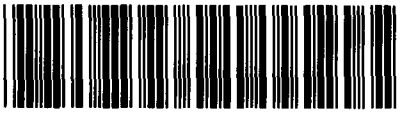

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SOAH DOCKET NO. 473-17-0119.WS
PUC DOCKET NO. 46245

APPLICATION OF DOUBLE DIAMOND UTILITY COMPANY, INC. FOR WATER AND SEWER RATE/TARIFF CHANGE	§ § § §	BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS

WHITE BLUFF RATEPAYERS GROUP'S
REPLY BRIEF ON CONTRIBUTION ISSUES

TO THE HONORABLE PUBLIC UTILITY COMMISSION OF TEXAS:

Pursuant to the Briefing Order issued on May 30, 2018, in this docket, White Bluff Ratepayers Group ("WBRG") hereby files this reply brief addressing the brief filed by Double Diamond Utility Co., Inc. ("DDU") on July 2, 2018, and would respectfully show as follows.

Response to Double Diamond Utilities

DDU's brief reads the Commission's questions very broadly. WBRG read the questions as seeking input as the difference between "developer contributions" and "customer contributions." DDU reads the questions as an invitation to relitigate the ALJ's and the Commission's previous determinations regarding DDU's rate base. WBRG objects to being forced to once again have to respond to DDU's attempts to fix its failure to meet its burden of proof regarding the character of its assets.

In its brief, DDU makes a sweeping claim that "[n]owhere does the TWC require exclusion of developer contributed capital from the rate base like it does customer contributed capital."[1] This assertion is consistent with DDU's position throughout this matter that developer contributions should be treated as the utility's invested capital (unless the utility—out of the goodness of its heart—decides to exclude some of the assets).

DDU's claim, however, ignores the plain language of the Texas Water Code ("TWC"), and ignores long-standing agency rules interpreting the statute. While the TWC does not expressly identify developer contributions as a class of assets to be excluded from rate base for purposes of earning a return, the statute does expressly limit a utility's opportunity to earn a return to "its [the utility's] invested capital,"[2] and the statute defines "original cost" as the actual

[1] DDU Brief at 9.
[2] Tex. Water Code §13.183(a)(1). (TWC)

cost paid for the property at the time the property is dedicated to public use.[3] As the Commission noted in *Sunbelt*, utility plant is dedicated to public service at the time that the first home buyer takes service, which is after the transfer of utility plant (at no cost) to the utility, meaning that the actual money cost to the utility at the time the plant is dedicated is zero.[4] The Commission's decision in *Sunbelt* was upheld by the Texas Supreme Court. The operative statutory provisions have not been changed by the legislature since the court's decision in 1979.

Commission rules also clearly state that, unless otherwise determined by the Commission, all contributions in aid of construction shall be deducted from the overall rate base.[5] The rule does not distinguish between customer and developer contributions because it is not necessary in this context. This rule, and the predecessor rule at the TCEQ, and the predecessor rule at the Commission before the transfer to the Texas Water Commission, have always been interpreted to exclude all contributed assets from rate base. No challenge has been made to this rule. DDU is simply wrong in its assertion that developer-contributed capital can be included in invested capital.

Next, DDU argues that it should be allowed to include the developer-contributed assets in its rate base because the assets "are still on its parent company's books as depreciable property,"[6] citing *Texas Water Commission v. Lakeshore Utility Company, Inc.*, 877 S.W.2d 814 (Tex. App.—Austin 1994, writ denied). While the court in *Lakeshore* stated that there "conceivably could be situations" where a utility could include as invested capital property owned by a separate entity, the situation conceived of by the court involved a situation where the property was owned by a non-developer parent holding company.[7] The facts in *Lakeshore* did not involve developer contributions. The Commission should not buy DDU's argument that a utility can include as its invested capital property that would otherwise be developer contributions simply because the property is owned by DDU's developer parent.

Additionally, DDU argues that the fact that DDI was both the developer and utility through 1996 is "not relevant" to the analysis and then uses extra-record evidence to argue that it met its burden of showing that a portion of DDI's investment was not accounted for as "cost-of-

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[3] TWC §13.185(b).

[4] *Examiner's Report, Petition of Sunbelt Utilities for Authority to Change Rates*, Docket No. 804, 3 P.U.C. Bull. 1167 (Mar. 22, 1978) at 3. Exhibit WBRG-1B.

[5] 16 TAC §24.31(c)(3)(D).

[6] DDU Brief at 10.

[7] *Lakeshore*, 877 S.W.2d at 821 & n.10.

lots" and offset against lot sales.[8] This part of DDU's brief is well beyond the scope of the issues subject to the briefing order, and is nothing more than an attempt to supplement the record long after the record closed and to create a wholly new argument regarding the evidence in the record.

WBRG's position throughout the hearing was that DDU had failed to reconcile its claim of an 80% Developer/ 20% Utility split on the initial utility plant investment. DDU's response to this argument was that it did not have these records[9] and that the records were irrelevant since it had no obligation to identify any of the plant as developer contributed. Now, at the very last minute, DDU claims that such records do exist, that the amounts can be reconciled, and DDU's brief offers testimony as to how the reconciliation can be made. DDU's brief contains two detailed pages of explanation and calculations. If DDU wanted to make this argument, it should have presented it in its direct case. DDU should not be allowed to claim during the hearing that the records did not exist, and now argue that the records do exist. DDU also should not be allowed to make the argument now based on workpapers not in evidence.[10] DDU does not identify the source of its opinion that this is the proper way to "reconcile" these numbers. WBRG has not been given time to review or to cross-examine the source of this opinion. The Commission should ignore these arguments.

Finally, DDU alleges that if the Commission excludes the developer-contributed assets from its rate base, the Commission will "jeopardize Double Diamond's financial integrity."[11] This claim is entirely unsupported by the record, and DDU offers no citation to any evidence supporting the claim. The evidence in the record supports a conclusion that the developer recovered the cost of its investment through lot sales, and that to allow DDU to include these assets in its rate base would cause the ratepayers to pay twice for the same facilities. If DDU's financial integrity is in jeopardy, it is for reasons other than not being allowed to charge its customers twice for the cost of the facilities. Also, the record shows that a bank was willing to lend DDU $3,000,000[12] without restricting the use of the funds to utility purposes. DDU's claims

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[8] DDU Brief at 12–15 and Attachment 1.

[9] Exhibit WBRG-1M, DDU's Response to WBRG 1-15 ("No documentation exists that corresponding entries were made in the financial records of the developer and the utility.").

[10] The Confidential Attachment 3 to DDU's Brief is not in record evidence.

[11] DDU Brief at 16.

[12] WBRG continues to believe that the Commission should review the propriety of this loan. DDU borrowed $3 million that was secured using the White Bluff utility assets. The funds were then transferred to DDU's parent for non-utility uses. The Commission should not allow an investor to remove all equity in a utility without taking

in its brief look like a demand for extra money in exchange for last-minute performance of its obligations. DDU should not be allowed to abandon service to its systems solely because it is not allowed to earn a return on money it did not invest. If nothing else, a utility needs to access capital to reinvest in its system the Water Code and the Commission's rules allow a utility to seek approval of a surcharge to use to generate these funds.[13]

DDU also makes a broad claim that the Commission's decision in this docket reflects a policy change that places the "financial integrity of all the water and sewer utilities . . . at severe risk."[14] It is unclear as to what "change" in policy or utilities DDU is referring. The "change" in policy to exclude contributed capital from rate base is not a change. It has been the State's policy since the late 1970s. Moreover, enforcement of the State's long-held policy should not put any reasonably-run utility's financial integrity at any risk. No utility should have created a business plan based on the State allowing the utility to earn a return on investment that the utility did not make.

DDU thought by filing its rate case without identifying the enormous amounts of developer contributions in its invested capital that the Commission and the ratepayers would not notice. Then, when called out on the failure to identify the contributions, DDU produced the 80/20 split, which it could not support with any documentation or accounting entries. The Commission should not allow DDU at this late stage to finally produce information and arguments that it should have provided in its application. That water has already flowed under the bridge.

Dated: July 9, 2018

Respectfully submitted,

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ATTORNEYS FOR
WHITE BLUFF RATEPAYERS GROUP

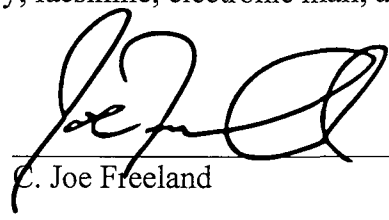
some steps to protect the ratepayers. The utility plant servicing WBRG's members is subject to foreclosure if Double Diamond fails to timely pay off this loan.

[13] TWC §13.183(b).

[14] DDU Brief at 16.

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing pleading was served on all parties of record in this proceeding on July 9, 2018, by hand-delivery, facsimile, electronic mail, and/or First Class Mail.



C. Joe Freeland