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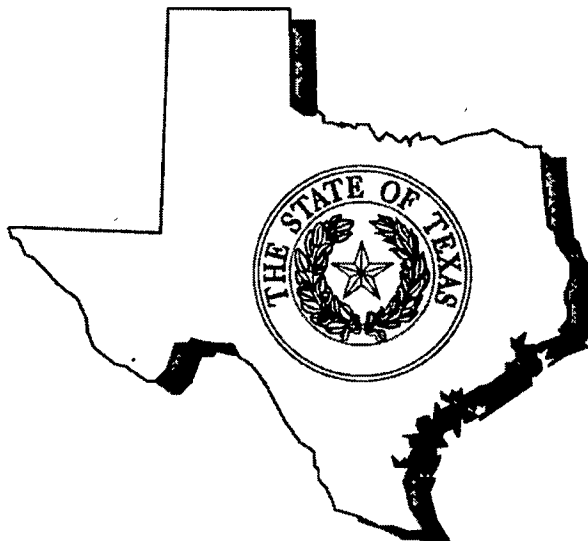
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**SOAH DOCKET NO. 473-16-1836.WS  
PUC DOCKET NO. 45231**

**RATEPAYER'S APPEAL OF THE  
DECISION BY TROPHY CLUB  
MUNICIPAL UTILITY DISTRICT  
NO. 1 TO CHANGE RATES**

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**BEFORE THE STATE OFFICE  
OF  
ADMINISTRATIVE HEARINGS**



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**DIRECT TESTIMONY OF  
ANDREW NOVAK  
WATER UTILITY DIVISION  
PUBLIC UTILITY COMMISSION OF TEXAS  
SEPTEMBER 20, 2016**

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**I. PROFESSIONAL QUALIFICATIONS**

**Q. Please state your name and business address for the record.**

A. Andrew C. Novak, Public Utility Commission of Texas, 1701 N. Congress Avenue, Austin, Texas.

**Q. Please provide a brief educational and professional background**

A. I am currently employed by the Public Utility Commission of Texas (PUC or Commission). I have been employed by the Commission since October 1, 2015 as a Financial Analyst. Prior to my employment with the Commission, I was employed by WHN Consulting from May 2015 to September 2015. I hold a Bachelor of Business Administration degree with a major in Finance from the University of Houston.

**Q. Please describe your current job responsibilities at the Commission.**

A. My responsibilities include reviewing and processing contested and uncontested rate change applications; sale, transfer, and merger applications (STMs); applications to obtain or amend a Certificate of Convenience and Necessity (CCNs); formal complaints and rate appeals filed with the PUC. For contested applications, my responsibilities include testifying as an expert witness on accounting and financial matters in rate cases and appeals, financial and managerial aspects of CCNs and STMs, and participating in the overall examination, review, and analysis of such applications.

**Q. Have you submitted testimony for the Commission before?**

A. Yes. A copy of all my previous testimonies is provided in Exhibit AN-1.

**II. PURPOSE & SCOPE OF TESTIMONY**

**Q. Please explain your role in this case.**

A. My role in this case is to conduct a financial review of the Trophy Club Municipal Utility District No. 1's (Trophy Club) records and information used by Trophy Club's board of directors to institute the rate change subject to this appeal. The purpose of my testimony is to present Staff's recommendation as to the overall cost of service or revenue requirement for the test period used by Trophy Club to set the rates which are the subject of this proceeding.

**Q. Have you performed an examination and review of the rate information, budget, discovery documents, direct testimonies and all supporting information filed by Trophy Club and the Intervenors?**

A. Yes, I have. I reviewed the cost of service documents initially provided by Trophy Club, in addition to Mr. Chris Ekrut's testimony on behalf of Trophy Club, and the direct testimony of Mr. William Rose, one of the Intervenors.

**III. METHODOLOGY**

**Q. Please describe the methodology Trophy Club used for determining the cost of service for water.**

A. There are two methodologies used in the retail water and sewer industries to determine the cost of service. The two methodologies are referred to as the "cash needs" method or the "utility method." Trophy Club's cost of service was determined using the cash needs method. As stated in the publication titled "Principles of Water Rates, Fees, and Charges:

1        *Manual of Water Supply Practices M1* " by the American Water Works Association (AWWA  
2        *M1 Manual*), "the objective of the cash needs approach for developing a cost of service is  
3        to provide revenues sufficient to recover total cash requirements for a given time period."  
4        The AWWA M1 Manual also states that the cash needs approach is appropriately used by  
5        government-owned utilities. Investor owned utilities (IOUs) normally use the utility  
6        method because of the profit motive, and the method's focus on return on investment.  
7        Municipalities and districts, like Trophy Club, which typically operate in a not-for-profit  
8        economy; therefore, they typically use the cash needs method because municipalities and  
9        districts focus on paying their cash expenses and debt service, which is normally used to  
10       pay for long term assets such as plant and equipment. The focus on debt service upholds a  
11       municipality's and district's ability to obtain debt and issue bonds for future required  
12       improvements. The cash needs method provides confidence that cash will be available to  
13       provide debt payments and preserve the financial integrity of the retail public utility.  
14       Under the cash needs method, the cost of service includes the following: allowable  
15       operating and maintenance expenses; reasonable and prudently incurred debt service costs;  
16       recurring capital improvements, and replacements; and a reasonable cash reserve account  
17       (or debt service coverage to build a reserve account) up to 50% of annual allowable debt  
18       payments. For a larger municipality or district, bond covenants will define debt service  
19       coverage requirements. Under the cash needs method, revenues must be adequate to cover  
20       all cash needs, including debt obligations as they become due.

21       **Q.     What test period is your review the cost of service based on?**

22       **A.     Fiscal Year (FY) 2015-2016.**

1     **Q.     Why did you use this test period?**

2     A.     I used this test period because Trophy Club's adopted operating budget was for FY 2015-  
3             2016. This operating budget represented the most current cash needs information available  
4             at the time Trophy Club made the decision to increase its rates. Furthermore, this is the  
5             period for which rates are being set. Districts like Trophy Club typically use budgeted  
6             information based on historical experience to set rates for future periods. The budgeting  
7             process typically allows for the goals of the district for its citizens to be met by setting rates  
8             to recover the budgeted expenditures. The budget has more relevance than historical data  
9             because of the requirement to meet the goals of the citizens expressed through the elected  
10            board of directors. Basing a future rate on an historical test year may not allow these goals  
11            to be met. Furthermore, a district should have no profit motive, and therefore, a carefully  
12            prepared budget should properly reflect the district's goals and afford the district the ability  
13            to financially meet those goals.

14    **Q.     Please explain the process you used to review Trophy Club's records to determine the**  
15       **cost of service to provide retail water service.**

16    A.     I requested and reviewed the records that Trophy Club had available at the time it made  
17             the decision to change its water and/or sewer utility rates. Pursuant to TWC § 13.043(e),  
18             "The Commission shall hear the appeal de novo and shall fix in its final order the rates the  
19             governing body should have fixed in the action from which the appeal was taken." P.U.C.  
20             Furthermore, 16 TAC § 24.41(e) (5) states that the Commission may, "consider only the  
21             information that was available to the governing body at the time the governing body made  
22             its decision and evidence of reasonable expenses incurred in the appeal proceedings." I use

1 the information provided by Trophy Club to determine the cost of service for providing  
2 water and sewer service. For a district, this normally consists of historical financial  
3 information and a budget.  
4

5 **IV. SUMMARY OF RECOMMENDATIONS**

6 **Q. Based upon the information provided through the parties' testimony and responses**  
7 **to requests for information, are you able to determine the cost of service for Trophy**  
8 **Club's water service?**

9 A. Yes. Based upon examination of Trophy Club's adopted budget, I am recommending a  
10 Revenue Requirement.

11 **Q. What is your recommendation regarding Trophy Club's revenue requirement?**

12 A. I agree with the revenue requirement Trophy Club budgeted, which was in the amount of  
13 \$7,505,018.

14 **Q. What is the basis for your recommendations?**

15 A. After careful review of Trophy Club's proposed budget, as well as the previous fiscal years  
16 budgets provided by Trophy Club, and documentation provided by Trophy Club which  
17 details the expenses the current budget was set off, Staff is recommending no adjustments  
18 be made to the revenue requirement.

19 **Q. What are the components and their amounts that make up the revenue requirement?**

20 A. The components and cost that are included in Trophy Club's revenue requirement are listed  
21 in the table below:

Water	\$4,522,914
Wastewater	\$1,336,207
Board of directors	\$23,522
Admin Overhead	\$1,298,508
Non-Departmental	\$517,797
Debt Service	\$1,602,777
Cost of Service	\$9,301,725
Non Rate Revenues	\$1,796,707
Revenue Requirement	\$7,505,018

1

2 **Q. Are the expenses associated with providing service to the customers of the Trophy**  
3 **Club Public Improvement District (PID) included in the cost of service?**

4 **A.** Yes. As stated in pg. 21 of Chris Ekrut's testimony, "for purposes of designing rates, there  
5 is no difference between In-District Customers and PID Customers."

6 **Q. When you reviewed William Rose's testimony, did you see anything related to the**  
7 **revenue requirement?**

8 **A.** Yes.

9 **Q. Did Mr. Rose oppose the revenue requirement as a whole?**

10 **A.** No.

11

12

#### V. RATE CASE EXPENSES

13 **Q. Did Trophy Club incur rate case expenses in this proceeding?**

14 **A.** Yes.

15 **Q. From what parties did Trophy Club incur expenses and in what amounts?**

16 **A.** As of the most recent filing, Trophy Club has incurred; \$33,862.50 from Newgen Strategies

1           & Solutions, \$1,000 from CP&Y, \$45,331.57 from the Carlton Law Firm, and \$11,154.74  
2           from the Liston Law Firm. This makes the total amount of rate case expenses, as of the  
3           most recent filing, \$91,448.81.

4       **Q.     Did Trophy Club budget for rate case expenses in the cost of service?**

5       A.     Yes they did, as evidenced by Trophy Club's response to Staff's RFI 4-1, which is provided  
6           in my testimony as attachment AN-1.

7       **Q.     What amount of rate case expenses do you recommend Trophy Club recover.**

8       A.     I recommend Trophy Club be allowed to recover no rate case expenses other than what is  
9           already included in the cost of service, unless final reasonable and necessary rate case  
10          expenses reviewed in this case end up exceeding \$150,000. If this occurs, I recommend the  
11          difference between the actual reasonable, necessary rate case expenses and the \$150,000  
12          budgeted for rate case expenses, be recovered through a surcharge to all of Trophy Club's  
13          customers.

14      **Q.     Please explain your reasoning.**

15      A.     Since Trophy Club budgeted rate case expenses for this proceeding and the amount of rate  
16          case expenses has not exceeded the amount budgeted, which is in the amount of \$150,000,  
17          there is no justification for allowing the recovery of rate case expenses for this proceeding,  
18          at this time. The rates were set using the budget, and rate case expense was included in the  
19          budget. Therefore, if an additional surcharge is allowed for rate case expense, the expense  
20          would be collected twice.

1

**VI. CONCLUSION**

2

**Q. Does this conclude your direct testimony at this point in the proceeding?**

3

**A. Yes. However, I reserve the right to supplement or adjust this testimony during the course of this proceeding as new facts or evidence becomes available.**

4

# Attachments

**REQUEST FOR INFORMATION  
QUESTION NOS. STAFF 4-1 THROUGH 4-26**

**Staff - 4-1.** Please admit or deny: Trophy Club MUD's legal expenses were budgeted to include an amount for this rate appeal proceeding. If the response is an admit, please provide the total amount of rate case expenses that were budgeted.

**Response:** Admit. \$150,000.

**Prepared by:** Jennifer McKnight

**Sponsored by:** Jennifer McKnight

**Staff - 4-2.** Please provide receipts and/or invoices justifying the amount of travel expenses budgeted for the board of directors. If this information has been provided previously, please identify the location of this information in the record.

**Objection:** TCMUD1 objects to this request as overbroad because it is not limited to the relevant test year and, without a time limitation, is irrelevant under the standard of review for this proceeding. TCMUD1 also objects to this request as it seeks information not reasonably available to TCMUD1 at the time TCMUD1 made its decision regarding the rates that are the subject of this appeal. Texas Water Code §13.043(e) limits the Commission's review to "only the information that was available to the governing body at the time the governing body made its decision and evidence of reasonable expenses incurred by the retail public utility in the appeal proceedings." Because the request is not limited in time, "receipts and/or invoices justifying the amount of travel expenses budgeted for the board of directors" includes information that was not available to TCMUD1 "at the time [it] made its decision...."

**Response:** Without waiving and notwithstanding the foregoing objections, responsive documents related to the test year will be produced.