

Control Number: 45283



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State Office of Administrative Hearings



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# Lesli G. Ginn Chief Administrative Law Judge

January 13, 2017

**TO:** Stephen Journeay, Director Commission Advising and Docket Management William B. Travis State Office Building 1701 N. Congress, 7th Floor

Austin, TX 78701

# RE: SOAH Docket No. 473-16-1834.WS PUC Docket No. 45283

Enclosed is the Proposal for Decision (PFD) in the above-referenced case. By copy of this letter, the parties to this proceeding are being served with the PFD.

Please place this case on an open meeting agenda for the Commissioners' consideration. Please notify me and the parties of the open meeting date, as well as the deadlines for filing exceptions to the PFD, replies to the exceptions, and requests for oral argument.

Sincerely,

Holly Vandroun

Holly Vandrovec Administrative Law Judge

Enclosure xc: All Parties of Record

### SOAH DOCKET NO. 473-16-1834.WS PUC DOCKET NO. 45283

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RATEPAYERS' APPEAL OF THE DECISION BY NORTH SAN SABA WATER SUPPLY CORPORATION TO CHANGE RATES BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS

## **PROPOSAL FOR DECISION**

Several ratepayers of North San Saba Water Supply Corporation (San Saba) appeal a water rate increase set by San Saba's Board of Directors (Board). Based on the evidentiary record, the Administrative Law Judge (ALJ) recommends that the Public Utility Commission of Texas (PUC or Commission) deny the ratepayers' appeal and approve new water rates other than those proposed by San Saba, order San Saba to refund rates collected in excess of the rates ordered by the Commission, and allow San Saba to recover its rate case expenses as a surcharge.

## I. JURISDICTION, NOTICE, BACKGROUND, AND PROCEDURAL HISTORY

The Commission has jurisdiction and authority pursuant to Texas Water Code §§ 13.001 and 13.043. On January 11, 2016, the Commission referred this case to the State Office of Administrative Hearings (SOAH). SOAH has jurisdiction over matters relating to the conduct of the hearing in this proceeding pursuant to Texas Government Code § 2003.049. Notice was not contested and is addressed only in the proposed findings of fact and conclusions of law.

On July 17, 2015, the Board notified the ratepayers of San Saba that new rates would go into effect on September 15, 2015.<sup>1</sup> On October 26, 2016, within 90 days after the effective date of the new rates, thirty-six ratepayers filed a petition with the Commission to appeal the adopted rates. San Saba serves 293 connections. Therefore, the 10% minimum threshold of ratepayers

<sup>&</sup>lt;sup>1</sup> Petition of Ratepayers to Appeal Rates Established by the Board of North San Saba, filed at the PUC on October 26, 2015.

		OL	D	_	NE	W
Monthly Base Rate (regardless	\$70.00	\$70.00 – Residential		\$82.00	-Re	sidential
of meter size)	\$200.00	) – Co	mmercial	\$400.00 - Commercia		ommercial
First 4,000 gallons of water	\$2.70	per	thousand	\$2.70	per	thousand
	gallons			gallons		
4,001 to 8,000 gallons of water	\$3.38	per	thousand	\$5.07	per	thousand
	gallons			gallons		
8,001 to 20,000 gallons of water	\$4.05	per	thousand	\$7.09	per	thousand
	gallons			gallons		۰.
20,001 gallons or more of water	\$4.73	per	thousand	\$9.46	per	thousand
-	gallons			gallons	1	

Staff recommends the following rates:

Monthly I	Base Rate	Gallonage Rates Per Gallons	1,000
Meter Size	Rate	Gallonage Ra	ite
5/8"	\$78.88	0-4,000 \$2	.70
1"	\$118.32	4,001-8,000 \$4	.00
1 1/2"	\$197.20	8,001-20,000 \$5	.00
2"	\$394.40	20,001+ \$6	.00
3"	\$631.04	,	

The ALJ recommends the following rates:

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Monthly I	Base Rate	Gallonage Rate Gallor	s Per 1,000 1s
Meter Size	Rate	Gallonage	Rate
5/8"	\$83.94	0-4,000	\$2.70
1"	\$125.91	4,001-8,000	\$3.93
1 1/2"	\$209.85	8,001-20,000	\$4.99
2"	\$419.70	20,001+	\$5.99
3"	\$671.52		

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<sup>2</sup> Tex. Water Code § 13.043(c); 16 Tex. Admin. Code § 24.41(b).

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On February 19, 2016, ALJ Holly Vandrovec convened a prehearing conference. Barbara Horn was admitted as a ratepayer, and San Saba and PUC staff (Staff) were also admitted as parties. Subsequently, the hearing on the merits was set for June 20-21, 2016. The case was abated by request of the parties, who engaged in mediation on July 8, 2016. Mediation was unsuccessful, and the hearing on the merits convened on October 14, 2016. The record closed on November 18, 2016, with the filing of briefs.

#### **II. LEGAL STANDARD**

The Texas Water Code allows ratepayers to appeal rates established by a water supply corporation.<sup>3</sup> An appeal "must be initiated by filing a petition for review with the [Commission] and the entity providing service within 90 days after the effective date."<sup>4</sup> "The petition must be signed by the lesser of 10,000 or 10 percent of those ratepayers whose rates have been changed and who are eligible to appeal."<sup>5</sup>

The Commission "shall hear the appeal de novo and shall fix in its final order the rates the governing body should have fixed in the action from which the appeal was taken."<sup>6</sup> Additionally, the Commission "may establish the effective date for the [Commission's] rates at the original effective date as proposed by the service provider, may order refunds or allow a surcharge to recover lost revenues, and may allow recovery of reasonable expenses incurred by the retail public utility in the appeal proceedings."<sup>7</sup> In establishing the rates, the Commission may consider "only the information that was available to the governing body at the time the governing body made its decision and evidence of reasonable expenses incurred by the retail public utility in the appeal proceedings."<sup>8</sup> The Commission shall ensure that every rate is "just

<sup>&</sup>lt;sup>3</sup> Tex. Water Code § 13.043(b)(1).

<sup>&</sup>lt;sup>4</sup> Tex. Water Code § 13.043(c); 16 Tex. Admin. Code § 24.41(b).

<sup>&</sup>lt;sup>5</sup> Tex. Water Code § 13.043(c); 16 Tex. Admin. Code § 24.41(b).

<sup>&</sup>lt;sup>6</sup> Tex. Water Code § 13.043(e).

<sup>&</sup>lt;sup>7</sup> Tex. Water Code § 13.043(e).

<sup>&</sup>lt;sup>8</sup> Tex. Water Code § 13.043(e).

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and reasonable," not "unreasonably preferential, prejudicial, or discriminatory," but "sufficient; equitable, and consistent in application to each class of customers;" and the Commission shall use a methodology that preserves the financial integrity of the retail public utility."<sup>9</sup>

The retail public utility has the burden of proof to show that its rate is just and reasonable.<sup>10</sup>

#### **III. EVIDENCE**

### A. Testimony of Ratepayer Barbara Horn

The direct testimony of ratepayer Barbara Horn was admitted into evidence; however, San Saba's objection to "Topic Two"<sup>11</sup> of Ms. Horn's testimony was sustained in SOAH Order No. 3. Ms. Horn testified that that she does not believe the rate increase by San Saba is just and reasonable. She states that water purchased by San Saba from the City of San Saba (City) costs only \$1.93 per 1,000 gallons; however, she is charged \$121.80 per month under the new rates for 1,000 gallons of water. She also argues that those using the most water are paying the least amount per gallon for that water. She describes the rate structure as a declining rate structure.<sup>12</sup>

Ms. Horn also points out several errors in a spreadsheet showing meter readings for San Saba's wells and casts doubt on the competency of the operator of San Saba's system, who Ms. Horn opines is over-paid. She points out that the operator was hired in April of 2010 at a compensation rate of \$49,500 per year. The operator is now paid \$90,000 per year. Ms. Horn points to the compensation for a foreman of a nearby water supply corporation who is paid

<sup>&</sup>lt;sup>9</sup> Tex. Water Code § 13.043(j); 16 Tex. Admin. Code § 24.41(i).

<sup>&</sup>lt;sup>10</sup> 16 Tex. Admin. Code § 24.12.

<sup>&</sup>lt;sup>11</sup> Topic Two involved an allegation of an error made by the Texas Commission on Environmental Quality during the administrative proceeding involving the rate appeal filed against San Saba on September 18, 2008.

<sup>&</sup>lt;sup>12</sup> The ALJ notes that the rate structure utilized by San Saba is actually an inclining rate structure where the water per gallon becomes more expensive as usage increases.

\$29,333 per year. Ms. Horn states that the foreman of the other water supply corporation leads a crew of seven workers, four of whom are compensated at a rate of \$21,168 per year each.

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Ms. Horn also casts doubt on San Saba's Cash Flow Projection and studies performed by ' the operator to determine leak rates.

## B. San Saba's Evidence

### 1. Testimony of Roger Whatley

Mr. Whatley's direct testimony (San Saba Exhibit 1), rebuttal testimony (San Saba Exhibits 2 and 3), and second, third, and fourth supplemental testimony (San Saba Exhibits 3-6) were admitted.

Mr. Whatley is the president of the Board and has been on the Board since March 2015. Mr. Whatley was the primary architect of the design and calculation of the new rates, which were adopted by the Board on August 11, 2015, and are the subject of this contested case. After first joining the Board, Mr. Whatley noticed that San Saba's income tended to be around \$27,000 per month, while its expenses averaged \$29,000 per month. San Saba's expenses at the time of his testimony averaged approximately \$33,000 per month. Mr. Whatley analyzed expenses, demand, customer classes, and other factors to develop a mathematical model for rates that would cover San Saba's monthly expenses, plus additional funds to cover legal fees and other non-routine expenses that arise. He used the data from January to December 2014 to develop the model, as well as information regarding income and expenses known for the first half of 2015. Mr. Whatley arrived at a revenue requirement of \$34,000 per month (\$408,000 per year).<sup>13</sup>

<sup>&</sup>lt;sup>13</sup> Mr. Whatley testified that he believes a monthly revenue requirement of 34,000 would be appropriate. San Saba Ex. 1 at 8. The monthly revenue requirement adopted by the Board for the new rates is slightly higher, at 34,032 (408,384 per year). San Saba Ex. 1 at 9.

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Mr. Whatley has several critiques of Staff's calculated revenue requirement and rates.<sup>14</sup>

These are:

- The revenue requirement fails to take into consideration known capital expenditures included in the June 25, 2015 feasibility study<sup>15</sup> received by San Saba to address infrastructure problems;
- The revenue requirement fails to take into consideration expenses related to two pending lawsuits;
- The revenue requirement fails to take into consideration known expenses related to compliance with Texas Commission on Environmental Quality (TCEQ) limits for combined radium;
- The revenue requirement fails to take into consideration known and necessary increases in water purchased from the City;<sup>16</sup>
- The allocation of fixed and variable costs for repairs and maintenance should be altered to take into consideration the fact that San Saba's system is very spread out, with many miles of pipe that require constant maintenance;
- The revenue requirement and rates fail to take into consideration a drop in demand due to increased rain brought on by El Nino (resulting in a drop in revenue); and
- Staff erred in "recasting" a 3-year loan (the Nelson Lewis Loan) as a 30-year loan resulting in San Saba not having enough revenue to pay the loan payments.

Mr. Whatley testified that he used the 2014 data and made appropriate adjustments to take the above known factors into consideration in determining the rate structure. He testified that Staff's failure to do so fails to preserve the financial integrity of San Saba because Staff's rates fail to cover San Saba's monthly expenses.

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<sup>&</sup>lt;sup>14</sup> One of the critiques was that Staff used the wrong number for the compensation of San Saba's operator. Staff agreed, fixed the error, and submitted modified exhibits shortly before the hearing.

<sup>&</sup>lt;sup>15</sup> See San Saba Ex. 8 (Testimony of Katherine Gage) at KG-2.

<sup>&</sup>lt;sup>16</sup> In order to keep combined radium levels within acceptable limits, San Saba must mix treated water purchased from the City with its own well water. Radium levels in its wells have been increasing, resulting in a higher need for water purchased from the City.

#### 2. Testimony of Katherine Gage

Katherine Gage's direct testimony (San Saba Exhibit'8) was admitted without objection.

Ms. Gage is on the Board and is a past president and secretary-treasurer. She testified as to the ongoing problems San Saba has had complying with TCEQ's combined radium limits and other infrastructure issues resulting from an aging system. TCEQ assessed a \$21,079 penalty on May 1, 2012, that was paid in full in September 2015. She testified that infrastructure improvements required by the TCEQ were over budget and that San Saba was in litigation with the engineering firm hired to perform the required work. Additional improvements required by TCEQ have yet to be made. A June 25, 2015 feasibility study outlines the cost to make certain improvements to meet the TCEQ requirements.

In November 2015, after the new rates went into effect, Ms. Gage met with James Smith of the Texas Rural Water Association (TRWA). Mr. Smith helped Ms. Gage by providing a "Water Revenue Requirements and Rate Design" spreadsheet that was used to calculate rates. The TRWA spreadsheet calculated an \$88.57 per month base rate.

#### **3.** Testimony of Will Broyles

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Will Broyles's direct testimony (San Saba Exhibit 7) was admitted without objection.

Mr. Broyles testified that he is compensated \$90,000 per year to act as the operator of San Saba's system. He is an independent contractor who uses his own vehicle and tools and hires and pays directly for any other labor needed to maintain the system. Mr. Broyles testified that he is essentially "on call" at all times to address leaks and other issues within the system. Mr. Broyles testified that, although the system has few connections, the system is very spread out and requires frequent leak repair. The large amount of pipe in an aging system makes it expensive to maintain and repair as compared to most other systems where the connections are closer together.

#### 4. Testimony of Richard T. Miller

Richard T. Miller's direct testimony and supplement to his direct testimony (San Saba Exhibits 9 and 10) were admitted without objection. Additionally, Mr. Miller supplemented the rate case expenses to include expenses incurred in the hearing and post-hearing briefing in an affidavit attached to San Saba's reply brief. The ALJ admits Mr. Miller's affidavit as San Saba Exhibit 11.

Mr. Miller also testified at the hearing as to the reasonable and necessary rate case expenses incurred by San Saba. He testified that he typically bills his clients at a rate of \$250 per hour, but agreed to represent San Saba at a rate of \$175 per hour. Likewise, his associate Regina Morgan typically bills at a rate of \$175 per hour, but agreed to represent San Saba at a rate of \$125 per hour. He testified that the expenses were necessary for the legal representation of San Saba in this contested case hearing and that they were reasonable. Mr. Miller's affidavit states that the rate case expenses total \$22,055.02. He attached all invoices showing the expenses, which consist of legal fees, postage, and travel.

### C. Staff's Evidence

#### 1. Testimony of Fred Bednarski, III

Mr. Bednarksi is an employee of the PUC and performed the analysis and calculations necessary to develop Staff's proposed revenue requirement. Mr. Bednarski used the cash-needs method to determine the revenue requirement. The cash-needs method is typically used by government-owned utilities and not-for-profit entities. The cash-needs method uses the following equation to determine the revenue requirement: revenue requirement = operating expenses + debt service + debt service coverage + capital expenditures. Mr. Bednarski made

adjustments to the expense account numbers included in Ms. Gage's testimony<sup>17</sup> by eliminating the following expenses: depreciation, long term debt, system depreciation, and a TCEQ penalty. Mr. Bednarski testified that depreciation is not used in the cash-needs calculation and that the long-term debt is addressed by factoring in annual debt payments and debt service coverage. Additionally, according to Mr. Bednarski, the TCEQ penalty should not be included as it is not an annual recurring expense to provide water and the utility's cash reserves and debt service coverage are sufficient to pay the penalty.

Mr. Bednarski calculated the debt service amount by including the annual loan payments for each of San Saba's loans with one exception—the Nelson Lewis Loan<sup>18</sup> was normalized as a 30-year loan instead of the actual 3-year loan period. Mr. Bednarski testified that this loan pays for capital improvements that are to have a much longer life than the 3-year loan period such that the cost of service would be overstated and the rates would not be reasonable and necessary. Mr. Bednarski also testified that it is unfair for current members to carry the burden for this expense, when the improvements will benefit customers for a 30-year period. To cover the actual amount of paying the total loan payment, Mr. Bednarski added in a 25% debt service coverage totaling \$25,763.37. This amount is also used to cover unexpected or non-recurring costs and variations in revenue caused by changing usage. After the total payment on the Nelson Lewis Loan is paid each year, Mr. Bednarski's debt service coverage results in \$5,773.66 per year to cover unexpected and non-recurring costs.

Mr. Bednarski's total calculated revenue requirement is \$378,500.53.

<sup>&</sup>lt;sup>17</sup> Mr. Bednarski testified that he used the inputs contained in the spreadsheet attached to Ms. Gage's testimony as Ex. KG-3. This exhibit was actually prepared by the Texas Rural Water Association (TRWA) using information from San Saba after the Board adopted the new rates. Although Mr. Bednarski testified that the TRWA's methodology is sound, that methodology yielded a base rate of \$88.57—far higher than the base rate recommended by either San Saba or Staff.

<sup>&</sup>lt;sup>18</sup> The Nelson Lewis Loan pays for overages for capital improvements that were incurred while the contractor (Nelson Lewis) was making improvements to San Saba's water system. San Saba must pay \$24,000 per year and the loan ends in June 2018. Once normalized for 30 years, the loan payments amount to \$4,010.29 per year.

In addition to calculating the revenue requirement, Mr. Bednarski allocated a portion of each expense as either fixed or variable. Mr. Bednarski made these allocations based on whether water usage was a cost driver for each expense. One of the disputed allocations was for repairs and maintenance, which Mr. Bednarski allocated 55% as fixed and 45% as variable.<sup>19</sup> Mr. Bednarski's total calculated amounts are \$277,329.04 for fixed costs and \$101,171.49 for variable costs.

#### <sup>\*</sup> 2. Testimony of Sean Scaff

Mr. Scaff is also an employee of the PUC. He took the revenue requirement and the fixed and variable costs calculated by Mr. Bednarski and designed a rate to recover revenue. Mr. Scaff recommended the following rates:

Monthly B	Base Rate	Gallonage Rate Gallor	s Per 1,000 1s
Meter Size •	Rate	Gallonage	Rate
5/8"	\$78.88	0-4,000	\$2.70
1"	\$118.32 <sup>,</sup>	4,001-8,000	\$4.00
1 1/2"	\$197.20	8,001-20,000	\$5.00
2"	\$394.40	20,001+	\$6.00
3"	\$631.04		,

Mr. Scaff agreed with the general conservation rate schedule, but believed that the rates calculated by San Saba generate revenue above the revenue requirement and variable costs developed by Mr. Bednarski. Mr. Scaff's rate design does not include a separate monthly charge for a commercial customer class as San Saba's does.

#### **IV. ANALYSIS AND RECOMMENDATION**

San Saba has proven a need for a rate increase in order to preserve the financial integrity of the utility; however, not at the rate San Saba proposes. San Saba's methodology for

<sup>&</sup>lt;sup>19</sup> San Saba argues that 80% should be allocated as fixed and 20% as variable.

calculating rates was not one of the most often used rate methodologies—the cash-needs method or the utility method. Rather, San Saba's methodology was ad hoc and San Saba was not able to clearly explain exactly how the rates were calculated and how the variables were addressed. San Saba did show that its cash reserves were rapidly depleting and that its monthly costs outpaced its monthly income, thereby putting the financial integrity of the utility at risk.

The ALJ agrees with Staff that the cash-needs method is the appropriate methodology to calculate the revenue requirement in this case because San Saba is a not-for-profit water supply corporation similar to a government-owned utility. However, it was clear from Mr. Bednarski's testimony that he based his calculation of the revenue requirement on inputs into an exhibit to Ms. Gage's testimony that was not prepared by San Saba, but was prepared by the TRWA after the new rates were adopted by the Board. Therefore, those are not necessarily the inputs that San Saba would have used or advocated for had it used the same spreadsheet provided by the TRWA to calculate its rates. This is clear in that the TRWA spreadsheet included an error as to the amount of contract labor paid to Mr. Broyles, which was incorrectly input as \$66,000 when it should have been \$90,000. This mistake was corrected in Mr. Bednarski's direct testimony the day before the hearing.

The ALJ agrees with the revenue requirement proposed by Mr. Bednarski and adopted by Staff, with two changes. First, the ALJ agrees with San Saba's projection that the water purchased from the City will cost \$68,418 and is a known and measurable change that is a reasonably anticipated, prudent projected expense based on figures known to San Saba at the time the rates were made.<sup>20</sup> Therefore, Staff should use \$68,418 in its revenue requirement calculation. Second, the ALJ finds that Staff's 25% debt service coverage does not allow sufficient cash reserves to cover unexpected and non-recurring costs. Until the Nelson Lewis Loan is paid off in June 2018, San Saba would only accrue \$5,773.66 per year in cash reserves under Staff's debt service coverage calculation. If San Saba were assessed another TCEQ

<sup>&</sup>lt;sup>20</sup> See Exhibit 19 to Horn Ex. 1. San Saba utilized known water purchases from the City for the first seven months of 2015 to project a total cost of water purchased from the City to be \$68,418. This was an increase over the cost of water purchased in 2014 (\$61,475), which is the cost used by Staff in its calculation.

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penalty similar to that assessed in 2012 (\$21,079), San Saba would not have the cash available to pay the fine, much less make any required infrastructure improvements. In addition, Ms. Gage's testimony states that not all of the TCEQ required infrastructure improvements have been made. This puts San Saba at risk for additional fines. Therefore, the ALJ recommends debt service coverage of 35%.

Staff's revenue requirement correctly eliminates depreciation expenses, which are improper when utilizing a cash-needs basis rate calculation. It also eliminates the long-term debt expense, which is recovered through annual debt payments and debt service coverage. Finally, it eliminates the TCEQ penalty, which is not a recurring annual debt and may be paid using San Saba's cash reserve and debt service coverage. With the change to Staff's revenue requirement accounting for the increased cost of water purchased from the City and the increased debt service coverage, the ALJ recommends that the appropriate revenue requirement is \$395,748.88.<sup>21</sup>

In addition to the change in the revenue requirement, the ALJ also agrees with San Saba that the nature of its system—relatively few connections spread out over a very large area, resulting in many miles of pipe—merits a change in the allocation of fixed and variable costs for repairs and maintenance. Mr. Bednarski could not explain why he allocated 55% of the repair and maintenance expenses to fixed and 45% to variable costs. Although Staff points to the 50-50 allocation included in the TRWA spreadsheet, again, that spreadsheet was not prepared by San Saba and was prepared after the rates were adopted by the Board. Mr. Broyles, the operator who performs the repair and maintenance to San Saba's system, testified that 80% of the costs of repair and maintenance are for pipe leaks, which are considered fixed costs because the presence of pipe in the system does not depend on the amount of water passing through the pipes.<sup>22</sup> Because Mr. Broyles is the operator who actually performs the maintenance on the system, and

<sup>&</sup>lt;sup>21</sup> See Attachment A to this PFD, a revised version of Mr. Bednarski's spreadsheet showing the ALJ's changes.

<sup>&</sup>lt;sup>22</sup> Mr. Bednarski testified that repair of pumps (as opposed to repair of pipes) would be considered a variable cost because pumps wear out depending on the amount of water pumped by the pumps. He also admitted that the San Saba system consists of highly compromised distribution lines.

Mr. Bednarski testified that he made the allocation without specific information regarding the needs of San Saba's infrastructure, the ALJ finds Mr. Broyles's testimony more persuasive. Therefore, the ALJ agrees that 80% of the expenses for repairs and maintenance should be allocated as fixed costs and 20% should be allocated as variable costs. This results in total recommended fixed costs of \$295,147.14 and total variable costs of \$100,601.74.<sup>23</sup>

For the calculation of the rates, the ALJ takes the fixed cost of \$295,147.14, divided by 293 connections, divided by 12 months, for a monthly base rate of \$83.94 per month for 5/8" meters. The ALJ utilizes the same factors as Staff to determine base rates for other meter sizes (the 5/8" rate times a factor of 1.5 for a 1" meter, 2.5 for a 1.5" meter, 5 for a 2" meter, and 8 for a 3" meter). The resulting recommended rates, which should be effective as of September 15, 2015, are as follows and are shown in the spreadsheet attached as Attachment B:

Monthly I	Base Rate	Gallonage Rates Gallon	s Per 1,000
Meter Size	Rate	Gallonáge	Rate
5/8"	\$83.94	0-4,000	\$2.70
1"	\$125.91	4,001-8,000	\$3.93
1 1/2"	\$209.85	8,001-20,000	\$4.99
2"	\$419.70	20,001+	\$5.99
3"	\$671.52		

Staff's proposed rates did not distinguish among customer classes (other than by meter size). Although San Saba's rates include a residential and a commercial customer class, San Saba presented no evidence as to how many commercial customers it has. Therefore, the ALJ does not recommend different rates for different customer classes. The parties may wish to address this issue in exceptions.

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<sup>&</sup>lt;sup>23</sup> See Attachment A.

If the Commission agrees with the rates recommended by the ALJ, San Saba must refund any rates collected in excess of those ordered by the Commission.<sup>24</sup> Because the ALJ cannot ascertain the exact amount of increased water rates collected, the ALJ recommends that the PUC order San Saba to calculate and fully account for all sums collected in excess of the rate finally ordered for each current customer or connection and to refund those rates over a period of time equal to the period such rates were charged.

The parties requested in their reply briefs that the rate case expense issue be severed into a separate docket to proceed after the Commission establishes San Saba's revenue requirement and corresponding rates. The ALJ declines to sever the rate case expense issue. The record on this matter is fully developed. The ALJ has all invoices generated by San Saba's counsel and counsel for Staff questioned Mr. Miller with respect to the expenses during the hearing. After a review of the invoices, and given the discounted attorney hourly rates charged to San Saba and the fact that Ms. Morgan's time was not charged to San Saba for participation in the mediation, the ALJ concludes that rate case expenses of \$22,055.02 are reasonable and necessary in this case. The ALJ recommends that the rate case expenses be recovered by a surcharge over a 12-month period as follows: \$22,055.02 divided by the total number of current customers, and then divided by 12.

# V. PROPOSED FINDINGS OF FACT, CONCLUSIONS OF LAW, AND PROPOSED ORDERING PARAGRAPHS

### A. Findings of Fact

- 1. On July 17, 2015, the Board of Directors (Board) of North San Saba Water Supply Corporation (San Saba) notified the ratepayers of San Saba that new water rates would go into effect on September 15, 2015. The Board met and voted to adopt the new rates on August 11, 2015.
- 2. San Saba's old rates and rates adopted on August 11, 2015 are as follows:

<sup>&</sup>lt;sup>24</sup> Although the ALJ's monthly base rate is higher than San Saba's base rate for residential customers, it is lower for commercial customers.

		OL	<b>D</b> "		NEV	N
Monthly Base Rate (regardless	\$70.00 -	- Resi	idential	\$82.00	– Res	sidential
of meter size)	\$200.00	) – Co	mmercial	\$400.0	0 - Co	ommercial
First 4,000 gallons of water	\$2.70	per	thousand	\$2.70	per	thousand
	gallons			gallons		
4,001 to 8,000 gallons of water	\$3.38	per	thousand	\$5.07	per	thousand
	gallons			gallons		
8,001 to 20,000 gallons of water	\$4.05	per	thousand	\$7.09	per	thousand
	gallons			gallons		
20,001 gallons or more of water	\$4.73	per	thousand	\$9.46	per	thousand
	gallons			gallons		

- 3. On October 26, 2016, within 90 days after the effective date of the new rates, thirty-six ratepayers, more than 10% of the affected ratepayers, timely filed a petition with the Public Utility Commission of Texas (Commission) to appeal the adopted rates.
- 4. This case was referred to the State Office of Administrative Hearings (SOAH) on January 11, 2016.
- 5. On February 19, 2016, Administrative Law Judge (ALJ) Holly Vandrovec convened a prehearing conference. Barbara Horn was admitted as a ratepayer, and San Saba and Commission staff (Staff) were also admitted as parties.
- 6. The hearing on the merits was set for June 20-21, 2016. The case was abated by request of the parties, who engaged in mediation on July 8, 2016. Mediation was unsuccessful, and the hearing on the merits convened on October 14, 2016. The record closed on November 18, 2016, with the filing of briefs.
- 7. San Saba is a water supply corporation that serves 293 connections and all residential and commercial connections utilize 5/8" meters.
- 8. To preserve its financial integrity, San Saba requires a rate increase above rates charged previous to its rate increase adopted on August 11, 2015.
- 9. The use of the cash-needs method is appropriate to calculate San Saba's revenue requirement and corresponding rates.
- 10. The revenue requirement calculated by Staff correctly eliminated depreciation expenses (not utilized in a cash-needs method rate calculation), long-term debt expense (recovered through annual debt payments and debt service coverage), and a Texas Commission on Environmental Quality penalty (which is not a recurring annual debt).
- 11. The revenue requirement calculated by Staff should have used San Saba's projection for the cost of water purchased from the City of San Saba, \$68,418, which was a known and

measurable change that was a reasonably anticipated projected expense based on figures known to San Saba at the time the Board adopted new rates.

- 12. The revenue requirement calculated by Staff should have used 35% in debt service coverage to allow San Saba sufficient cash reserves to cover unexpected and non-recurring costs.
- 13. San Saba's total revenue requirement in this proceeding is \$395,748.88.
- 14. The San Saba system is located in a rural area and includes many miles of pipe that are highly compromised and require frequent repairs. Eighty percent of repair and maintenance expenses are used to repair pipe and are fixed costs. Twenty percent of repair and maintenance expenses are variable costs. This allocation of fixed and variable costs for repair and maintenance expenses should be reflected in San Saba's rate structure.
- 15. San Saba's total fixed costs are \$295,147.14 and total variable costs are \$100,601.74.
- 16. San Saba's rates adopted on August 11, 2015, collect more than the revenue requirement of \$395,748.88.
- 17. San Saba's monthly base rate should be calculated by dividing the total fixed costs of \$295,147.14 by 293 connections, then dividing by 12 months. The resulting monthly base rate is \$83.94 per month for 5/8" meters.
- 18. Base rates for other meter sizes should be calculated by multiplying the 5/8" meter size by an appropriate factor—a factor of 1.5 for a 1" meter, 2.5 for a 1.5" meter, 5 for a 2" meter, and 8 for a 3" meter.
- 19. The gallonage charges should be calculated by apportioning the total variable costs of \$100,601.74 utilizing an increasing block method.
- 20. The rate design for San Saba's rates, effective September 15, 2015, is as follows:

Monthly I	Base Rate	Gallonage Rates Per Gallons	1,000
Meter Size	Rate	Gallonage R	ate
5/8"	\$83.94	0-4,000 \$2	2.70
1"	\$125.91	4,001-8,000 \$3	3.93
1 1/2"	\$209.85	8,001-20,000 \$4	1.99
2"	\$419.70	20,001+ \$5	5.99
3"	\$671.52		

- 21. San Saba presented no evidence as to the number of customers in residential and commercial customer classes.
- 22. San Saba incurred reasonable and necessary rate case expenses in the amount of \$22,055.02.
- 23. Rate case expenses should be recovered by a surcharge over a 12-month period as follows: \$22,055.02 divided by the total number of current customers, divided by 12.

### B. Conclusions of Law

- 1. San Saba is a retail public utility. Tex. Water Code § 13.002(19).
- 2. San Saba is a water supply corporation. Tex. Water Code § 13.002(24).
- 3. Ratepayers may appeal rates established by a water supply corporation. Tex. Water Code § 13.043(b)(1).
- 4. The petition appealing the rates adopted by San Saba was timely filed with the Commission within 90 days after the effective date of the rates and was signed by more than 10% of the ratepayers whose rates were changed. Tex. Water Code § 13.043(c); 16 Tex. Admin. Code § 24.41(b).
- The Commission has jurisdiction over this proceeding. Tex. Water Code § 13.043(b)(1), (e).
- 6. SOAH has jurisdiction over matters relating to the conduct of this proceeding. Tex. Util. Code § 14.053; Tex. Gov't Code ch. 2003.
- 7. San Saba has the burden of proof to establish that the contested rates are just and reasonable. 16 Tex. Admin. Code § 24.12.
- 8. The Commission may consider only the information that was available to San Saba at the time it adopted its rates. Tex. Water Code § 13.043(e).
- 9. San Saba proved that its projection for the cost of water purchased from the City of San Saba, \$68,418, was a known and measurable change that was a reasonably anticipated projected expense based on figures known to San Saba at the time the Board adopted new rates. Tex. Water Code § 13.043(e).
- 10. San Saba proved that eighty percent of repair and maintenance expenses are used to repair pipe and are fixed costs and that twenty percent of repair and maintenance expenses are variable costs, based on information known to San Saba at the time the Board adopted the new rates. Tex. Water Code § 13.043(e).

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- 11. San Saba's rates must be just and reasonable; not be unreasonably preferential, prejudicial, or discriminatory; and sufficient, equitable, and consistent in application to each class of customers. Tex. Water Code § 13.043(j).
- 12. When setting rates, the Commission must use a "methodology that preserves the financial integrity of the retail public utility." Tex. Water Code § 13.043(j).
- 13. The use of the cash-needs method was appropriate in this case.
- 14. As to San Saba's request to recover its reasonable rate case expenses in this proceeding, the Commission may consider evidence of reasonable expenses incurred by San Saba in the appeal proceedings. Tex. Water Code § 13.043(e).
- 15. San Saba may recover the expenses it has incurred in this proceeding to the extent those expenses were reasonable and necessary. 16 Tex. Admin. Code § 24.41(e)(2).
- 16. San Saba proved that it incurred reasonable rate case expenses in the amount of \$22,055.02 for the pendency of this proceeding.

### C. Proposed Ordering Paragraphs

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In accordance with the above findings of fact and conclusions of law, the Commission issues the following Order:

1. Effective as of September 15, 2015, and beginning with the next billing cycle after this Order is issued, San Saba shall charge the following water rates:

Monthly <b>H</b>	Base Rate	Gallonage Rates Gallon	s Per 1,000 s
Meter Size	Rate	Gallonage	Rate
5/8"	\$83.94	0-4,000	\$2.70
1"	\$125.91	4,001-8,000	\$3.93
1 1/2"	\$209.85	8,001-20,000	\$4.99
2"	\$419.70	20,001+	\$5.99
3"	\$671.52		

2. Beginning with the next billing cycle after this Order is issued, San Saba shall fully account for all sums collected since September 15, 2015 in excess of the rates set forth above, and shall refund those sums over the same number of months as San Saba's newly adopted rates were collected.

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- 3. Beginning with the next billing cycle after this Order is issued, San Saba may recover its rate case expenses through a monthly surcharge, as follows:
  - a. The surcharge shall be calculated by dividing \$22,055.02 by the total number of current customers, and then dividing the result by 12; and
  - b. The surcharge shall be collected for 12 months or until the total amount is collected, whichever occurs first.

SIGNED January 13, 2017.

Ch Vandroux

HOLL¥ VANDROVEC ADMINISTRATIVE LAW JUDGE STATE OFFICE OF ADMINISTRATIVE HEARINGS

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	lerided Revenue Nequirement - Attacmment A							
c	2	U VSSWSC Revenue	Staff	E Staff Revenue	щ	G Water Fixed	т ×	Vater Variable
Line #	Revenue Account	Requirement	Adjustments	Requirement	% Fixed	Cost	Variable	Cost
2	Capital Fee		(1.500.00)	(1.500.00)	50%	(750.00)	50%	1750 00
'n	Membership Fee	1	(1,000.00)	(1,000.00)	50%	(500.00)	, 50%	(500.00
4	Late Fee	1	(720.00)	(720.00)	50%	(360.00)	50%	(360.00
້	Line Extension	1	(3,275.00)	(3,275.00)	50%	(1,637.50)	50%	(1,637.50
0 1	Interest Income		(165.00)	(165.00)	50%	(10.66)	50%	(82.50
80	Total Income	• -	(6,699.32)	(6,699.32)	50%	(3,349.66)	50%	(3,349.66
6	Expense Account							
10	Salaries	16,590.00		16,590.00	100%	16,590.00	、%0	•
#	Contract Labor	66,000 00	24,000.00	90,000,06	100%	90,000,06	%0	,
7 5	Utilities Demiserand Maintenance	29,096.00		29,096.00	%0	1	100%	29,096.00
14		30,051.00		30,051.00	80%	24,040.80	20%	6,010.20
15	Accounting & Legal	4,680.00		4,680.00	100%	4.680.00	%0 %0	
16	Insurance - WC & Liability	5,914.00		5,914.00	100%	5,914.00	%0	1
17	License & Dues	5,467.00		5,467.00	100%	5,467.00	%0	1
18	Postage & Freight	2,316.00		2,316.00	100%	2,316.00	%0	,
19	Deprectation	10,484 00	(10,484.00)	1		'		-
21	Miscelianeous	534.00		534.00	20%	106.80	80%	427.20
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23	System Depreciation	128.504.00	(128,504,00)	00.014,000	80		%00T	68,418.UU
24	TCEQ Fine	7,020.00	- (7,020.00)			•		
25	Total Operations & Maintenance Cost	395,666.00	(139,039.32)	256,626.68	61%	156,024.94	39% 1	100,601.74
27	Debt Service (Notes to Financial Statements and Agreements Provided)							
28	USDA Annual Loan Pmt Amount (5%, 40 Years, \$650,000, 9/2031)		37,680.00	37,680.00	100%	37,680.00	%0	
29	TWDB Annual Loan Pmt Amount (4.07%, 10 Years, \$310,000, 1/2022)	•	38,664.00	38,664.00	100%	38,664.00	%0	-
80	TWDB Annual Loan Pmt Amount (0.28%-5.79%, 30 Years, \$335,000, 1/20	1	22,699 20	22,699.20	100%	22,699.20	%0	
	Nelson Lewis, Inc. Annual Loan Pmt Amount (4%, 3 Years, \$70,000, 6/2018 annual PMT = \$24 800 161 Normalized for 30 vesse for							
31	supplement to original loan cost of \$335,000)	I	4,010.29	4,010.29	100%	4,010.29	%0	
32	Total Annual Debt Payments		103,053.48	103,053.48	100%	103,053.48	8	
ŝ	Debt Coverage 1.35		36,068.72	36,068.72	100%	36,068.72	%0	•
34	Total Revenue Requirement \$	395,666.00	\$ 82.88	\$ 395,748.88	74.58%	\$ 295,147.14	25.42%	\$ 100,601.74

	Multi-Tien	ed Rates	
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	1" 1 1/2 2" 3"		•
r	1" 1 1/2 2" 3" venue generated	by Minimum Charge	\$ 295,133
r Total re	1" 1 1/2 2" 3" venue generated	by Minimum Charge	\$ 295,133
r Total re	1" 1 1/2 2" 3" venue generated Volumetric F	by Minimum Charge	\$ 295,133
r Total re	1" 1 1/2 2" 3" venue generated Volumetric F	by Minimum Charge Revenue	\$ 295,133
	1" 1 1/2 2" 3" venue generated Volumetric F to to	by Minimum Charge Revenue 0 4000	\$ 295,133 29,936
Total re 0 1 400	1" 1 1/2 2" 3" venue generated Volumetric F to to to 10 10	by Minimum Charge Revenue 0 4000 <sup>1</sup> 8000	\$ 295,133 \$ 29,936 29,944
Total re 0 1 400 800	1" 1 1/2 2" 3" venue generated Volumetric F to to 10 10 10 10 10 10 10 10 10 10	by Minimum Charge Revenue 0 4000 <sup>3</sup> 8000 20000	\$ 295,133 \$ 295,133 29,936 29,044 28,981
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Total re 0 1 400 800 200	1" 1 1/2 2" 3" venue generated Volumetric F to to 10 10 10 10 10 10 10 10 10 10	by Minimum Charge Revenue 0 4000 <sup>3</sup> 8000 20000 0	\$ 295,133 \$ 295,133 29,936 29,044 28,981 12,650
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Charge	\$100,611
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# STATE OFFICE OF ADMINISTRATIVE HEARINGS

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### **AUSTIN OFFICE**

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300 West 15th Street Suite 502 Austin, Texas 78701 Phone: (512) 475-4993 Fax: (512) 322-2061

# **SERVICE LIST**

AGENCY:	Public Utility (	Commission of Texas (PUC)
STYLE/CASE:	NORTH SAN CHANGE RA	SABA WATER SUPPLY CORPORATION TO
SOAH DOCKET NUMBER:	473-16-1834.W	'S
<b>REFERRING AGENCY CASE:</b>	45283	( 
STATE OFFICE OF ADMINIS'	FRATIVE	ADMINISTRATIVE LAW JUDGE
HEARINGS		ALJ HOLLY VANDROVEC
<b>REPRESENTATIVE / ADDRES</b>	SS ·	PARTIES
RICHARD T. MILLER MILLER & SPINKS, L.L.P. 414 E. WALLACE ST. P.O. BOX 99 SAN SABA, TX 76877 (325) 372-4400 (PH) (325) 372-3645 (FAX)		
		NORTH SAN SABA WSC
SAM CHANG ATTORNEY PUBLIC UTILITY COMMISSION OF LEGAL AND ENFORCEMENT DIVISION 1701 N. CONGRESS AVE., SUITE 8-11 AUSTIN, TX 78711-3326 (512) 936-7260 (PH) (512) 936-7268 (FAX) sam.chang@puc.texas.gov	TEXAS ON 0	
		PUBLIC UTILITY COMMISSION OF TEXAS
BARBARA HORN BILL HARDY RATE PAYERS' COMMITTEE 7255 COUNTY ROAD 124 SAN SABA, TX 76877 (325) 372-4676 (PH)		
· ·	,	RATE PAYERS' COMMITTEE
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