to TCMUD 12, and that abuse is contrary to the public interest.

In conclusion, based upon the evidence presented in this case, TCMUD 12 respectfully prays that the ALJ recommend that the Commission enter an Order that states:

> The Commission has determined the protested rates, including WTCPUA's new methodology for setting the wholesale water services rates, adversely affects the public interest. The Commission concludes the following public interest criteria have been violated: WTCPUA abused its monopoly power in its provision of wholesale water services to TCMUD 12 based upon WTCPUA's disparate bargaining power and WTCPUA change to the computation of the revenue requirement and rate from one methodology to another. The Commission remands the matter to the State Office of Administrative Hearings for further evidentiary proceedings on the rate pursuant to P.U.C. Subst. R. 24.135.

Respectfully Submitted,

SMITH TROSTLE & HUERTA LLP
4401 Westgate Blvd., Ste. 330
Austin, Texas 78745
(512) 494-9500 (Telephone)
(512) 494-9505 (Facsimile)
ktrostle@smithtrostle.com

By: J. Kay Trostle
J. Kay Trostle
State Bar No. 20238300
Miguel A. Huerta
State Bar No. 00787733

ATTORNEYS FOR TRAVIS COUNTY MUNICIPAL UTILITY DISTRICT NO. 12

CERTIFICATE OF SERVICE

I hereby certify that on this 3rd day of August 2015, a true and correct copy of the above and foregoing document is being served via electronic mail, facsimile, U.S. mail and/or hand delivery to all parties of record.

J. Kay Trostle

Opinion issued June 25, 2015.

In The

Court of Appeals

For The

First District of Texas

NO. 01-14-00102-CV

NAVARRO COUNTY WHOLESALE RATEPAYERS; M.E.N. WATER SUPPLY CORPORATION; ANGUS WATER SUPPLY CORPORATION; CHATFIELD WATER SUPPLY CORPORATION; CORBET WATER SUPPLY CORPORATION; CITY OF BLOOMING GROVE; CITY OF FROST; CITY OF KERENS; AND COMMUNITY WATER COMPANY, Appellants

V.

ZACHARY COVAR, EXECUTIVE DIRECTOR OF THE TEXAS COMMISSION ON ENVIRONMENTAL QUALITY; THE TEXAS COMMISSION ON ENVIRONMENTAL QUALITY, ITS COMMISSIONERS, BRYAN SHAW, CARLOS RUBENSTEIN AND TOBY BAKER, AND CITY OF CORSICANA, Appellees

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On Appeal from the 419th District Court
Travis County, Texas[1]

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[1] Pursuant to its docket equalization authority, the Supreme Court of Texas transferred the appeal to this Court. *See* Misc. Docket No. 14-001 (Tex. Jan. 7,

Trial Court Case No. D-1-GN-12-000226

MEMORANDUM OPINION

This is an administrative law case in which the plaintiffs, wholesale purchasers of water from the City of Corsicana, challenge the trial court's judgment affirming an order by the Texas Commission on Environmental Quality that dismissed their rate appeal. At issue was whether the plaintiffs, pursuant to 30 TEX. ADMIN. CODE § 291.133, carried their burden to show that the protested rate "adversely affected the public interest." We affirm.

BACKGROUND

The Parties and the Contracts

The City of Corsicana is the regional water provider in Navarro County and provides service to over 11,000 retail customers and 21 wholesale customers. Plaintiffs are eight of Corsicana's wholesale customers [collectively, "the Ratepayers"]. Of Corsicana's 11,000 retail customers, 9,000 are residential retail customers. The average water use of a residential retail user is less than 6,000 gallons per month. In contrast, each of the wholesale ratepayers purchases over 1,000,000 gallons of water per month, which it then resells to its own retail customers.

2014); *see also* TEX. GOV'T CODE ANN. § 73.001 (West 2013) (authorizing transfer of cases).

Corsicana sells water to the Ratepayers pursuant to individual contracts. Since the 1960s, the contracts have given Corsicana the right to raise its rates. In 2001, Corsicana created a "standard contract," which was intended to be used whenever a wholesale customer amended its contract. Seven of the Ratepayers—M.E.N. Water Supply Corporation, Angus Water Supply Corporation, Chatfield Water Supply Corporation, Corbet Water Supply Corporation, City of Frost, and Community Water Company—entered into the standard contract. Two of the Ratepayers—City of Blooming Grove and City of Kerens—did not. The standard contract provides the following regarding rate changes:

> Section 4.02. The rates stated in the contract are the prevailing rates which "may be changed or modified from time to time by Seller in accordance with Section 4.03 of this Contract during the time it remains in effect.
>
> Section 4.03. Rate Revision. Purchaser acknowledges and agrees that Seller's city council has the right to revise by ordinance, from time to time and as needed, the rates charged hereunder to cover all reasonable, actual, and expected costs incurred by Seller to provide the potable water supply service to Seller's customers. Except as provided in subsection b below, if, during the term of this contract, Seller revises its minimum inside city retail water rate, then such revised rate shall likewise apply to water usage by Purchaser under this Contract.

Early versions of the contracts in the 1960s and 1970s charged all customers on a declining block rate, i.e., a rate in which the price per 1,000 gallons decreases as usage increases. Later, Corsicana used a flat volumetric rate for all customers. From 2006 to 2008, Corsicana raised its volumetric rate from $2.14 per 1,000

gallons to $3.00 per 1,000 gallons. Nevertheless, by 2008, Corsicana's "Utility Fund," which is comprised of revenues and expenses from its water and wastewater utilities had a $1 million shortfall. Because Corsicana does not operate on credit, it must have a cash reserve available to cover potential shortfalls and emergencies.

The 2009 Rate Increase

One of the ways that Corsicana sought to increase its Utility Fund was to raise its water rates. Under the rate adopted, Corsicana charges each of its customers—both wholesale and retail—a monthly base rate that is determined by the size of the customer's meter. The base rates range from $17.60 for a 5/8- or 3/4-inch meter to $1,695.52 for a 10-inch meter. Regardless of the meter size, the base rate includes the first 1,000 gallons used per month. For water use in excess of 1,000 gallons per month, Corsicana charges tiered volumetric rates, in inclining blocks. The volumetric rate is $3.00 per 1,000 gallons for 1-10,000 gallons; $3.15 per 1,000 gallons for 10,001-25,000 gallons; and $3.25 per 1,000 gallons for over 25,000 gallons.

The Ratepayers' Appeals

Arguing that the 2009 rate increase disproportionately affected wholesale ratepayers when compared to residential retail ratepayers, the Ratepayers appealed Corsicana's rate change by filing a Petition with the Texas Commission on

Environmental Quality ["the Commission"]. The Commission referred the case to the State Office of Administrative Hearings ["SOAH"], where an Administrative Law Judge ["ALJ"] conducted a hearing to determine whether the rate change "affected a public interest." *See* 30 TEX. ADMIN. CODE §§ 291.131-.133. After the hearing, the ALJ issued a Proposal for Decision ["PFD"] and a proposed order finding that the Ratepayers failed to show that the 2009 rate increase adversely affected the public interest. After considering the ALJ's PFD, the Commission agreed that the Ratepayers had failed to show that the rate change adversely affected the public interest, holding that "[t]he public-interest inquiry set out in 30 TAC § 291.133(a)(1)-(4) does not include a comparison of the protested rate's impacts on wholesale and retail customers." The Ratepayers then appealed to the Travis County District Court, which affirmed the Commission's order dismissing the rate appeal. This appeal followed.

PROPRIETY OF COMMISSION'S "PUBLIC INTEREST" RULING

In four issues on appeal, the Ratepayers contend that:

1. Rate discrimination must be considered in a public interest hearing;

2. If the Commission correctly interpreted the public interest rules to preclude consideration of rate discrimination, the rules are invalid;

3. Corsicana's wastewater subsidy is not a "cost of service" issue; and

4. Corsicana's Utility Fund deficit is not a "changed condition" that may be considered under 30 TAC § 291.133(a)(3)(B) or a factor that supports Corsicana's 2009 Rate Increase.

Standard of Review

The substantial-evidence standard of the Texas Administrative Procedure Act ("APA") governs our review of the Commission's final order. *See* TEX. GOV'T CODE ANN. § 2001.174 (West 2008). The APA authorizes reversal or remand of an agency's decision that prejudices the appellant's substantial rights because the administrative findings, inferences, conclusions, or decisions (1) violate a constitutional or statutory provision, (2) exceed the agency's statutory authority, (3) were made through unlawful procedure, (4) are affected by other error of law, or (5) are arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion. *Id.* § 2001.174(2)(A)-(D), (F). Otherwise, we may affirm the administrative decision if we are satisfied that "substantial evidence" exists to support it. *Id.* § 2001.174(1), (2)(E).

We review the agency's legal conclusions for errors of law and its factual findings for support by substantial evidence. *Heat Energy Advanced Tech., Inc. v. W. Dallas Coal. for Envtl. Justice*, 962 S.W.2d 288, 294–95 (Tex. App.—Austin 1998, pet. denied). Substantial evidence "does not mean a large or considerable