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PUC DOCKET NO. 42866

PETITION OF TRAVIS COUNTY	§	BEFORE THE STATE OFFICE
MUNICIPAL UTILITY DISTRICT	§	
NO. 12 APPEALING CHANGE OF	§	
WHOLESALE WATER RATES	§	
IMPLEMENTED BY WEST	§	
TRAVIS COUNTY PUBLIC	§	OF
UTILITY AGENCY, CITY OF BEE	§	
CAVE, TEXAS, HAYS COUNTY,	§	
TEXAS AND WEST TRAVIS	§	
COUNTY MUNICIPAL UTILITY	§	
DISTRICT NO. 5	§	ADMINISTRATIVE HEARINGS

DIRECT TESTIMONY

OF

RICHARD A. BAUDINO

ON BEHALF OF

WEST TRAVIS COUNTY PUBLIC UTILITY AGENCY

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DECEMBER 19, 2014

**DIRECT TESTIMONY OF
RICHARD A. BAUDINO**

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ATTACHMENTS

A	Resume
B	Excerpts from <i>Microeconomics: Principles, Problems, and Policies</i>
C	TCMUD 12 Response to WTCPUA RFP No. 1-16
D	TCMUD 12 Response to WTCPUA RFA No. 1-44

1 **I. QUALIFICATIONS AND SUMMARY**

2 **A. Qualifications**

3 **Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS.**

4 A. My name is Richard A. Baudino. I am a Consultant with J. Kennedy and Associates,
5 Inc., an economic consulting firm specializing in utility ratemaking and planning
6 issues. My business address is 570 Colonial Park Drive, Suite 305, Roswell, Georgia
7 30075.

8 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
9 **PROFESSIONAL EXPERIENCE.**

10 A. I provide this information in Attachment A, including a list of my testimony
11 experience.

12 **Q. ARE YOU FAMILIAR WITH P.U.C. SUBST. R. 24.133, THE PUBLIC**
13 **INTEREST TEST, AS IT RELATES TO THE PUBLIC UTILITY**
14 **COMMISSION'S ("PUC" OR "COMMISSION") REVIEW OF WHOLESALE**
15 **WATER RATES?**

16 A. Yes, I am. I understand that the issue of whether the wholesale rates adversely
17 impact the public interest is the sole focus of this proceeding.

18 **B. Summary**

19 **Q. ON WHOSE BEHALF ARE YOU PROVIDING TESTIMONY IN THIS**
20 **PROCEEDING?**

21 A. I am providing testimony on behalf of West Travis County Public Utility Agency
22 ("WTCPUA").

1 3. TCMUD 12 had substantial bargaining power in its negotiations with the
2 LCRA (now the WTCPUA). The LCRA (now the WTCPUA) did not have
3 disparate bargaining power over TCMUD 12 during the negotiation of the
4 original wholesale water treatment services contract, the negotiation of the
5 assignment of that contract, or the adoption of the protested rates.

6 4. The LCRA (now the WTCPUA) did not have sole control over the price of its
7 wholesale water treatment service or the quantities provided. TCMUD 12 had
8 significant input into the amount and the price of water treatment services it
9 received from the LCRA (now the WTCPUA).

10 5. The WTCPUA is not abusing monopoly power. Rather, it is acting in a
11 prudent manner according to the wholesale water treatment services
12 agreement it acquired from the LCRA.

13 **Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?**

14 A. Section II of my testimony will present a brief explanation of the creation of the
15 WTCPUA and of the wholesale water treatment services agreement that TCMUD 12
16 originally entered into with the LCRA and that was later assigned to the WTCPUA.
17 This historical background is important because it establishes the LCRA, and later the
18 WTCPUA, not as a monopolist, but rather as a sole source provider of water
19 treatment services pursuant to an agreement with TCMUD 12. At the time this
20 agreement was entered into, TCMUD 12 had at least one other option to taking
21 wholesale water treatment services from the LCRA. However, it is unclear if
22 TCMUD 12 did a thorough investigation of other potential providers of these
23 services.

1 which the LCRA agreed to provide wholesale services for the treatment of raw water,
2 and the delivery of that treated water to TCMUD 12.¹ The obligations of the LCRA
3 under the TCMUD 12 Agreement were transferred to the WTCPIUA, with the
4 agreement of the TCMUD 12, through the "Agreement Regarding Transfer of
5 Operations of the West Travis County Water System from the Lower Colorado River
6 Authority, to the West Travis County Public Utility Agency," ("2012 Amendment")
7 between LCRA, WTCPIUA, and TCMUD 12, effective on March 19, 2012.² By
8 virtue of these agreements, the WTCPIUA accepted the responsibility of serving the
9 customers, including TCMUD 12, that were formerly served by the LCRA.
10 Essentially, the WTCPIUA stepped into the shoes of the LCRA's TCMUD 12
11 Agreement.

12 **III. ANALYSIS OF MARKET POWER AND**
13 **BARGAINING POWER**

14 **A. 2009 TCMUD 12 Agreement**

15 **Q. DID TCMUD 12 ORIGINALLY HAVE ALTERNATIVES TO PURCHASING**
16 **WATER TREATMENT SERVICES FROM THE LCRA?**

17 **A.** Yes. TCMUD 12 witness DiQuinzio admits that TCMUD 12 had alternatives to
18 LCRA's water treatment services.³ In 2009, TCMUD 12 apparently determined that
19 the alternatives were more expensive than purchasing wholesale water treatment
20 services from LCRA. TCMUD 12 then opted to purchase wholesale water treatment
21 services from LCRA.

¹ The TCMUD 12 Agreement is attached to the testimony of Mr. Donald G. Rauschuber. In the interest of conserving resources, I am not also attaching it to my testimony.

² The 2012 Amendment is attached to the testimony of Mr. Donald G. Rauschuber. In the interest of conserving resources, I am not also attaching it to my testimony.

³ Direct Testimony of Joseph A. DiQuinzio, Jr. at 5-6 and 13 (Oct. 31, 2014).

1 to the operation and maintenance of the system and associated expenses, all related to
2 the system used to provide the wholesale water treatment services.

3 **Q. DOES ARTICLE IV OF THE TCMUD 12 AGREEMENT CONTAIN**
4 **LANGUAGE THAT INDICATES THAT THE SYSTEM WAS SET UP BY**
5 **THE LCRA AND ITS CUSTOMERS FOR THEIR MUTUAL BENEFIT?**

6 A. Yes. Section 4.03 – LCRA System to be Self-Sufficient contains the following
7 agreement:

8 The LCRA System shall be comprised of the facilities
9 described in Recital No. 1, together with such improvements,
10 extensions, enlargements, betterments, additions, and
11 replacements thereto as are reasonable and necessary to
12 provide water to the LCRA Service Area and Wholesale Water
13 Services to District No. 12 on behalf of the Districts. The
14 parties agree that the Costs of the LCRA System shall be
15 allocated to and borne by all of the customers of the LCRA
16 System, including District No. 12, in a fair and equitable
17 manner and so that the LCRA System is self-sufficient.

18 The facilities referred to in Recital No. 1 comprise the West Travis County
19 Regional Water System. This language is quite clear that LCRA and its customers
20 entered into a mutually beneficial agreement whereby the LCRA provided water
21 treatment services at cost, that rates would be non-discriminatory, and that those rates
22 would support the system being self-sufficient.

23 **Q. DID THE TCMUD 12 AGREEMENT PROVIDE AN AVENUE FOR TCMUD**
24 **12 TO PROTEST, DISPUTE OR APPEAL THE CHARGES AND RATES**
25 **CONTAINED IN THE AGREEMENT?**

26 A. Yes. Section 6.06 – Protests, Disputes or Appeals protected TCMUD 12's rights to
27 dispute and even appeal the rates and charges from LCRA:

1 **Q. DOES THE FOREGOING DISCUSSION SUPPORT YOUR VIEW THAT**
2 **INSTEAD OF BEING A MONOPOLY, LCRA WAS CHOSEN IN 2009 BY**
3 **TCMUD 12 AS A SOLE PROVIDER OF WHOLESALE WATER**
4 **TREATMENT SERVICES?**

5 A. Yes. It is quite clear that in 2009 TCMUD 12 chose the LCRA to be its sole provider
6 and that the TCMUD 12 Agreement was freely negotiated between the LCRA and
7 TCMUD 12 for the mutual benefit of both parties. It is clear from the terms of the
8 TCMUD 12 Agreement that TCMUD 12 is a large customer that was fully capable of
9 negotiating contract terms and protections for its position as a buyer of services from
10 LCRA. Recital No. 4 of the TCMUD 12 Agreement underscores this with the
11 following language:

12 District No. 12 desires to obtain wholesale services for the
13 treatment of raw water and delivery of potable water to District
14 No. 12, on behalf of the Districts, from the LCRA System, and
15 LCRA desires to provide such services to District No. 12, on
16 behalf of the Districts.

17 **Q. MR. BAUDINO, WHY IS IT IMPORTANT FOR THE PUC TO**
18 **UNDERSTAND THE HISTORICAL RELATIONSHIP BETWEEN LCRA**
19 **AND TCMUD 12 IN ITS DETERMINATION OF WHETHER THE WTCPUA**
20 **IS ACTING AS A MONOPOLY?**

21 A. It is vitally important because, as described above, the WTCPUA stepped into the
22 shoes of the LCRA with respect to its provision of wholesale water treatment services
23 to TCMUD 12 and other customers who formerly took service from the LCRA. The
24 original TCMUD 12 Agreement that was negotiated between the LCRA and TCMUD
25 12 was, in my opinion, clearly an arms-length transaction that established the LCRA
26 as a sole source provider of wholesale water treatment services to TCMUD 12, not as

1 **C. Adoption of 2013 Rates**

2 **Q. DO YOU HAVE AN OPINION AS TO THE BARGAINING POWER OF**
3 **TCMUD 12 AT THE TIME THAT THE WTCPUA ADOPTED THE RATES**
4 **THAT ARE THE SUBJECT OF THIS PROCEEDING?**

5 A. Yes. Based on WTCPUA witness Mr. Rauschuber's Direct Testimony, the
6 WTCPUA undertook extensive efforts to involve its wholesale customers in the
7 development of the wholesale water treatment services rates prior to their adoption in
8 November 2013. The fact that the WTCPUA undertook these efforts and used the
9 input received from the wholesale customers, and the additional fact that the
10 WTCPUA afforded the customers an opportunity to revise their contractual
11 obligations, leads me to conclude that the TCMUD 12 exercised significant
12 bargaining power prior to the adoption of the 2013 rates by the WTCPUA.

13 **D. Monopoly Market Structure and its Applicability to the LCRA and**
14 **the WTCPUA.**

15 **Q. ACCORDING TO ECONOMIC LITERATURE, WHAT CONDITIONS**
16 **CHARACTERIZE A MONOPOLY MARKET STRUCTURE?**

17 A. In economics literature, there are several generally recognized conditions that
18 characterize a pure monopoly market structure. For purposes of this proceeding,
19 I refer to *Microeconomics: Principles, Problems, and Policies* by Campbell R.
20 McConnell, Stanley L. Brue, and Sean M. Flynn. This is one of the standard
21 textbooks on basic microeconomic theory and is used in universities throughout the
22 United States. This book is also commonly relied upon by economists. In Chapter
23 12, Pure Monopoly, the authors provide five basic characteristics of a monopoly
24 market. These five characteristics are as follows:

1 Agreement between the LCRA and TCMUD 12 and evaluate whether the LCRA was
2 a monopoly provider of wholesale water treatment services to TCMUD 12.

3 **Q. PLEASE ADDRESS THESE MONOPOLY CHARACTERISTICS AS**
4 **APPLIED TO THE LCRA/WTCPUA.**

5 A. In conducting my examination, I will apply the first, third, and fourth characteristics
6 of a monopoly market to the wholesale water treatment services provided first by the
7 LCRA and then by the WTCPUA. In one sense, it is correct that there are no *existing*
8 adequate substitutes for wholesale water treatment services, but TCMUD 12 chose
9 not to exercise an ownership alternative or to seek alternative providers of those
10 services.

11 **Q. THE FIRST NOTED CHARACTERISTIC OF A MONOPOLY MARKET IS**
12 **THAT THERE IS ONLY ONE PROVIDER OF A GOOD OR SERVICE. WAS**
13 **THE LCRA THE ONLY OPTION FOR THE PROVISION OF WHOLESALE**
14 **WATER TREATMENT SERVICES TO TCMUD 12?**

15 A. No. TCMUD 12 chose the LCRA as a sole source provider after looking at its
16 available options and determining that the LCRA was the most economic provider of
17 wholesale water treatment services. TCMUD 12 witness DiQuinzio described this
18 process in his Direct Testimony.⁵ DiQuinzio explained that TCMUD 12 made the
19 decision that building and operating its own system would have been more expensive
20 than taking service from the LCRA, and then it decided to negotiate a separate
21 wholesale water services agreement with the LCRA. Therefore, it is clear that

⁵ Direct Testimony of Joseph A. DiQuinzio, Jr. at 5-6 (Oct. 31, 2014).

1 Q. IF TCMUD 12 FAILED TO FULLY EXPLORE ITS OPTIONS FOR
2 WHOLESALE WATER TREATMENT SERVICES, CAN ONE
3 OBJECTIVELY CONCLUDE THAT EITHER THE LCRA OR THE
4 WTCPUA ACTED AS MONOPOLISTS?

5 A. Absolutely not. Without full knowledge of available alternative wholesale water
6 treatment services at the time the TCMUD 12 Agreement was entered into by the
7 LCRA and TCMUD 12, one cannot reasonably conclude that the LCRA acted as a
8 monopoly provider of wholesale water treatment services to TCMUD 12.

9 Furthermore, since the WTCPUA essentially stepped into the shoes of the
10 LCRA in terms of assuming its rights and responsibilities under the TCMUD 12
11 Agreement, one also cannot conclude that the WTCPUA is a monopoly provider of
12 wholesale water treatment services to TCMUD 12.

13 Q. GIVEN THE FOREGOING DISCUSSION, IS IT APPROPRIATE FOR
14 TCMUD 12 TO NOW ARGUE THAT THE WTCPUA IS OPERATING AS A
15 MONOPOLIST?

16 A. No. In my view, it is highly inappropriate for TCMUD 12 to be arguing at this point
17 in time that the WTCPUA is operating as a monopoly. Basically, TCMUD 12 chose
18 the LCRA (now the WTCPUA) as a sole source provider of wholesale water
19 treatment services after looking at the alternative of owning the treatment facilities
20 itself. The LCRA (now the WTCPUA) was a lower cost, more economic alternative.
21 Furthermore, it is not clear that TCMUD 12 fully and prudently explored all the
22 options available to it at the time it originally entered into the TCMUD 12 Agreement
23 with the LCRA. TCMUD 12 has simply not made the case that the WTCPUA is now
24 operating as a monopoly provider of wholesale water treatment services.

1 TCMUD 12 is now claiming that the WTCPUA is a monopolist. Clearly, the LCRA
2 (now the WTCPUA) is a sole source provider of wholesale water treatment services
3 based on a negotiated agreement. Therefore, The WTCPUA is not a monopolist.

4 **Q. WITH RESPECT TO THE THIRD CHARACTERISTIC OF A MONOPOLY**
5 **MARKET, WAS EITHER THE LCRA OR THE WTCPUA A PRICE MAKER**
6 **WITH COMPLETE CONTROL OVER PRICES AND QUANTITIES?**

7 A. No, definitely not. As I describe above, TCMUD 12 is a large consumer of wholesale
8 water treatment services and voluntarily entered into negotiations with the LCRA for
9 those services. Those negotiations produced the 2009 TCMUD 12 Agreement
10 between the LCRA and TCMUD 12. The TCMUD 12 Agreement contained the rate
11 agreements and service protections I described earlier. In addition, Mr. DiQuinzio
12 testified in his Direct Testimony that TCMUD 12 entered into an extended period of
13 negotiations for specific quantities of water to be treated by the LCRA.⁸ Indeed, this
14 was an arms-length transaction between a buyer and a seller for wholesale water
15 utility service and TCMUD 12 provided no evidence that the LCRA was solely in
16 control of the quantities or prices negotiated and ultimately agreed to by both parties.

17 This third characteristic also was not present in 2012 when the WTCPUA
18 assumed the TCMUD 12 Agreement as part of its purchase of the West Travis
19 County Regional Wholesale Water and Wastewater System ("LCRA System"). As
20 part of its agreement to purchase the LCRA System, the WTCPUA was obligated to
21 obtain the consent of TCMUD 12 to assign the TCMUD 12 Agreement from LCRA
22 to the WTCPUA. Under the TCMUD 12 Agreement, TCMUD 12 could withhold its
23 consent to assignment under limited certain circumstances. However, TCMUD 12

⁸ Direct Testimony of Joseph A. DiQuinzio, Jr. at 6-7 (Oct. 31, 2014).

1 reduce their contractual obligation with the WTCPUA, which is clear evidence that
2 the WTCPUA was not acting as a monopolist, and was not a price maker.

3 The fact that TCMUD 12 was able to negotiate additional considerations from
4 the LCRA and the WTCPUA, and had an opportunity to change the quantity of
5 services purchased from the WTCPUA, shows that it had substantial bargaining
6 power, which is relevant to the P.U.C. SUBST. R. 24.133(a)(3)(A). TCMUD 12 also
7 had additional leverage in terms of being asked for its approval of the proposed
8 transfer of assets from the LCRA to the WTCPUA.

9 **Q. THE FOURTH NOTED CHARACTERISTIC OF A MONOPOLY MARKET**
10 **IS THAT THERE ARE INSURMOUNTABLE BARRIERS TO ENTRY. ARE**
11 **THERE INSURMOUNTABLE BARRIERS TO ENTRY IN THE**
12 **WHOLESALE MARKET FOR WATER TREATMENT SERVICES IN**
13 **TCMUD 12'S SERVICE AREA?**

14 A. No. In examining barriers to entry, there are several types to be considered. First,
15 exclusive service franchises and service territories may be granted by governmental
16 authorities to public utilities, and so constitute insurmountable legal barriers to entry.
17 The purpose of franchises and service territories is to protect the utility from
18 competition. In return, the utility accepts some form of regulation by the
19 governmental entity that granted the franchise or service territory, and usually is
20 tasked with an obligation to serve everyone within the territory. There is no exclusive
21 franchise or exclusive territory for wholesale water treatment services in TCMUD
22 12's geographical area, so this barrier to market entry does not exist.

23 Second, the monopolist may have ownership or control of essential resources.
24 This condition could apply to the LCRA's provision of raw water to TCMUD 12 in

1 copper industries.¹⁰ High cost of entry is a barrier to entry in the jet engine,
2 automobile, commercial aircraft, and petroleum-refining industries.¹¹

3 The important point here is that the presence of economies of scale and high
4 cost of entry do not necessarily point to a monopoly market. Oligopolistic industries
5 also possess these barriers to entry and the industries cited by McConnell/Brue/Flynn
6 are not regulated as to prices charged and/or quantities produced.

7 **IV. RESPONSE TO TCMUD 12 WITNESS ZARNIKAU**

8 **Q. ON PAGE 5, LINES 14 AND 15 OF HIS DIRECT TESTIMONY, TCMUD 12**
9 **WITNESS ZARNIKAU CONCLUDED THAT THE WTCPUA IS A**
10 **MONOPOLY. DO YOU HAVE ANY GENERAL COMMENTS ON HIS**
11 **CONCLUSION REGARDING THE ALLEGED MONOPOLY STATUS OF**
12 **THE WTCPUA?**

13 **A.** Yes. As a general matter, TCMUD 12 witness Zarnikau failed to address the history
14 of the TCMUD 12 Agreement and the bargaining between TCMUD 12 and the
15 LCRA. He took a sole supplier agreement and concluded that this was evidence of a
16 monopoly. This logic and approach is fatally flawed for the reasons I have already
17 discussed.

18 As I stated earlier in my testimony, it is critical to understand how TCMUD
19 12 and the LCRA reached the TCMUD 12 Agreement that was assumed by the
20 WTCPUA in 2012. The WTCPUA stepped into the role of a sole source provider of
21 wholesale water treatment services for TCMUD 12 pursuant to an already existing

¹⁰ Campbell R. McConnell, Stanley L. Brue, and Sean M. Flynn, *Microeconomics: Principles, Problems, and Policies* at 286 (2013) (see Attachment B).

¹¹ *Id.* at 287.

1 would be associated with such a system. TCMUD 12 witness Zarnikau provided no
2 economic, financial, or accounting analysis of his own with which one could compare
3 the per unit costs of a new system with the costs and rates at which the LCRA was
4 willing to provide wholesale water treatment services. In my opinion, Zarnikau does
5 not provide an adequate foundation for his conclusion. Apparently, TCMUD 12 also
6 failed to consider such alternatives as whether development of a water treatment
7 system could be phased-in or totally built out, which could also affect the economics
8 of alternative water treatment options.

9 **Q. ON PAGE 8, LINES 21 THROUGH 24, TCMUD 12 WITNESS ZARNIKAU**
10 **TESTIFIED THAT BUILDING A NEW SYSTEM “MIGHT LEAD TO THE**
11 **ABANDONMENT OF CAPACITY RESERVED ON THE SYSTEM**
12 **CONTROLLED BY THE SUPPLIERS WHICH TCMUD 12 HAS ALREADY**
13 **PAID FOR.” DO YOU AGREE?**

14 **A.** No. Zarnikau’s point here is extremely important, but not in the manner he suggests.
15 The fact is that TCMUD 12 had a very strong financial incentive to continue taking
16 service under the TCMUD 12 Agreement that was assumed by the WTCPUA. Based
17 on the TCMUD 12 Agreement that TCMUD 12 negotiated with the LCRA,
18 TCMUD 12 was credited with the Connection Fees it paid, and in return, was
19 guaranteed reservation capacity in the LCRA system for the number of living unit
20 equivalents (“LUE”) for which a Connection Fee had been paid up to TCMUD 12’s
21 contractual capacity of 2,125 LUEs. Mr. DiQuinzio noted in his Direct Testimony
22 that one of the critical provisions that induced TCMUD 12 to approve the 2012
23 Amendment was the transfer of the paid Connection Fees from the LCRA to the
24 WTCPUA, which ensured that TCMUD 12 received full credit for the paid

1 Q. ON PAGES 8 THROUGH 9 OF HIS DIRECT TESTIMONY, TCMUD 12
2 WITNESS ZARNIKAU SPECULATED ON HOW THE WTCPUA MIGHT
3 RESPOND TO AN ATTEMPT BY TCMUD 12 TO DEVELOP A
4 COMPETING SYSTEM THAT WOULD REPLACE THE WTCPUA'S
5 WATER TREATMENT SYSTEM. DO YOU AGREE WITH HIS
6 SPECULATION?

7 A. No. Not only is Zarnikau's testimony irrelevant, it is completely inapplicable as to
8 the question of whether the WTCPUA is a monopoly. The "No Competition"
9 provision in the "Acquisition, Water Supply, Wastewater Treatment and Conditional
10 Purchase Agreement" is between *the Participants of the WTCPUA*, not between the
11 WTCPUA and any of its wholesale customers. Section 7.07(h) of this agreement
12 essentially protects the value of the assets purchased by the WTCPUA from the
13 LCRA. This clause is mutually beneficial to the Participants of the WTCPUA. It
14 does not, and cannot, prohibit competition from other providers of wholesale water
15 treatment service.

16 Q. ON PAGE 10 OF HIS DIRECT TESTIMONY, TCMUD 12 WITNESS
17 ZARNIKAU CITED § 13.001(b) OF THE TEXAS WATER CODE AND
18 § 31.001(B) OF THE PUBLIC UTILITY REGULATORY ACT WITH
19 RESPECT TO THE DEFINITIONS OF RETAIL PUBLIC UTILITIES. DO
20 THESE PROVISIONS HAVE ANY BEARING ON THE WTCPUA'S
21 PROVISION OF WHOLESALE WATER TREATMENT SERVICES TO
22 TCMUD 12?

23 A. No. The issue before the PUC is whether the WTCPUA is a monopoly provider of
24 *wholesale* water treatment services to TCMUD 12. Zarnikau misinterprets Texas

1 that in 2013 there were, indeed, no practical alternatives, this does not suggest that
2 the WTCPUA now suddenly has disparate bargaining power.

3 TCMUD 12 witness Zarnikau claimed further evidence of disparate
4 bargaining power when the Board of the WTCPUA allegedly ignored the concerns
5 TCMUD 12 expressed over the rates the WTCPUA put into effect for calendar year
6 2014.¹⁷ His allegation here is without merit. As I stated earlier in my testimony, the
7 TCMUD 12 Agreement that the WTCPUA assumed from the LCRA provided in
8 Section 6.06 that TCMUD 12 had the power to protest rates charged by the LCRA, to
9 continue to receive service during the pendency of such protest, and that rates
10 collected subject to protest would be placed in an interest-bearing account. Section
11 7.02 provided TCMUD 12 the ability to examine the books and records of the LCRA
12 with respect to its rates and charges. These protections were preserved when the
13 WTCPUA assumed the TCMUD 12 Agreement. The mere fact that the WTCPUA
14 implemented new rates for calendar year 2014 does not suggest any disparate
15 bargaining power on the part of the WTCPUA. Furthermore, the TCMUD 12
16 Agreement allows for such rate changes in Section 4.01.f., as follows:

17 At any time while this Agreement is in effect, LCRA, subject
18 to applicable law, may modify the Connection Fee, the
19 Monthly Charge and the Volume Rate consistently with the
20 terms of this Agreement as appropriate to recover the Costs of
21 the LCRA System in a just, reasonable and nondiscriminatory
22 manner from District No. 12 and the other customers of the
23 LCRA System.

24 Based on my reading on the TCMUD 12 Agreement, the WTCPUA acted
25 within its rights according to Section 4.01.f.

¹⁷ *Id.* at 15, lines 14-18.

1 cover the costs of its services, and LCRA would keep the
2 surcharge to cover LCRA's costs of administration.

3 This is not an abuse of monopoly power in any way. This is simply an
4 example of the WTCPUA collecting contractual costs pursuant to the TCMUD 12
5 Agreement. The administrative charge being collected by the WTCPUA will not be
6 kept by the WTCPUA, but will be transferred to the LCRA as compensation for its
7 services in administering the remaining wholesale services agreements of Deer Creek
8 Water Company and Lazy Nine MUD No. 1A.

9 **Q. PLEASE SUMMARIZE YOUR CONCLUSIONS WITH RESPECT TO**
10 **TCMUD 12 WITNESS ZARNIKAU'S ALLEGATIONS OF ABUSE OF**
11 **MONOPOLY POWER ON THE PART OF THE WTCPUA.**

12 A. Even if the PUC concludes that the WTCPUA is a monopoly, which I do not support,
13 the WTCPUA did not abuse any such monopoly power with respect to the standard of
14 P.U.C. SUBST. R. 24.133(a)(3)(A), Determination of Public Interest. In my opinion,
15 the WTCPUA acted within its rights and responsibilities according to the TCMUD 12
16 Agreement assumed from the LCRA, which originally had been negotiated between
17 the LCRA and TCMUD 12.

18 **Q. DOES THIS COMPLETE YOUR TESTIMONY?**

19 A. Yes.

RESUME OF RICHARD A. BAUDINO

EDUCATION

New Mexico State University, M.A.
Major in Economics
Minor in Statistics

New Mexico State University, B.A.
Economics
English

Thirty-two years of experience in utility ratemaking and the application of principles of economics to the regulation of electric, gas, and water utilities. Broad based experience in revenue requirement analysis, cost of capital, rate of return, cost and revenue allocation, and rate design.

REGULATORY TESTIMONY

Preparation and presentation of expert testimony in the areas of:

Cost of Capital for Electric, Gas and Water Companies
Electric, Gas, and Water Utility Cost Allocation and Rate Design
Revenue Requirements
Gas and Electric Industry Restructuring and Competition
Fuel Cost Auditing
Ratemaking Treatment of Generating Plant Sale/Leasebacks

EXPERIENCE

1989 to

Present: **Kennedy and Associates: Consultant** – Responsible for consulting assignments in the area of revenue requirements, rate design, cost of capital, economic analysis of generation alternatives, electric and gas industry restructuring/competition and water utility issues.

1982 to

1989: **New Mexico Public Service Commission Staff: Utility Economist** – Responsible for preparation of analysis and expert testimony in the areas of rate of return, cost allocation, rate design, finance, phase-in of electric generating plants, and sale/leaseback transactions.

**Expert Testimony Appearances
of
Richard A. Baudino
(As of December 2014)**

Date	Case	Jurisdic.	Party	Utility	Subject
10/83	1803, 1817	NM	New Mexico Public Service Commission	Southwestern Electric Coop	Rate design
11/84	1833	NM	New Mexico Public Service Commission	El Paso Electric Co.	Service contract approval, rate design, performance standards for Palo Verde nuclear generating system
1983	1835	NM	New Mexico Public Service Commission	Public Service Co. of NM	Rate design
1984	1848	NM	New Mexico Public Service Commission	Sangre de Cristo Water Co.	Rate design.
02/85	1906	NM	New Mexico Public Service Commission	Southwestern Public Service Co.	Rate of return
09/85	1907	NM	New Mexico Public Service Commission	Jornada Water Co.	Rate of return.
11/85	1957	NM	New Mexico Public Service Commission	Southwestern Public Service Co.	Rate of return.
04/86	2009	NM	New Mexico Public Service Commission	El Paso Electric Co.	Phase-in plan, treatment of sale/leaseback expense.
06/86	2032	NM	New Mexico Public Service Commission	El Paso Electric Co.	Sale/leaseback approval.
09/86	2033	NM	New Mexico Public Service Commission	El Paso Electric Co.	Order to show cause, PVNGS audit.
02/87	2074	NM	New Mexico Public Service Commission	El Paso Electric Co.	Diversification.
05/87	2089	NM	New Mexico Public Service Commission	El Paso Electric Co.	Fuel factor adjustment.
08/87	2092	NM	New Mexico Public Service Commission	El Paso Electric Co.	Rate design.
10/87	2146	NM	New Mexico Public Service Commission	Public Service Co. of New Mexico	Financial effects of restructuring, reorganization.
07/88	2162	NM	New Mexico Public Service Commission	El Paso Electric Co.	Revenue requirements, rate design, rate of return
01/89	2194	NM	New Mexico Public Service Commission	Plains Electric G&T Cooperative	Economic development
01/89	2253	NM	New Mexico Public Service Commission	Plains Electric G&T Cooperative	Financing.
08/89	2259	NM	New Mexico Public Service Commission	Homestead Water Co.	Rate of return, rate design
10/89	2262	NM	New Mexico Public Service Commission	Public Service Co. of New Mexico	Rate of return.
09/89	2269	NM	New Mexico Public Service Commission	Ruidoso Natural Gas Co.	Rate of return, expense from affiliated interest
12/89	89-208-TF	AR	Arkansas Electric Energy Consumers	Arkansas Power & Light Co.	Rider M-33
01/90	U-17282	LA	Louisiana Public Service Commission	Gulf States Utilities	Cost of equity
09/90	90-158	KY	Kentucky Industrial Utility Consumers	Louisville Gas & Electric Co.	Cost of equity
09/90	90-004-U	AR	Northwest Arkansas Gas Consumers	Arkansas Western Gas Co.	Cost of equity, transportation rate
12/90	U-17282 Phase IV	LA	Louisiana Public Service Commission	Gulf States Utilities	Cost of equity.
04/91	91-037-U	AR	Northwest Arkansas Gas Consumers	Arkansas Western Gas Co.	Transportation rates

**Expert Testimony Appearances
of
Richard A. Baudino
(As of December 2014)**

Date	Case	Jurisdic.	Party	Utility	Subject
11/95	I-940032	PA	Industrial Energy Consumers of Pennsylvania	State-wide all utilities	Investigation into Electric Power Competition
05/96	96-030-U	AR	Northwest Arkansas Gas Consumers	Arkansas Western Gas Co.	Revenue requirements, rate of return and cost of service
07/96	8725	MD	Maryland Industrial Group	Baltimore Gas & Electric Co., Potomac Electric Power Co. and Constellation Energy Corp	Return on equity.
07/96	U-21496	LA	Louisiana Public Service Commission	Central Louisiana Electric Co	Return on equity, rate of return.
09/96	U-22092	LA	Louisiana Public Service Commission	Entergy Gulf States, Inc	Return on equity.
01/97	RP96-199-000	FERC	The Industrial Gas Users Conference	Mississippi River Transmission Corp	Revenue requirements, rate of return and cost of service.
03/97	96-420-U	AR	West Central Arkansas Gas Corp.	Arkansas Oklahoma Gas Corp.	Revenue requirements, rate of return, cost of service and rate design
07/97	U-11220	MI	Association of Business Advocating Tariff Equity	Michigan Gas Co. and Southeastern Michigan Gas Co.	Transportation Balancing Provisions
07/97	R-00973944	PA	Pennsylvania American Water Large Users Group	Pennsylvania American Water Co.	Rate of return, cost of service, revenue requirements.
03/98	8390-U	GA	Georgia Natural Gas Group and the Georgia Textile Manufacturers Assoc.	Atlanta Gas Light	Rate of return, restructuring issues, unbundling, rate design issues.
07/98	R-00984280	PA	PG Energy, Inc. Intervenor	PGE Industrial	Cost allocation.
08/98	U-17735	LA	Louisiana Public Service Commission	Cajun Electric Power Cooperative	Revenue requirements.
10/98	97-596	ME	Maine Office of the Public Advocate	Bangor Hydro- Electric Co.	Return on equity, rate of return.
10/98	U-23327	LA	Louisiana Public Service Commission	SWEPSCO, CSW, and AEP	Analysis of proposed merger.
12/98	98-577	ME	Maine Office of the Public Advocate	Maine Public Service Co	Return on equity, rate of return.
12/98	U-23358	LA	Louisiana Public Service Commission	Entergy Gulf States, Inc.	Return on equity, rate of return
03/99	98-426	KY	Kentucky Industrial Utility Customers, Inc.	Louisville Gas and Electric Co.	Return on equity.
03/99	99-082	KY	Kentucky Industrial Utility Customers, Inc.	Kentucky Utilities Co.	Return on equity.
04/99	R-984554	PA	T. W. Phillips Users Group	T. W. Phillips Gas and Oil Co.	Allocation of purchased gas costs
06/99	R-0099462	PA	Columbia Industrial Intervenor	Columbia Gas of Pennsylvania	Balancing charges.
10/99	U-24182	LA	Louisiana Public Service Commission	Entergy Gulf States, Inc.	Cost of debt.
10/99	R-00994782	PA	Peoples Industrial Intervenor	Peoples Natural Gas Co.	Restructuring issues.
10/99	R-00994781	PA	Columbia Industrial Intervenor	Columbia Gas of Pennsylvania	Restructuring, balancing charges, rate flexing, alternate fuel
01/00	R-00994786	PA	UGI Industrial Intervenor	UGI Utilities, Inc.	Universal service costs, balancing, penalty charges, capacity assignment
01/00	8829	MD & United States	Maryland Industrial Gr.	Baltimore Gas & Electric Co	Revenue requirements, cost allocation, rate design
02/00	R-00994788	PA	Penn Fuel Transportation	PFG Gas, Inc., and North Penn Gas Co	Tariff charges, balancing provisions.
05/00	U-17735	LA	Louisiana Public Service Commission	Louisiana Electric Cooperative	Rate restructuring.

**Expert Testimony Appearances
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Date	Case	Jurisdic.	Party	Utility	Subject
08/05	9036	MD	Maryland Industrial Group	Baltimore Gas & Electric Co	Revenue requirement, cost allocation, rate design, tariff issues
01/06	2005-0034	KY	Kentucky Industrial Utility Customers, Inc.	Kentucky Power Co.	Return on equity
03/06	05-1278-E-PC-PW-42T	WV	West Virginia Energy Users Group	Appalachian Power Company	Return on equity
04/06	U-25116	LA	Louisiana Public Service Commission	Entergy Louisiana, LLC	Transmission Issues
07/06	U-23327	LA	Louisiana Public Service Commission	Southwestern Electric Power Company	Return on equity, service quality
08/06	ER-2006-0314	MO	Missouri Office of the Public Counsel	Kansas City Power & Light Co.	Return on equity, weighted cost of capital
08/06	06S-234EG	CO	CF&I Steel, L.P. & Climax Molybdenum	Public Service Company of Colorado	Return on equity, weighted cost of capital
01/07	06-0960-E-42T	WV	West Virginia Energy Users Group	Monongahela Power, Potomac Edison	Return on equity
01/07	43112	AK	AK Steel, Inc.	Vectren South, Inc.	Cost allocation, rate design
05/07	2006-661	ME	Maine Office of the Public Advocate	Bangor Hydro-Electric	Return on equity, weighted cost of capital.
09/07	07-07-01	CT	Connecticut Industrial Energy Consumers	Connecticut Light & Power	Return on equity, weighted cost of capital
10/07	05-UR-103	WI	Wisconsin Industrial Energy Group, Inc.	Wisconsin Electric Power Co.	Return on equity
11/07	29797	LA	Louisiana Public Service Commission	Cleco Power, LLC and Southwestern Electric Power	Lignite Pricing, support of settlement
01/08	07-551-EL-AIR	OH	Ohio Energy Group	Ohio Edison, Cleveland Electric, Toledo Edison	Return on equity
03/08	07-0585, 07-0585, 07-0587, 07-0588, 07-0589, 07-0590, (consol.)	IL	The Commercial Group	Ameren	Cost allocation, rate design
04/08	07-0566	IL	The Commercial Group	Commonwealth Edison	Cost allocation, rate design
06/08	R-2008-2011621	PA	Columbia Industrial Intervenor	Columbia Gas of PA	Cost and revenue allocation, tariff issues
07/08	R-2008-2028394	PA	Philadelphia Area Industrial Energy Users Group	PECO Energy	Cost and revenue allocation, tariff issues
07/08	R-2008-2039634	PA	PPL Gas Large Users Group	PPL Gas	Retainage, LUFG Pct.
08/08	6680-UR-116	WI	Wisconsin Industrial Energy Group	Wisconsin P&L	Cost of equity
08/08	6690-UR-119	WI	Wisconsin Industrial Energy Group	Wisconsin PS	Cost of equity
09/08	ER-2008-0318	MO	The Commercial Group	AmerenUE	Cost and revenue allocation
10/08	R-2008-2029325	PA	U.S. Steel and Univ. of Pittsburgh Med. Center	Equitable Gas Co.	Cost and revenue allocation
10/08	08-G-0609	NY	Multiple Intervenor	Niagara Mohawk Power	Cost and revenue allocation
12/08	27800-U	GA	Georgia Public Service Commission	Georgia Power Company	CWIP/AFUDC issues, review financial projections
03/09	ER08-1056	FERC	Louisiana Public Service Commission	Entergy Services, Inc	Capital structure
04/09	E002/GR-08-1065	MN	The Commercial Group	Northern States Power	Cost and revenue allocation and rate design
05/09	08-0532	IL	The Commercial Group	Commonwealth Edison	Cost and revenue allocation

**Expert Testimony Appearances
of
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(As of December 2014)**

Date	Case	Jurisdct.	Party	Utility	Subject
09/11	11-G-0280	NY	Multiple Intervenors	Corning Natural Gas Co	Cost and revenue allocation
10/11	4220-UR-117	WI	Wisconsin Industrial Energy Group	Northern States Power	Cost and revenue allocation, rate design
02/12	11AL-947E	CO	Climax Molybdenum, CF&I Steel	Public Service Company of Colorado	Return on equity, weighted cost of capital
07/12	120015-EI	FL	South Florida Hospitals and Health Care Association	Florida Power and Light Co	Return on equity, weighted cost of capital
07/12	12-0613-E-PC	WV	West Virginia Energy Users Group	American Electric Power/APCo	Special rate proposal for Century Aluminum
07/12	R-2012-2290597	PA	PP&L Industrial Customer Alliance	PPL Electric Utilities Corp	Cost allocation
09/12	05-UR-106	WI	Wisconsin Industrial Energy Group	Wisconsin Electric Power Co.	Class cost of service, cost and revenue allocation, rate design
09/12	2012-00221	KY	Kentucky Industrial Utility Consumers	Louisville Gas & Electric, Kentucky Utilities	Return on equity
10/12	9299	MD	Maryland Energy Group	Baltimore Gas & Electric	Cost and revenue allocation, rate design, cost of equity, weighted cost of capital
10/12	4220-UR-118	WI	Wisconsin Industrial Energy Group	Northern States Power Company	Class cost of service, cost and revenue allocation, rate design
10/12	473-13-0199	TX	Steering Committee of Cities Served by Oncor	Cross Texas Transmission, LLC	Return on equity, capital structure
01/13	R-2012-2321748 et al.	PA	Columbia Industrial Intervenors	Columbia Gas of Pennsylvania	Cost and revenue allocation
02/13	12AL-1052E	CO	Cripple Creek & Victor Gold Mining, Holcim (US) Inc.	Black Hills/Colorado Electric Utility Company	Cost and revenue allocations
06/13	8009	VT	IBM Corporation	Vermont Gas Systems	Cost and revenue allocation, rate design
07/13	130040-EI	FL	WCF Hospital Utility Alliance	Tampa Electric Co	Return on equity, rate of return
08/13	9326	MD	Maryland Energy Group	Baltimore Gas and Electric	Cost and revenue allocation, rate design, special rider
08/13	P-2012-2325034	PA	PP&L Industrial Customer Alliance	PPL Electric Utilities, Corp.	Distribution System Improvement Charge
09/13	4220-UR-119	WI	Wisconsin Industrial Energy Group	Northern States Power Co.	Class cost of service, cost and revenue allocation, rate design
11/13	13-1325-E-PC	WV	West Virginia Energy Users Group	American Electric Power/APCo	Special rate proposal of Felman Production, LLC
06/14	R-2014-2406274	PA	Columbia Industrial Intervenors	Columbia Gas of Pennsylvania	Cost and revenue allocation, rate design
08/14	05-UR-107	WI	Wisconsin Industrial Energy Group	Wisconsin Electric Power Co.	Cost and revenue allocation, rate design
10/14	ER13-1508 et al	FERC	Louisiana Public Service Commission	Entergy Services, Inc	Return on equity
11/14	14AL-0660E	CO	Climax Molybdenum Co. and CFI Steel, LP	Public Service Co. of Colorado	Return on equity, weighted cost of capital
11/14	R-2014-2428742	PA	AK Steel	West Penn Power Company	Cost and revenue allocation

McCONNELL BRUE FLYNN

microeconomics

QUICK REVIEW 13.1

- Monopolistic competition involves a relatively large number of firms operating in a noncollusive way and producing differentiated products with easy industry entry and exit.
- In the short run, a monopolistic competitor will maximize profit or minimize loss by producing that output at which marginal revenue equals marginal cost.
- In the long run, easy entry and exit of firms cause monopolistic competitors to earn only a normal profit.
- A monopolistic competitor's long-run equilibrium output is such that price exceeds the minimum average total cost (implying that consumers do not get the product at the lowest price attainable) and price exceeds marginal cost (indicating that resources are underallocated to the product).
- The efficiency loss (or deadweight loss) associated with monopolistic competition is greatly muted by the benefits consumers receive from product variety.

Oligopoly

LO13.5 Describe the characteristics of oligopoly.

In terms of competitiveness, the spectrum of market structures reaches from pure competition, to monopolistic competition, to oligopoly, to pure monopoly (review Table 10.1). We now direct our attention to **oligopoly**, a market dominated by a few large producers of a homogeneous or differentiated product. Because of their “fewness,” oligopolists have considerable control over their prices, but each must consider the possible reaction of rivals to its own pricing, output, and advertising decisions.

A Few Large Producers

The phrase “a few large producers” is necessarily vague because the market model of oligopoly covers much ground, ranging between pure monopoly, on the one hand, and monopolistic competition, on the other. Oligopoly encompasses the U.S. aluminum industry, in which three huge firms dominate an entire national market, and the situation in which four or five much smaller auto-parts stores enjoy roughly equal shares of the market in a medium-size town. Generally, however, when you hear a term such as “Big Three,” “Big Four,” or “Big Six,” you can be sure it refers to an oligopolistic industry.

Homogeneous or Differentiated Products

An oligopoly may be either a **homogeneous oligopoly** or a **differentiated oligopoly**, depending on whether the

firms in the oligopoly produce standardized (homogeneous) or differentiated products. Many industrial products (steel, zinc, copper, aluminum, lead, cement, industrial alcohol) are virtually standardized products that are produced in oligopolies. Alternatively, many consumer goods industries (automobiles, tires, household appliances, electronics equipment, breakfast cereals, cigarettes, and many sporting goods) are differentiated oligopolies. These differentiated oligopolies typically engage in considerable nonprice competition supported by heavy advertising.

Control over Price, but Mutual Interdependence

Because firms are few in oligopolistic industries, each firm is a “price maker”; like the monopolist, it can set its price and output levels to maximize its profit. But unlike the monopolist, which has no rivals, the oligopolist must consider how its rivals will react to any change in its price, output, product characteristics, or advertising. Oligopoly is thus characterized by *strategic behavior* and *mutual interdependence*. By **strategic behavior**, we simply mean self-interested behavior that takes into account the reactions of others. Firms develop and implement price, quality, location, service, and advertising strategies to “grow their business” and expand their profits. But because rivals are few, there is **mutual interdependence**: a situation in which each firm's profit depends not just on its own price and sales strategies but also on those of the other firms in its highly concentrated industry. So oligopolistic firms base their decisions on how they think their rivals will react. Example: In deciding whether to increase the price of its cosmetics, L'Oréal will try to predict the response of the other major producers, such as Clinique. Second example: In deciding on its advertising strategy, Burger King will take into consideration how McDonald's might react.

Entry Barriers

The same barriers to entry that create pure monopoly also contribute to the creation of oligopoly. Economies of scale are important entry barriers in a number of oligopolistic industries, such as the aircraft, rubber, and copper industries. In those industries, three or four firms might each have sufficient sales to achieve economies of scale, but new firms would have such a small market share that they could not do so. They would then be high-cost producers, and as such they could not survive. A closely related barrier is the large expenditure for capital—the cost

Attachment C

SOAH Docket No. 473-14-5144, Docket No. 42866

TCMUD 12's Responses to PUA's RFPs

RFP No. 1-16

Page 1 of 1

RFP NO. 1-16:

Produce all documents and correspondence between MUD 12 and third parties regarding the provision of Water Treatment Services to MUD 12.

RESPONSE:

Miguel A. Huerta, Counsel for TCMUD 12 conferred with David Klein and Georgia Crump, Counsel for the WTCPUA regarding this request. By agreement of Counsel, the phrase "Water Treatment Services" as used in this request, is defined by the entire definition of the term "Water Treatment Services" as set forth in the Instructions.

After a diligent search, TCMUD 12 has not identified any documents responsive to this request.

RFA NO. 1-42:

Admit or deny that MUD 12 received correspondence from the PUA or its representatives regarding a meeting held at 12117 Bee Cave Road, Building 3, Suite 120, Bee Cave, Texas 78738 on May 14, 2013, regarding the PUA's wholesale Water Treatment Services rates.

RESPONSE:

Admit that on May 10, 2013 a representative of MUD 12 received an email from Nelissa Heddin regarding a WTCPUA Wholesale Customer Committee Meeting to be held on May 14, 2013.

RFA NO. 1-43:

Admit or deny that one or more representatives of TCMUD 12 attended a meeting held at 12117 Bee Cave Road, Building 3, Suite 120, Bee Cave, Texas 78738 on May 14, 2013, regarding the PUA's wholesale Water Treatment Services rates.

RESPONSE:

Admit.

RFA NO. 1-44:

Admit or deny that between January 1, 2009 and March 6, 2014, officials, employees, representatives, and/or contractors of MUD 12 engaged in discussions or meetings with officials, employees, representatives, or contractors of other water providers, other than LCRA or the PUA, for a supply of treated water.

RESPONSE:

Deny. *See also* TCMUD 12 Response to PUA RFP 1-2.