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

**APPLICATION OF DOUBLE § PUBLIC UTILITY COMMISSION**  
**DIAMOND UTILITY COMPANY, INC. §**  
**FOR A RATE/TARIFF CHANGE § OF TEXAS**

**ORDER ON REHEARING**

This Order addresses Double Diamond Utilities Company, Inc.'s application to increase rates for water and sewer service provided to two resort developments, The Cliffs in Palo Pinto County, and White Bluff in Hill County, which are owned by an affiliate of Double Diamond Utilities. Double Diamond Utilities filed two rate-filing packages, one for its White Bluff water and sewer systems and one for its water and sewer systems at The Cliffs. Each rate-filing package included a rate increase for water and sewer rates. Double Diamond Utilities requested a revenue requirement of \$568,764 for the White Bluff water system, \$572,130 for the White Bluff sewer system, \$426,112 for The Cliffs water system, and \$317,357 for The Cliffs sewer system, each based on a 2015 calendar-year test year.

The State Office of Administrative Hearings (SOAH) administrative law judge (ALJ), after conducting a hearing, issued a proposal for decision recommending a revenue requirement of \$375,150 for the White Bluff water system, \$349,074 for the White Bluff sewer system, \$383,758 for The Cliffs water system, and \$319,791 for The Cliffs sewer system, based on adjustments to the expenses, rate base, depreciation, and return on invested capital proposed in the application. In response to exceptions to the proposal for decision and replies to the exceptions filed by the parties, the ALJ made several corrections and clarifications to the proposal. In addition, the ALJ supplemented the analysis for several issues discussed in the proposal for decision and provided a recommendation on an aspect of the expense for federal incomes taxes raised in the exceptions.

The Commission agrees with the majority of the ALJ's determinations in the proposal for decision, as corrected and clarified. However, the Commission disagrees with and rejects the ALJ's conclusions regarding Double Diamond Utilities' employee labor expense, other plant maintenance expense, professional services expense, miscellaneous expense, and return on equity. The Commission's decisions result in a revenue requirement of \$310,868 for the White Bluff water

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system, \$196,032 for the White Bluff sewer system, \$358,088 for The Cliffs water system, and \$296,017 for The Cliffs sewer system.

Except as discussed in this Order, the Commission adopts the proposal for decision, including findings of fact and conclusions of law.

## I. Discussion

### A. Procedural History

On August 1, 2016, Double Diamond Utilities filed two rate-filing packages for two resort developments, The Cliffs in Palo Pinto County, and White Bluff in Hill County. Each rate-filing package addressed rates for both water service and sewer service. The Commission referred the docket to SOAH for a hearing on September 8, 2016. A hearing on the merits began on October 24, 2018 and concluded on October 27, 2018.

After the proposal for decision was filed, the parties filed exceptions and replies to exceptions. The ALJ filed a response and made corrections and clarifications to the proposal for decision. In addition, the ALJ supplemented his analysis on several issues. Subsequently, the Commission heard oral argument at its May 10, 2018 open meeting, discussed the proposal for decision, and then instructed Commission Staff to conduct a number run to calculate a revenue requirement and rates that reflected the Commission's discussion at the open meeting.

The Commission issued its original order in this matter on August 30, 2018. The White Bluff Ratepayers Group, a ratepayer-intervenor group, and Double Diamond Utilities each filed a motion for rehearing on September 21, 2018 and September 24, 2018, respectively. On October 12, 2018, the Commission, by written order, extended the time to act on the motions for rehearing to the maximum extent allowed by law.<sup>1</sup>

However, before considering the merits of the motions for rehearing, the Commission instructed Commission Staff to conduct a second number run to correct an error in its initial order regarding Double Diamond Utilities' grinder-pump costs. Double Diamond Utilities' grinder--pump costs are discussed below in subsection D. The Commission's initial order, filed on August 30, 2018, stated that Double Diamond Utilities must capitalize all test-year costs for the

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<sup>1</sup> Order Extending Time to Act on Motions for Rehearing (Oct. 12, 2018).

purchase of replacement grinder pumps for the White Bluff sewer system.<sup>2</sup> However, the Commission's decision on that issue was not properly reflected in Commission Staff's initial number run nor in the tariff approved in the original order for the White Bluff sewer system and the rate base in the approved tariff did not include \$76,409 in grinder-pump replacement costs for the test year.

On October 31, 2018, Commission Staff filed revised number-run schedules reflecting the Commission's decision to capitalize \$76,409 spent during the test year on replacement grinder pumps and to recalculate the rates for White Bluff sewer. In addition, Commission Staff's filing contained updated tariffs for both the White Bluff and The Cliffs water and sewer systems.

In its open meeting on November 8, 2018, the Commission acted on the motions for rehearing. After considering the motions for rehearing, the Commission concluded that its original order was deficient because it failed to properly state some of its decision or to explain the basis for some of its decisions and that there were errors in its original order. Accordingly, the Commission granted rehearing to allow it to correct these problems in its original order.

In its open meeting on August 29, 2019, the Commission discussed whether there was sufficient evidence to support an order on rehearing or whether an additional hearing may be necessary to address certain issues.

In its open meeting on September 12, 2019, the Commission discussed which issues should be addressed in the order on rehearing. The Commission concluded that the order on rehearing should include a compliance docket for the calculation of refunds and surcharges following the final rates established by the Commission, corrections to address the grinder-pump issue consistent with the Commission's decision, identifying the specific depreciation expense on developer-contributed assets for White Bluff water and sewer systems, identifying the original cost for applicable assets for both White Bluff water and White Bluff sewer systems, and the allocation of the salary disallowance approved by the Commission. Additionally, the Commission instructed Commission Staff to perform an additional number run to address these issues and attendant changes.

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<sup>2</sup> Order at 5 (Aug. 30, 2018).

On October 2, 2019, Commission Staff filed its third number run, relevant schedules, and updated proposed tariffs for the White Bluff and The Cliffs water and sewer systems.

On October 31, 2019, the Commission requested clarification from Commission Staff regarding the annual depreciation amount for grinder pumps for the White Bluff sewer system. On November 5, 2019, Commission Staff filed a response clarifying that the annual depreciation amount for grinder pumps for the White Bluff sewer system were included in the revenue requirement schedule included in the October 2, 2019 number run.

The Commission adds new findings of fact 17A through 17V to address events that transpired after the issuance of the proposal for decision. Other changes to the proposal for decision are discussed below.

### **B. The Utility's Books**

The issues discussed in this Order have a recurring theme: poor records or no records to document the costs that Double Diamond Utilities seeks to include in its rates. It is unclear from this record whether Double Diamond Utilities does not have a system to properly account for the utility's costs, whether it fails to maintain adequate records to support its accounts, whether it simply failed to have its records admitted into evidence in this matter, or a combination of these factors. The Commission therefore deems it necessary to discuss Double Diamond Utilities' legal obligations to maintain an appropriate system of accounts and supporting records.

Every water and sewer utility in this state is required to maintain a uniform system of accounts of all business transacted in the manner and form prescribed by this Commission.<sup>3</sup> This includes the form of the utility's books, accounts, and records to be kept by the utility, including receipts and other types of records required by the Commission.<sup>4</sup> A utility is required to keep books, accounts, and other records "accurately and faithfully."<sup>5</sup> By rule, the Commission requires utilities to maintain its books and records in accordance with the uniform system of accounts adopted by the National Association of Regulatory Utility Commissioners (NARUC), and to keep its books on a monthly basis so that "for each month all transactions applicable thereto shall be entered into the books of the utility."<sup>6</sup>

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<sup>3</sup> Tex. Water Code § 13.131(a) (TWC).

<sup>4</sup> *Id.*

<sup>5</sup> *Id.* § 13.131(e).

<sup>6</sup> 16. Tex. Admin. Code (TAC) § 24.127.

Under the NARUC uniform system of accounts, a utility is required to keep books and other records that support the entries in its books “so as to be able to furnish readily full information as to any item included in any account. . . .” and other records that support the entries in its books “so as to be able to furnish readily full information as to any item included in any account.”<sup>7</sup>

The books and records in the NARUC uniform system of accounts “include not only account records..., but all other records, such as minute books, stock books, reports, correspondence, memoranda, etc., which may be useful in developing the history of, or facts regarding, any transaction.”<sup>8</sup> Further, a “utility shall not destroy any such books or records unless the destruction thereof is permitted by rules and regulations of the Commission.”<sup>9</sup>

Thus, Double Diamond Utilities is required to keep books and records that accurately reflect the cost of utility service for its water and sewer systems, including every transaction related to its provision of utility service. It must also maintain those records and present those records in a rate proceeding before this Commission to prove that the costs it seeks to include in its rates meet the requirements of the Texas Water Code and Commission rules when such costs are challenged.

The purpose of the rule is to allow this Commission to meet its obligation to establish an adequate revenue requirement,<sup>10</sup> based on the evidentiary record, so that the Commission can set rates that are just and reasonable to both the utility and the ratepayers. In addition, the rule is intended to ensure that a utility has appropriate and adequate records to present in a rate-filing package when it seeks to revise its rates. As discussed in this Order, Double Diamond Utilities has, in many instances, failed to present adequate evidence to support its requested rates, or in some cases, admitted that it has no such records.

To reflect these statutory requirements, the Commission adds conclusions of law 4A and 4B.

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<sup>7</sup> National Association of Regulatory Utility Commissioners Uniform System of Accounts for Class B Water Utilities at 13 (Accounting Instructions, ¶2A); NARUC Uniform System of Accounts for Class B Water Utilities at 14 (Accounting Instructions, ¶2A) (hereafter cited as Class B Accounts).

<sup>8</sup> Class B Accounts at 13 (water), 14 (sewer) (Accounting Instructions ¶2B).

<sup>9</sup> *Id.* (Accounting Instructions ¶2C).

<sup>10</sup> TWC § 13.183.

### C. Employee Salaries

Double Diamond Utilities initially requested a total of \$171,960 in employee labor expenses for its White Bluff water and sewer systems. The total amount for employee expenses was challenged by the White Bluff Ratepayers Group and is discussed in subsection 1. The salaries of two employees, totaling \$43,680, were challenged by Commission Staff and are discussed in subsection 2. For the remaining employee salaries, totaling \$107,394, Commission Staff did not challenge the amount of the salaries, but did challenge the allocation of employee salaries between the White Bluff water and sewer systems. The allocation of these salaries is discussed in subsection 3.

#### 1. Known and Measurable Change

The total amount requested for test-year salaries for the White Bluff systems was for seven employees. However, all seven employees did not work the entire year; there were only four employees working at the time of hearing.<sup>11</sup> Double Diamond Utilities stated that it was not seeking a known and measurable change in employee labor expenses but that it had adjusted the amount requested to include the total annual salary of all seven employees.<sup>12</sup> Double Diamond Utilities' witness, Mr. Gracy, testified, however, that the amounts actually paid to the seven employees during the test year was \$151,074.<sup>13</sup> The ALJ agreed that Double Diamond Utilities had failed to show that a known and measurable change in employee labor expenses was reasonably certain to occur and that its employee labor expense must therefore be reduced by \$20,886 to \$151,074 to reflect the actual test-year expense.<sup>14</sup>

#### 2. Salaries of Mr. Whitworth and Mr. Keeton

Included in the \$151,074 of Double Diamond Utilities' actual test-year employee labor expenses for its White Bluff systems was \$20,800 for the salary of Jerry Whitworth and \$22,880 for the salary of Danny Keeton. According to Double Diamond Utilities, Mr. Whitworth and Mr. Keeton are backhoe operators that are involved in all tap installations, excavation for installing

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<sup>11</sup> PFD at 21.

<sup>12</sup> PFD at 21.

<sup>13</sup> PFD at 21, citing Direct Testimony of Randy Gracy, DDU Ex. 3 at 15:3–15:6 and Tr. at 104:14-17 (Gracy Cross) (Oct. 24, 2017); *see also* Tr. at 205:22–210:2 (Joyce Cross) (Oct. 24, 2017).

<sup>14</sup> PFD at 22.

taps, clean up of the work site after the installations, and perform *other duties* as needed within the utility department.<sup>15</sup>

Commission Staff argued that the salaries of employees Mr. Whitworth and Mr. Keeton should be excluded because the work orders provided by Double Diamond Utilities show that Mr. Whitworth and Mr. Keeton spend only 1% of their time installing taps, leaving 99% of their time unaccounted for as *other duties*.<sup>16</sup> Because Double Diamond Utilities did not provide any supporting documentation detailing what these other duties include, Commission Staff recommended removing these salaries from employee labor because the other-duties description is too vague to determine whether the salaries are reasonable and necessary expenses for the provision of utility services.<sup>17</sup>

The ALJ concluded that Double Diamond Utilities met its burden to show that Mr. Whitworth's and Mr. Keeton's salaries are reasonable and necessary expenses because they worked on and answered service calls related to both systems.<sup>18</sup> However, the ALJ also concluded that evidence provided gave no explanation of what work was performed, how long it took, or what any of the service calls involved.<sup>19</sup>

The Commission disagrees with the ALJ's determination regarding the salaries of Mr. Whitworth and Mr. Keeton. The Texas Water Code and the Commission's rule limits the expenses that may be included in a utility's cost of service to expenses that are reasonable and necessary to provide utility service to the ratepayers.<sup>20</sup> Double Diamond Utilities has the burden to prove that the salaries for the positions held by Mr. Whitworth and Mr. Keeton are a reasonable and necessary expense of the utility. To meet its burden of proof, Double Diamond Utilities must present evidence that the employee worked on matters related to the utility, quantify the time spent performing that work, and the salary paid for utility-related work.

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<sup>15</sup> Rebuttal Testimony of Randy Gracy 4:17–19 (Oct. 16, 2017); *see also* Commission Staff Ex. 2A, Workpapers of Emily Sears, at ES Workpaper 4 (Sept. 22, 2017).

<sup>16</sup> Commission Staff's Initial Brief at 9–11; Tr. at 335:21-336:7 (Sears Cross) (Oct. 25, 2017); Tr. at 338:18-24 (Sears Cross) (Oct. 25, 2017).

<sup>17</sup> *Id.*

<sup>18</sup> PFD at 8–9.

<sup>19</sup> *Id.*

<sup>20</sup> *See* TWC §§ 13.183(a)(1) and 13.185(d) and (g); *See also* 16 TAC § 24.31(b).



The record reflects that Mr. Whitworth and Mr. Keeton were backhoe operators that were involved in all tap installations, but only spent a small proportion of time installing taps.<sup>21</sup> Mr. Whitworth and Mr. Keeton spent their other remaining time performing other duties as needed. However, Double Diamond Utilities did not provide any evidence explaining or detailing what these other duties entail, whether any of these other duties related to utility matters or the provision of utility service, or the amount of time spent working on utility matters, if any.

In addition, Double Diamond Utilities presented no evidence on whether any of these other duties required skill operating a backhoe, why Double Diamond Utilities needs more than one full-time backhoe operator (given the small amount of time needed for this activity), the market-salary rate for a backhoe and equipment operator, or the experience and skill level of these employees.

The only other evidence in the record regarding the job duties of Mr. Whitworth and Mr. Keeton is Double Diamond Utilities' witness Mr. Gracy's one-sentence statement that all employees are cross-trained in both water and sewer operations to work at both systems.<sup>22</sup>

The record does not contain any work orders, time sheets, or other evidence that would explain how Mr. Whitworth and Mr. Keeton spent the majority of their time completing other duties, the amount of time Mr. Whitworth and Mr. Keeton worked on either system, if any, or even what system they worked on. A conclusory statement that these two men spent an unspecified amount of time on other duties is not sufficient to show that these costs are related to the provision of utility service or that the costs are reasonable and necessary. Mr. Gracy's statement that all employees are cross trained to work on both systems does not provide any explanation as to what specific tasks the employees completed, whether these tasks required the operation of a backhoe, or whether any of these tasks were needed to provide utility service. This single statement is likewise insufficient to meet Double Diamond Utilities' burden. Further, the Commission notes that even the ALJ describes the evidence in the record supporting how Mr. Whitworth and Mr. Keeton spend 99% of their time as "scant and non-specific."<sup>23</sup>

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<sup>21</sup> Rebuttal Testimony of Jay Joyce, DDU Ex. 11 at 4:17-5:1 (Oct. 16, 2017); Workpapers for Rebuttal Testimony of Jay Joyce at 90 (Oct. 16, 2017); Tr. at 403:10-18 (Sears Redirect) (Oct. 25, 2017).

<sup>22</sup> Rebuttal Testimony of Randy Gracy, DDU Ex. 8 at 4:14-4:16 (Oct. 16, 2017).

<sup>23</sup> PFD at 8.

Double Diamond Utilities has not met its burden to show that the salaries for the positions held by Mr. Whitworth and Mr. Keeton are a reasonable and necessary expense for the provision of utility service. The fact that a person was cross-trained to work on either system or performs other duties is not evidence that the person actually worked on a system or that the person's salary is a reasonable or necessary expense.

Thus, aside from tap installations, Double Diamond Utilities has not shown that Mr. Whitworth and Mr. Keeton worked on matters related to providing water and sewer service to its customers. However, the costs related to tap installations are recovered from customers from tap fees and are not therefore properly included in Double Diamond Utilities' cost of service. Under Double Diamond Utilities' tariffs, customers are required to pay a charge to recover the cost of utility taps.<sup>24</sup> Because the costs related to tap installations are recovered through a customer--specific charge, those costs may not be included in Double Diamond Utilities' cost of service used to set base rates.

Double Diamond Utilities had a sufficient opportunity to meet its burden of proof by admitting evidence on the other duties for Whitmore and Keeton; however, it failed to do so. Therefore, removing the \$20,800 salary of Mr. Whitworth and the \$22,880 salary of Mr. Keeton from Double Diamond Utilities' cost of service is warranted because Double Diamond Utilities did not prove that the salaries of these employees are reasonable and necessary to provide service to ratepayers and a portion of their salaries are recovered through a customer charge. Double Diamond Utilities allocated the salaries of its employees evenly between the water and sewer systems with the exception of one employee, Clovis Wilhelm. Therefore, it is appropriate to allocate the removal of the salaries of Mr. Whitworth and Mr. Keeton evenly between the White Bluff water and sewer systems.

Double Diamond Utilities' total employee labor expense that may be included in base rates is \$107,394.

To reflect its decision on this issue, the Commission deletes finding of fact 23, renumbers findings of fact 52 through 54, modifies and renumbers finding of fact 55, and adds new findings of fact 22A through 22D and 23A through 23Q, and adds new conclusion of law 6A.

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<sup>24</sup> See Revised Number Run and Tariffs for Water CCN No. 12078 and Sewer CCN No. 20705 at The Cliffs and White Bluff water utility tariff at 2 and The Cliffs and White Bluff sewer utility tariff at 2 (Oct. 2, 2019).

### 3. Allocation of Employee Salaries

With one exception, Double Diamond Utilities allocated the salaries of its employees evenly between the water and sewer systems; however, the salary of Clovis Wilhelm was allocated 25% to the White Bluff water system and 75% to the White Bluff sewer system.<sup>25</sup> These allocations of the requested \$171,960 in employee labor expenses resulted in expenses of \$80,520 for the White Bluff water system and \$91,440 for the White Bluff sewer system.<sup>26</sup> (The Commission notes that these numbers do not reflect the disallowances discussed above.) Double Diamond Utilities stated it allocated the employee salaries in this manner because all employees are cross-trained in both water and sewer operations and work seamlessly between the water and sewer systems.<sup>27</sup>

Commission Staff argued that Double Diamond Utilities had not shown that the 50-50% allocation was warranted. Commission Staff proposed that the salary of Clovis Wilhelm be allocated to the sewer system because he only holds a wastewater operator's license and his job duties only relate to the wastewater treatment plant.<sup>28</sup> Likewise, Commission Staff recommend that the salaries of Jody Bledsoe (because he held only a water operator's license) and Dwayne Cota (because he had an expired water operator's license) be allocated to the water system.<sup>29</sup>

The ALJ concluded that Double Diamond Utilities met its burden to show that the allocation of salaries is reasonable because employees are trained on both systems and work on both systems.<sup>30</sup>

The Commission disagrees with the ALJ's conclusion that Double Diamond Utilities met its burden to show that its allocation of employee salaries is reasonable. As previously noted, a utility must keep its records in accordance with the NARUC uniform system of accounts. The system of accounts must properly reflect the costs for the water system and the costs for the sewer system. The accounts must reflect the actual time spent working on the water system and the actual time spent on the sewer system. Charges to these accounts should not be based on estimates

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<sup>25</sup> Commission Staff Ex. 2, Direct Testimony of Emily Sears at Attachment ES-5 (Sept. 22, 2017); and PFD at 8.

<sup>26</sup> PFD at 7 (table).

<sup>27</sup> DDU Ex. 8, Rebuttal Testimony of Randy Gracy at 4:14 – 5:1 (Oct. 16, 2017).

<sup>28</sup> Commission Staff Ex. 2, Direct Testimony of Emily Sears (Sept. 22, 2017) at 12:17-13:1 (CS Ex. 2)

<sup>29</sup> Commission Staff Ex. 2, Direct Testimony of Emily Sears (Sept. 22, 2017) at 13:3–7.

<sup>30</sup> PFD at 9.

or be made in an arbitrary fashion.<sup>31</sup> Double Diamond Utilities did not provide any evidence on the amount of time each employee spends working on each system or even which system the employee worked on. The fact that all employees are cross-trained to work on both utilities does not mean that each employee worked on both utilities, or if they did, that their time was split evenly between the two systems. Given the absence of actual time records for the employees, the better approach in this proceeding is to allocate the employee salaries based on the type of license held by each employee and their actual job duties.

However, this approach is not the Commission's preferred approach when tasked with determining the appropriate allocation of employee salaries between systems. Rather, the allocation of salaries should be based on accurate timekeeping records that demonstrate the amount of time an employee actually worked on a particular system, as required by the NARUC uniform system of accounts. A salary allocation based on the amount of time an employee actually worked on a particular system would not affect the overall revenue recovered by the utility, but would affect the rates paid by the customers for each system. The rates set by the Commission must be just and reasonable to customers and it is not appropriate for customers of one system to subsidize the customers of another system. Nor is it appropriate for a customer of both systems to pay an inflated rate for one of the services. Rates for each system must be set at a level that corresponds to each system's cost of service and must be based on the amount of time an employee actually spends working on a system and providing service to that system's ratepayers. The method adopted by this Commission in this Order best achieves those goals and conforms with statutory and regulatory requirements.

Accordingly, the \$107,394 that may be included in Double Diamond Utilities' employee labor expense must be allocated as discussed in this subsection. Mr. Bledsoe held a current water license and an expired wastewater license. Therefore, any of Mr. Bledsoe's salary included in the sewer system's costs must be moved to the water system's costs. Mr. Willhelm held a current wastewater license, accordingly, any of his salary included in the water system's costs must be moved to the sewer system's costs. Mr. Cota held a class D water license; thus, any of his salary included in the sewer system's costs must be moved to the water system's costs. Any of the salaries of Mr. Bledsoe and Mr. Willhelm included in the sewer system's costs must be moved to the water

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<sup>31</sup> Class B Accounts at 18 (water), 17 (sewer).

system's costs. Any of the salary of Mr. Wilhelm included in the water system's costs must be moved to the sewer system's cost.

To reflect its decision on this issue the Commission deletes findings of fact 22 and 24 through 26 and adds new findings of fact 26A through 26H.

#### **D. Other Plant Maintenance Expenses**

Double Diamond Utilities requested a total of \$142,010 in expenses for other plant maintenance at its White Bluff systems. This total included a request of \$79,590.73 for grinder-pump expenses for the White Bluff sewer system.

Although Double Diamond Utilities and Commission Staff both agree that grinder pumps have a service life of about ten years,<sup>32</sup> Double Diamond Utilities stated that it treats costs related to grinder pumps as a recurring annual expense because these costs recur from year-to-year and are a constant maintenance issue in the operation of the White Bluff sewer system. In support of its position, Double Diamond Utilities provided the testimony of Victoria Harkins. Ms. Harkins testified that each year 20 to 30 grinder pumps (out of 259 at White Bluff) are replaced with new pumps and approximately half of its existing grinder pumps are repaired.<sup>33</sup> Therefore, she concluded that both replacement and repair costs should be treated as recurring annual expenses instead of capital investments.<sup>34</sup>

In response to Double Diamond Utilities, Commission Staff argued that Double Diamond Utilities should reclassify all of its grinder-pump expenses as capitalized assets because grinder pumps have a service life of more than one year.<sup>35</sup> In addition, Commission Staff argued that Double Diamond Utilities' capitalization policy requires the grinder pumps to be capitalized rather than expensed.<sup>36</sup> The capitalization policy establishes a three-factor test to determine whether to capitalize an expense.<sup>37</sup> First, the expense must be greater than or equal to \$750.00. Second, the

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<sup>32</sup> Rebuttal Testimony of Victoria Harkins at 3:18–4:5 (Oct. 16, 2017); Tr. at 344:3-4 (Sears Cross) (Oct. 25, 2017).

<sup>33</sup> Tr. at 484:12–488:25 (Harkins Direct) (Oct. 26, 2017).

<sup>34</sup> *Id.*; Rebuttal Testimony of Victoria Harkins at 5-6 (Oct. 16, 2017).

<sup>35</sup> Commission Staff Ex. 4, Errata to the Direct Testimony of Jolie Mathis at 6:9–11 (Oct. 23, 2017); Errata to the Direct Testimony of Emily Sears at 18:1–6 (Oct. 23, 2017); Tr. at 344:17–20 (Sears Cross) (Oct. 25, 2017).

<sup>36</sup> Commission Staff Ex. 6, Double Diamond Utilities' Response to Staff RFI 1-26 at DDU16-015961 (Aug. 11, 2017).

<sup>37</sup> *Id.*

expense must materially extend the useful life of the plant or equipment more than one year. Third, the expense is not a typical, recurring expense.

The ALJ determined that Double Diamond Utilities' capitalization policy did not apply because its grinder-pump costs are a typical and recurring expense incurred by Double Diamond Utilities to repair and replace the pumps in the White Bluff sewer system.<sup>38</sup> Therefore, Double Diamond Utilities' treatment of grinder-pump costs as annual expenses was appropriate.<sup>39</sup>

The Commission disagrees with the ALJ's determination to treat all of Double Diamond Utilities' grinder-pump costs as recurring annual expenses. Whether a type of expense is typical and recurring is not determinative of whether an expense is an ordinary expense or a capital expense. There is no dispute that the expense Double Diamond Utilities seeks to recover includes the maintenance and repair of existing grinder pumps and the purchase of new grinder pumps. In general, a maintenance and repair expense to keep an asset in its current operating condition or restore it to its previous operating condition is an ordinary expense that should be recorded in an expense account and included in the operation and maintenance expense category in setting rates. While some repairs may be such that the usefulness or efficiency of the asset is so enhanced that the expense should be capitalized, the limited evidence in this case does not show that the maintenance and repair expenses sought by Double Diamond Utilities are of this type. Thus, the Commission agrees that the maintenance and repair expenses are ordinary expenses.

However, the Commission disagrees that the cost of new grinder pumps to replace pumps that are no longer operational to meet system needs should be expensed because Double Diamond Utilities incurs this type of expense on an annual basis. Many utilities make capital investments every year. Such investments are both typical and recurring. Whether an expense should be capitalized depends on the specific characteristics of the asset, including the life of the asset, i.e., whether the expense is consumed in the current accounting period.

Based upon the ten-year life of the pumps, the cost of the pumps, and the use of the pumps, the Commission concludes that expense for new and replacement pumps must be capitalized and treated as invested capital for rate-making purposes. Such capital expenses are properly recorded in utility plant asset accounts for equipment, not operations expense accounts.

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<sup>38</sup> PFD at 16–17.

<sup>39</sup> *Id.*

Further, the ALJ's reliance on the testimony of Double Diamond Utilities' witness is misplaced.<sup>40</sup> Ms. Harkins is an engineer, not an accountant. While her testimony related to the engineering aspects of the grinder pumps is credible, her testimony on proper accounting is not. For instance, Ms. Harkins's reference to the exception in the NARUC uniform systems of accounts for small tools and other appurtenances<sup>41</sup> is inapplicable. What may be excluded from equipment accounts under that exception are "hand and other portable tools, which are likely to be lost or stolen or which have a value of less than \$400 or short life . . . ."<sup>42</sup> This exception does not include plant equipment like the grinder pumps.

Because capital investments have a useful life, only a portion of the investment is properly recorded in the current year and the utility recovers that amount through its depreciation expense over the life of the asset. In addition, the utility recovers a return on that investment. By categorizing the grinder pump investments as an annual expense, Double Diamond Utilities recovers 100% of its grinder-pump investment in the first year of a pump's operation, and every year thereafter, instead of spreading the recovery of the investment over the useful life of the pump.

The Commission concludes that, for the White Bluff sewer system, Double Diamond Utilities must expense all test-year costs incurred to maintain and repair grinder pumps and must capitalize all test-year costs to purchase new and replacement grinder pumps. This approach ensures every ratepayer who benefits from the pump's operation may bear their appropriate share of the cost of the pump over the service life of the pump.

This approach is also consistent with the NARUC accounting standards and policies that are mandated by Commission rule. The NARUC accounting standards specify that costs associated with the installation of pumping equipment (such as grinder pumps) should be added to a specific account associated with utility plant and equipment—not with utility expenses. NARUC account 371 for wastewater utilities states that a utility "shall include the cost installed of pumping equipment," and specifies the particular costs that may be included.<sup>43</sup> Although Ms. Harkins stated she relied on criteria and standards from the NARUC accounting policies to support Double Diamond Utilities' treatment of grinder-pump costs as expenses rather than capital investments,

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<sup>40</sup> PFD at 14, 16–17, citing Rebuttal Testimony of Victoria Harkins, DDU Ex. 9 at 3.

<sup>41</sup> Rebuttal Testimony of Victoria Harkins, DDU Ex. 9 at 3:18–23.

<sup>42</sup> NARUC Account at 25 (sewer) (Accounting Instructions ¶21).

<sup>43</sup> NARUC Account at 85 (sewer) (Wastewater Utility Plant ¶371, Pumping Equipment).

Ms. Harkins failed to note NARUC's accounting instructions and the language in NARUC account 371 and its applicability to Double Diamond Utilities' installation of new and replacement grinder pumps. As previously noted, 16 Texas Administrative Code (TAC) § 24.127 requires class B utilities, like Double Diamond Utilities, to maintain its books and records in accordance with the uniform system of accounts as adopted and amended by NARUC for a utility classified as a NARUC class B utility. Therefore, Double Diamond Utilities must capitalize the costs for new and replacement grinder pumps.

Regarding Double Diamond Utilities' capitalization policy, the Commission agrees with the ALJ's conclusion that the capitalization policy does not apply to its grinder-pump costs, but reaches that conclusion for a different reason. The Commission concludes that Double Diamond Utilities' capitalization policy, at least as interpreted by Double Diamond Utilities, violates 16 TAC § 24.127 because it does not follow proper accounting procedures regarding the capitalization of pumping equipment as prescribed by NARUC's uniform system of accounts. While the Commission may approve deviations for the NARUC system of accounts, there is no evidence that the Commission has approved Double Diamond Utilities' capitalization policy and it does not do so here.

Therefore, Double Diamond Utilities must expense all test-year costs incurred to repair grinder pumps and capitalize all test-year costs to purchase new and replacement grinder pumps. This approach ensures that the cost of all grinder pumps used to make normal and routine repairs to the utility system are expensed, while the actual replacement of grinder pumps is capitalized in accordance with NARUC accounting standards regarding the installation of pumping equipment. Accordingly, for its White Bluff sewer system, Double Diamond Utilities shall expense the \$3,181.73 for grinder-pump repair costs and capitalize the \$76,409 in test-year expenses for new and replacement grinder pumps. The Commission's decision on this issue is prospective. To reflect its decision on this issue, the Commission deletes findings of fact 39 and 41, modifies finding of fact 37, and adds new findings of fact 35A, 36A, and 38A through 38M.

#### **E. Professional Services**

Double Diamond Utilities requested \$2,907 for professional services to obtain an amendment to its certificate of convenience and necessity (CCN) in 2015 to allow it to provide



sewer service at The Cliffs resort. Commission Staff asserted that this is not a proper cost to recover through rates because it is not a recurring expense.

Although the ALJ noted that a CCN amendment is not a recurring expense, the ALJ concluded that the cost associated with the CCN amendment is reasonable and necessary to provide sewer service to customers at The Cliffs, and recommended that these expenses be recovered through a rate rider.<sup>44</sup>

The Commission is required to “base a utility’s expenses on historic test year information adjusted for known and measurable changes . . . .”<sup>45</sup> In addition, the Commission is to fix a utility’s revenue requirement at a level to permit the utility a reasonable opportunity to earn a reasonable return on its investment and recover its reasonable and necessary operating expenses.<sup>46</sup> Finally, the Commission must set rates that are just and reasonable.<sup>47</sup>

Although Double Diamond Utilities incurred expenses of \$2,907 for obtaining a CCN amendment during the test year, the Commission disagrees with the ALJ’s conclusion to allow recovery of the cost of the CCN amendment for The Cliffs system. The Commission uses historical costs to establish a revenue requirement to be recovered through rates on a going-forward basis that will provide the utility with sufficient revenues to properly run its business. Rates are not set to recover historical costs, but are set to recover the anticipated future revenue requirement of the utility. Thus, test-year expenses are adjusted for known and measurable changes to set a revenue requirement that is more reflective of the utility’s present and future cost of providing service.

An expense incurred in the test year that is not a recurring type of cost and should not be recovered through rates. First, it is a known and measurable change to the test-year expenses. Second, allowing recovery of such a non-recurring expense through rates is not just and reasonable to customers or the utility.

There is no dispute that a utility does not seek to amend its CCN on an annual, or even a periodic basis. Some utilities never amend their CCN and Double Diamond Utilities presented no

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<sup>44</sup> PFD at 18–19.

<sup>45</sup> TWC § 13.185(d)(1).

<sup>46</sup> *Id.* § 13.183(a).

<sup>47</sup> *Id.* § 13.182(a).

evidence that it would seek an amendment to its CCN in the future. Thus, it is known that the expense for the 2015 CCN amendment is not the type of expense the utility must cover going forward, and the \$2,907 in expenses is measurable. This expense must therefore be removed from Double Diamond Utilities' revenue requirement as it does not need this amount to cover its present and future cost of providing utility service. Accordingly, setting rates to recover this annual revenue is not just and reasonable as such rates would recover revenue that is not needed. If an expense is not recurring, it should not be included in a utility's revenue requirement and recovered from ratepayers through rates year after year. The use of a test year, when appropriately adjusted for known and measurable changes, both positive and negative, limits costs to those recurring costs that can reasonably be expected to continue into the future. Otherwise, a utility could artificially inflate expenses included in its test year and requested revenue requirement by saving a large portion of its one-time expenses for the test year.

Consequently, Double Diamond Utilities' requested \$2,907 for professional services to obtain an amendment to its CCN must be excluded from its revenue requirement.

To reflect its decision on this issue, the Commission deletes findings of fact 45 and 46 and adds new findings of fact 46A and 46B.

#### **F. Miscellaneous Expenses**

Double Diamond Utilities requested total miscellaneous expenses of \$55,685 for its White Bluff systems and \$41,113 for its systems at The Cliffs. These requested amounts include a percentage of the overhead expenses of the White Bluff and The Cliffs resorts. Double Diamond Utilities explained that because the utility offices are located within the resorts' administrative buildings, the utility uses some of the resorts' resources, and is then billed by the resorts for the resources used.<sup>48</sup> The resorts' overhead expenses include the salary for the general manager and office manager at the resorts, employee compensation (including commissions and bonuses), payroll expenses, electricity, water and sewer, office space, phones, computers, copiers, uniforms, and small tools. The utility systems are billed a total of 3.3% of all overhead and general and administrative expenses incurred by each resort.

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<sup>48</sup> Tr. at 329:25–330:6 (Sears Cross) (Oct. 25, 2017); Rebuttal Testimony of Randy Gracy at 8:12–9:2 (Oct. 16, 2017); Tr. at 474:4–475:6 (Gracy Cross Rebuttal) (Oct. 26, 2017).

Commission Staff asserted that these allocated expenses duplicated items already included in Double Diamond Utilities' cost of service and included items not applicable to utility service. Double Diamond Utilities disputed this assertion and claimed that some of the expenses were similar, but did not duplicate any costs included in its cost of service. The White Bluff Ratepayers Group argued that these costs were affiliate expenses that could not be included in rates absent specific Commission findings.<sup>49</sup>

The ALJ concluded that the resort overhead expenses billed to Double Diamond Utilities' water and sewer systems at White Bluff and The Cliffs are reasonable and necessary to furnish service to Double Diamond Utilities' customers.<sup>50</sup> The ALJ reasoned that although there are costs that appear in both Double Diamond Utilities' cost of service and the resort budget, a 3% portion of the resorts' total overhead expenses is reasonable because Double Diamond Utilities is saving money on office space, supplies, and employees through the assignment of these overhead costs.

As to the assertion that these costs are affiliate expenses, the ALJ stated that it is unclear whether Double Diamond Utilities "actually makes any payments to the resorts for these costs."<sup>51</sup> The ALJ then states: "It appears from the evidence that these are costs incurred by the resort, 3% of which are then expensed to [Double Diamond Utilities] . . . ."<sup>52</sup>

The Commission disagrees with the ALJ's recommendation and instead adopts Commission Staff's recommended disallowances of \$8,380 for water and \$6,068 for sewer from White Bluff's requested miscellaneous expenses, and \$20,075 for water and \$18,270 for sewer from The Cliffs requested miscellaneous expenses.<sup>53</sup>

The Commission interprets the ALJ's language to mean that Double Diamond Utilities does not actually pay the resort anything for these "shared expenses," and that the utility simply records this amount on its books as an expense, even though it does not actually incur an expense. If that is the case, then these amounts may not be included in Double Diamond Utilities test-year expenses or used to set its revenue requirement. A utility may record as a cost in its books "the

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<sup>49</sup> PFD at 23–25.

<sup>50</sup> PFD at 25.

<sup>51</sup> PFD at 26.

<sup>52</sup> *Id.*

<sup>53</sup> Commission Staff Ex. 2, Direct Testimony of Emily Sears at 9:11–10:2 (Sept. 22, 2017).

amount of money actually paid” for a service.<sup>54</sup> If a utility does not pay for a service, it may not include the amount in its test-year expenses or recover the amount in rates.

But even if Double Diamond Utilities actually pays the resort, the evidence in the record shows that the amount of resort overhead expenses billed to the White Bluff systems and The Cliffs systems includes the cost of items unrelated to the provision of utility service. Further, the amounts billed to Double Diamond Utilities are not based on Double Diamond Utilities’ actual share of resort expenses that it directly uses; instead, it is an average, across-the-board charge of 3% of all overhead and general and administrative expenses incurred by the resort.

Resort expenses, such as advertising for the resort, commissions and bonuses for resort employees, or uniforms for resort employees, cannot be allocated to the utility because these items are not used to provide utility services.<sup>55</sup> Indeed, Double Diamond Utilities’ witness Mr. Gracy confirmed that some expenses included in the 3% charge are not used by the utility.<sup>56</sup> Further, Double Diamond Utilities provided no evidence regarding the amount of time amenities and resources were used at the resort buildings, or whether the amenities and resources were used for utility purposes, if at all, or the costs of such amenities and resources. Moreover, the record does not contain any work orders, time sheets, or other evidence that show the amount of time the general manager and office manager spend working on utility matters, if any. Thus, a reduction in Double Diamond Utilities’ requested expense is warranted.

The Commission further concludes that expenses paid by Double Diamond Utilities to the resorts are an affiliate transaction under Texas Water Code (TWC) § 13.185(e).<sup>57</sup> The entities that own and operate the resorts are wholly-owned subsidiaries of Double Diamond-Delaware, Inc., and qualify as an affiliate under TWC § 13.002(2). Thus, amount paid by Double Diamond Utilities to the resorts, if in fact any actual payments were made, are an affiliate payment under TWC § 13.185(e).

Payments made to an affiliate “may not be allowed either as capital cost or as expense except to the extent the [Commission] finds the payment to be reasonable and necessary.” Such a finding, “must include specific statements setting forth the cost of each item to the affiliate, and

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<sup>54</sup> NARUC Account at 9 (Definitions ¶9, definition of cost).

<sup>55</sup> Tr. at 330:6–8 (Sears Cross) (Oct. 25, 2017); Tr. at 475:10 (Gracy Rebuttal Cross) (Oct. 26, 2017).

<sup>56</sup> Tr. at 475:10 (Gracy Rebuttal Cross) (Oct. 26, 2017).

<sup>57</sup> TWC § 13.185(e).

must find that the price to the utility is no higher than prices charged by the affiliate to its other affiliates, or to unaffiliated persons or corporations.”<sup>58</sup> Double Diamond Utilities presented no evidence to allow such detail findings to be made. Allocating a percentage of all of the resorts overhead and general administrative expenses is grossly inadequate to meet the statutory standards. Without evidence to make these required specific findings, the Commission may not allow Double Diamond Utilities to recover these expenses.

To reflect its decision on this issue, the Commission modifies finding of fact 60, deletes findings of fact 61 through 67, deletes conclusion of law 6, adds new findings of fact 65A through 65N, and adds new conclusions of law 5A and 6B through 6H.

**G. Depreciation Expense-Known and Measurable Changes**

In its application, Double Diamond Utilities requested the following depreciation expenses for each of its four systems. It appears that these changes are limited to collection and distribution lines for the water and sewer systems at both resorts.

<b>Double Diamond Utilities’ Requested Depreciation Expense<sup>59</sup></b>				
	<u>White Bluff</u>	<u>White Bluff</u>	<u>The Cliffs</u>	<u>The Cliffs</u>
	<u>Water</u>	<u>Sewer</u>	<u>Water</u>	<u>Sewer</u>
Test year (2015)	\$78,805	\$69,816	\$45,823	\$38,159
Known and Measurable Changes	\$31,272	\$14,884	\$32,620	(\$8,896)
<b>Adjusted Test Year Depreciation Expense</b>	<b>\$110,077</b>	<b>\$84,700</b>	<b>\$78,443</b>	<b>\$29,263</b>

The White Bluff Ratepayers Group challenged the known and measurable changes because Double Diamond Utilities provided no explanation to support those changes and they are based on a trended cost study that artificially inflated the original cost of the assets beyond the costs shown on Double Diamond Utilities’ books.<sup>60</sup> Because Double Diamond Utilities possessed reliable

<sup>58</sup> *Id.*

<sup>59</sup> Double Diamond Utilities’ Application Amendment, Schedules I-1, Revenue Requirement Summary (Apr. 26, 2017).

<sup>60</sup> PFD at 27.

accounting records to establish depreciation, the ratepayers group argued that a trended cost study could not be used under Commission rules to establish the original costs of the assets.<sup>61</sup>

Double Diamond Utilities based these changes on a trended cost study performed by Ms. Harkins, who stated that the study was needed because the original invoices were not available.<sup>62</sup> However, Tim Grout, Double Diamond Utilities' chief financial officer, testified that the actual costs of the subject assets are on the balance sheet, are based on invoices, and that he had no reason to doubt the book values for those assets.<sup>63</sup> Ms. Harkins testified that she only looked at invoices and did not review the balance sheet or general ledger.<sup>64</sup> She further stated that if the costs shown on the balance sheet were lower than the cost she developed in her trending study, she would have used the lower number.<sup>65</sup> Double Diamond Utilities argued that the trending study was appropriate because the balance sheet did not provide enough detail.<sup>66</sup>

The ALJ stated that it is not clear whether adequate historical records exist that show the original cost of the assets. The ALJ further stated that while there was not a complete set of invoices, Ms. Harkins did not review the balance sheets to see if the costs were recorded there. The ALJ also stated that there was no testimony that all of the original cost of these assets were not included in the balance sheet and that Mr. Grout testified that the actual costs were on the depreciation list and therefore the balance sheet as well.<sup>67</sup> Thus, there are some historical records to establish the original costs and the ALJ concluded that Double Diamond Utilities failed to meet its burden to show that a trending study could be used under Commission rules.<sup>68</sup>

The Commission adopts the ALJ's recommendation to reject Double Diamond Utilities' request for known and measurable changes to depreciation for both White Bluff and The Cliffs water and sewer systems. The change is simply "the difference between the costs shown in [Double Diamond Utilities'] accounts and the costs developed by Ms. Harkins through her trended cost study."<sup>69</sup> Consequently, the proposed changes are not a known and measurable change but

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<sup>61</sup> *Id.*

<sup>62</sup> PFD at 27, citing Double Diamond Utilities Ex. 5 at 8 (Harkins direct) and Tr. at 186.

<sup>63</sup> *Id.*

<sup>64</sup> *Id.* at 27-28, citing Tr. at 187-88.

<sup>65</sup> PFD at 28.

<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> PFD at 29.

<sup>69</sup> PFD at 29, citing Tr. at 205.

simply a difference in methods of determining costs. And, because there are historical records available to establish the original costs, use of a trending study to establish the original costs is not appropriate. Consequently, Double Diamond Utilities failed to meet its burden to show that the depreciation expenses are known and measurable changes.

To reflect its decision on this issue, the Commission deletes findings of fact 75 through 77 and adds new findings of fact 68A through 68E, 73A, 73B, 74A and 74B.

#### H. Federal Income Tax Expense

After the issuance of the proposal for decision, Commission Staff recommended that the rates ultimately adopted by the Commission for Double Diamond Utilities reflect a lower tax expense due to the change in the federal income tax rate as a result of the Tax Cuts and Jobs Act of 2017.<sup>70</sup> The Commission's accounting order in Project No. 47945 directed Commission Staff to review each investor-owned utility in Texas, on a case-by-case basis, to determine the appropriate mechanism to adjust the utility's rates to reflect the changes to the federal tax rate.<sup>71</sup> Double Diamond Utilities agreed with Commission Staff's recommendations regarding the effects of the change in the federal income tax rate.<sup>72</sup> In its correction letter filed on May 2, 2018, the ALJ stated that the Commission should adopt Commission Staff's recommendations.<sup>73</sup>

In *Suburban Utility Corporation v. Public Utility Commission of Texas*,<sup>74</sup> the Texas Supreme Court held that Suburban Utility, a subchapter S corporation, "is entitled to a reasonable cost of service allowance for federal income taxes actually paid by its shareholders on [the utility's] taxable income or for taxes it would be required to pay as a conventional corporation, whichever is less."<sup>75</sup> In setting rates, the Commission has considerable discretion to determine the appropriate method and amount of income-tax expense because "[t]he income tax calculation is no different than other elements of utility ratemaking."<sup>76</sup>

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<sup>70</sup> Commission Staff's Exceptions to the Proposal for Decision at 10–11 (Mar. 28, 2018).

<sup>71</sup> *Proceeding to Investigate and Address the Effects of Tax Cuts and Jobs Act of 2017 on the Rates of Texas Investor-Owned Utility Companies*, Project No. 47945, Amended Order Related to Changes in Federal Income Tax Rates at 1 (Feb. 15, 2018).

<sup>72</sup> Double Diamond Utilities' Responses to Exceptions to the Proposal for Decision at 12 (Apr. 12, 2018).

<sup>73</sup> Letter from Administrative Law Judge Casey Bell, State Office of Administrative Hearings to Stephen Journeay, Commission Counsel, Public Utility Commission of Texas (May 2, 2018) (filed in the docket).

<sup>74</sup> *Suburban Util. Corp. v. Pub. Util. Comm'n*, 652 S.W.2d 358 (Tex. 1983).

<sup>75</sup> 652 S.W.2d at 364.

<sup>76</sup> *Pub. Util. Comm'n v. GTE Sw. Inc.*, 901 S.W.2d 401, 409–411 (Tex. 1995).

The White Bluff and The Cliffs water and sewer systems are owned and operated by Double Diamond Utilities.<sup>77</sup> Double Diamond Utilities is a subchapter S corporation,<sup>78</sup> which is a pass-through entity for purposes of federal income taxes.<sup>79</sup> Double Diamond-Delaware, Inc., also a subchapter S corporation, is the parent company and sole shareholder of Double Diamond Utilities.<sup>80</sup> R. Mike Ward is the majority shareholder of Double Diamond-Delaware, owner of 94.8% of the shares, with an employee stock ownership plan owning 5.2%.<sup>81</sup> Because Double Diamond-Delaware is also a pass-through entity, it is likely that the majority of tax expenses of Double Diamond Utilities are paid at the individual level by Mr. Ward, the majority shareholder of Double Diamond-Delaware. However, the record does not reflect what amount of Double Diamond Utilities' tax expense is paid by Mr. Ward or the applicable tax rate.

The Commission notes that recent changes to federal income tax law have reduced the income tax rate for corporations from 35% to 21%.<sup>82</sup> Therefore, the Commission concludes that it is reasonable to calculate Double Diamond Utilities' tax expense as if it were a C corporation with a federal income tax rate of 21% for ratemaking purposes. This treatment will provide Double Diamond Utilities a reasonable amount for federal income tax expense.

To reflect its decision on this issue, the Commission adds new findings of fact 79A through 79H and corresponding ordering paragraphs.

### I. Invested Capital

The Commission must set a rate that will permit a utility a reasonable opportunity to earn a reasonable return on its invested capital used and useful in rendering service to the public over and above its reasonable and necessary operating expenses.<sup>83</sup> Double Diamond Utilities' invested capital (rate base) has never been established or approved by the Commission because prior cases were settled and no such determination was made.<sup>84</sup> Thus, the Commission must determine the

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<sup>77</sup> Direct Testimony of Randy Gracy at 6:15–21 (Aug. 4, 2017).

<sup>78</sup> See 26 U.S.C. § 1361.

<sup>79</sup> Direct Testimony of Debi Loockerman at 3:15–4:2 (Sept. 22, 2017).

<sup>80</sup> *Id.* at Attachment 8, Double Diamond Utilities' Response to Response to Staff RFI 1-34.

<sup>81</sup> Direct Testimony and Workpapers of Nelisa Heddin, WBRG Ex. 1 at 11:3–.

<sup>82</sup> Pub. L. No. 115-97, 131 Stat. 2054 (Dec. 22, 2017). An Act to provide for reconciliation pursuant to titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018.

<sup>83</sup> TWC § 13.183(a)(1).

<sup>84</sup> Direct Testimony and Workpapers of Nelisa Heddin, WBRG Ex. 1 at 22:1-23:10.



invested capital of Double Diamond Utilities in accordance with TWC § 13.185 and Commission rules.

A utility's invested capital must be based on the original cost of property used and useful in providing utility service, less depreciation.<sup>85</sup> Utility property funded by explicit customer agreements or customers contributions in aid on construction may not be included in invested capital.<sup>86</sup> All contributions in aid of construction, developer contributions, and other sources of cost-free capital must be deducted from rate base.<sup>87</sup>

Double Diamond-Delaware began construction of the White Bluff resort in 1990 and began construction of the utility systems at White Bluff in 1990 or 1991.<sup>88</sup> Double Diamond Utilities, the applicant in this proceeding, did not exist until December 1996. Until December 1996, Double Diamond, Inc., a wholly-owned subsidiary of Double Diamond-Delaware, was both the developer and the utility company at White Bluff and contracted for the construction of the original infrastructure of the utility systems.

After Double Diamond Utilities was created in December 1996, also as a wholly-owned subsidiary of Double Diamond-Delaware, Double Diamond Utilities claims that the original utility infrastructure and other assets existing at that time were "transferred in some form or fashion from Double Diamond, Inc. to [Double Diamond Utilities]."<sup>89</sup> However, there is no evidence in the record to corroborate this assertion, and there is no evidence in the record that Double Diamond Utilities paid any amount for these assets. The record also reflects that the majority of assets installed after the creation of Double Diamond Utilities in December 1996 were paid for by Double Diamond Properties Construction Co., another wholly-owned subsidiary of Double Diamond-Delaware.<sup>90</sup> Again, there is no evidence in the record that Double Diamond Utilities paid any amount for these assets.

Despite the fact that Double Diamond Utilities did not exist until 1996, Double Diamond Utilities initially filed an application stating that all of its investment in the White Bluff water and sewer systems is used and useful, and therefore the appropriate amount of developer contributions

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<sup>85</sup> TWC §13.185(b).

<sup>86</sup> TWC §13.185(b).

<sup>87</sup> 16 TAC § 24.31(c)(2)(B)(v); 16 TAC § 24.31(c)(3).

<sup>88</sup> Direct Testimony of Randy Gracy at 7:13, 23; 10:17 (Aug. 4, 2017).

<sup>89</sup> Tr. at 57:10–12 (Gracy Cross) (Oct. 24, 2017).

<sup>90</sup> WBRG Ex. 1 at 18:11–19:10.

is zero.<sup>91</sup> However, Double Diamond Utilities later agreed to reclassify 80% of the costs of its assets as paid by the developer and 20% as paid by the utility in accordance with company practice.<sup>92</sup> Double Diamond witness Mr. Gracy testified that Double Diamond has been allocating costs in this manner since 1990 or 1991.<sup>93</sup> Mr. Gracy stated that Double Diamond has applied the 80% developer and 20% utility split to all capital investments in the systems, including those in the initial infrastructure until 2008, when the infrastructure for the systems was finally completed. At that point, it was decided that all future capital investments would be 100% funded by the utility.<sup>94</sup> However, he admitted that he could not find any documentation reflecting any of these assertions.<sup>95</sup>

In order to determine what assets should be classified as developer-contributed for this proceeding, Double Diamond Utilities used an asset list prepared by its witness Ms. Harkins to identify 80% of costs associated with White Bluff assets.<sup>96</sup>

Ms. Harkins was retained by Double Diamond Utilities in October 2016 to update asset inventories for Double Diamond Utilities' four systems, including the White Bluff water and sewer systems, and support Double Diamond Utilities' submitted rate base and depreciation information. In her direct testimony, Ms. Harkins explained how she created the asset lists for each of the four systems.<sup>97</sup> Ms. Harkins first reviewed previous rate-case applications filed by Double Diamond Utilities in 2008 and 2009. She then requested all invoices from Double Diamond Utilities for capital items through 2015. Ms. Harkins then created an asset list for each system using the 2008 and 2009 rate-case filings and the requested invoices. She also removed capital assets that had fully depreciated since the 2008 and 2009 filings and updated service lives for each asset.

Ms. Harkins used information from a trending study she completed in 2007 (as part of Double Diamond Utilities' prior rate-case application) to create the asset lists for the four systems.<sup>98</sup> A trending study is used to estimate the original cost of an asset at its date of

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<sup>91</sup> See Application at 12:13-15; see also Double Diamond Utilities Initial Brief at 21 (Nov. 22, 2017).

<sup>92</sup> Direct Testimony of Randy Gracy at 8:3-10 (Aug. 4, 2017); Double Diamond's Initial Brief at 21 (Nov. 22, 2017).

<sup>93</sup> Tr. at 67:10-20 (Gracy Cross) (Oct. 24, 2017).

<sup>94</sup> *Id.*; see also Direct Testimony and Workpapers of Nelisa Heddin, WBRG Ex. 1 at 38:6-39:12.

<sup>95</sup> *Id.*

<sup>96</sup> Direct Testimony of Jay Joyce at 12:16-13:4 (Aug. 4, 2017); Double Diamond Ex. 6-C, White Bluff Asset List; Tr. at 70:3-70:22 (Gracy Cross) (Oct. 24, 2017).

<sup>97</sup> Direct Testimony of Victoria Harkins at 7:2-10:20 (Aug. 4, 2017).

<sup>98</sup> *Id.* at 8:1-8:6.

installation. Ms. Harkins testified that a trending study was necessary primarily because invoices provided by Double Diamond Utilities did not account for the total cost of the pipes at any of Double Diamond Utilities' systems.<sup>99</sup> Therefore, Ms. Harkins conducted the trending study to estimate the original cost of the pipes and other assets at the time of installation at each of the four systems.

Trending studies are allowable under Commission rules to estimate the original cost of utility plant if reliable and verifiable historical records are not available.<sup>100</sup> However, as discussed above, because there are historical records available to establish the original costs, use of a trending study to establish the original costs is not appropriate.

The trending study process starts with a cost of an asset at the time of review and assessment. An index value is then assigned to each asset for its "current" cost and for its cost at the date of its installation. The indices provide a guide to determine appropriate changes in costs since the date of installation. By multiplying the current cost of the asset to its assigned index values, an estimated original cost is calculated.

To arrive at an estimated cost for each asset as part of her study, Ms. Harkins began with the current cost of each asset in 2007 and estimated each assets' installation date.<sup>101</sup> Ms. Harkins requested invoices reflecting 2007 costs from Double Diamond Utilities' then-current suppliers and also researched other costs she could not obtain from suppliers. She then used the Handy Whitman Indices, an index that calculates the cost trends for different types of utility construction, to trend back the current costs to the approximate date of installation. In her testimony, she explained that an index value is assigned for the current date and for the date of installation to provide a guide to determine appropriate changes in costs since the date of installation. Then, by multiplying the current cost by the indices given per year (current and date of installation), an estimated original cost for an asset can be calculated.

After calculating an original cost for each asset, Ms. Harkins then took the trended original cost for each asset, subtracted any costs that may have been double-counted based on her review of invoices, and then depreciated the remainder.<sup>102</sup> She then listed the estimated original cost for

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<sup>99</sup> *Id.* at 8:8–8:15.

<sup>100</sup> 16 TAC § 24.31(c)(2)(B)(i).

<sup>101</sup> Direct Testimony of Victoria Harkins at 8:8–9:22 (Aug. 4, 2017).

<sup>102</sup> *Id.*

each trended asset on its corresponding asset list. Finally, to update the 2007 study for this application, Ms. Harkins updated the asset lists for each system to remove replaced assets and those assets that had depreciated out. She also updated each asset list to reflect capital assets invoiced since 2007 for each system.

The completed asset lists for each of the four systems, including the assets with estimated original costs (the trended assets), are attached to Double Diamond Utilities' witness Mr. Joyce's direct testimony and include a summary of each asset for each system, its service life, date of installation, original cost, net book value, depreciation expense, and accumulated depreciation.

Further, each asset list also identified the portion of asset costs allocated to the utility and the portion designated as developer-contributed. Double Diamond Utilities' identified developer contributions and reduced its rate base amounts in its application by \$1,186,277 and \$137,457 for the White Bluff water and sewer systems, respectively.<sup>103</sup> However, Double Diamond Utilities erroneously applied its 80-20 split to the net book value of each asset—instead of applying the split to the original cost of each asset—thus, undercounting the amount of its developer-contributed costs. In addition, despite the fact that Double Diamond Utilities did not exist at the time the initial infrastructure was constructed, Double Diamond Utilities also applied its 80-20 split to the initial investment in the White Bluff systems.<sup>104</sup> Double Diamond Utilities noted, however, that the identified developer contributions set forth in the White Bluff application are “hypothetical,” as Double Diamond Utilities is unable to determine the actual amount of developer contributions.<sup>105</sup>

The ALJ determined that Double Diamond Utilities did not meet its burden to show that its proposed split was appropriate or supported by the record evidence. The ALJ further concluded that Double Diamond Utilities failed to show what amount of the original cost of utility assets included in its proposed rate base for White Bluff were contributed by the utility.<sup>106</sup> Accordingly, the ALJ recommended that the majority of White Bluff's assets should be treated as developer contributions and removed from rate base. However, the ALJ also found that the evidence showed

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<sup>103</sup> Double Diamond Utilities' Application Amendment, Schedules III-2, Rate Base Summary (Apr. 26, 2017).

<sup>104</sup> Direct Testimony of Randy Gracy at 8:3–8:10, 10:21–11:4 (Aug. 4, 2017).

<sup>105</sup> Double Diamond's Initial Brief at 21 (Nov. 22, 2017).

<sup>106</sup> PFD at 49–50.

that seven utility assets claimed as part of Double Diamond Utilities' rate base were paid for by Double Diamond Utilities, and the net book value of these assets should remain in Double Diamond Utilities' rate base as invested capital.<sup>107</sup> The amount of the assets that should remain in rate base are \$68,355.48 for White Bluff water and \$24,029.64 for White Bluff sewer. For these seven assets, the record evidence demonstrates that the original cost for the applicable White Bluff water assets is \$71,367.48 and the original cost for the applicable White Bluff sewer assets is \$25,624.64.<sup>108</sup>

The Commission agrees with the ALJ's conclusions regarding the invested capital of Double Diamond Utilities that should be classified as developer contributions. Double Diamond Utilities produced no documentation or accounting records to support the claim of its 80-20 split. Double Diamond Utilities is in the best position to access and discover the evidence necessary to differentiate between plant, equipment, and property contributed by the developer and that invested by Double Diamond Utilities. However, it failed to produce evidence accurately identifying the amount of plant assets contributed by Double Diamond Utilities.

Further, it is unclear whether the 80-20 split testified to by Mr. Gracy accurately, or even approximately, represents the amount of developer contributions for the White Bluff systems. The only evidence provided by Double Diamond Utilities is Mr. Gracy's testimony that the decision of how the costs of the utility assets were split was initially made in 1990 and 1991.

In addition, Double Diamond Utilities did not exist at the time the original infrastructure for the water and sewer systems at White Bluff was constructed. The investment made in that infrastructure came from Double Diamond, Inc. The evidence shows that Double Diamond, Inc. paid for the utility assets included in Double Diamond Utilities' rate base that were installed prior to December 1996. Further, approximately 61% of the water system assets and 60% of the sewer system assets included in Double Diamond Utilities' requested rate base for White Bluff were constructed before December 1996.<sup>109</sup>

Accordingly, the Commission agrees with the ALJ's conclusions regarding the invested capital of Double Diamond Utilities that should be classified as developer contributions. To reflect

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<sup>107</sup> PFD at 50.

<sup>108</sup> Direct Testimony and Workpapers of Nelisa Heddin, WBRG Ex. 1 at 19:12-20:9.

<sup>109</sup> Direct Testimony and Workpapers of Nelisa Heddin, WBRG Ex. 1 at 19:12-20:9.

its decision on this issue, the Commission deletes finding of fact 98 and modifies finding of fact 100 and conclusion of law 8, and adds new findings of fact 87A through 87D, 90A through 90C, 93A through 93I, and 100A through 100D.

### J. Sunbelt Utilities v. Public Utility Commission

In addition to arguing against Double Diamond Utilities' proposed split, the White Bluff Ratepayers Group also argued that the holding in *Sunbelt Utilities v. Public Utility Commission*<sup>110</sup> is applicable and controlling in this proceeding. In that case, Sunbelt, a newly formed water and sewer utility, filed an application to change its water and sewer rates in Harris County.<sup>111</sup> A development company affiliated with the utility installed the initial utility system and transferred the assets to the utility without charge. The developer then wrote off the entire cost of the utility system in one year.<sup>112</sup> The Commission's examiner determined that because the development company recovered the cost of the utility assets through lot sales, the purchasers of the lots should not pay for the utility assets a second time through utility rates.<sup>113</sup> Thus, the utility assets paid for by the development company and recovered through lot sales should be excluded from rate base.<sup>114</sup> The Commission agreed with the examiner.

In 1979, the Supreme Court of Texas stated that the principal question in that case was "whether the Commission properly excluded the developer's cost of the utility system from the rate base because the rate payers had already paid for this system as part of the purchase price of their lots."<sup>115</sup> In answering this question, the court evaluated the issue of customer contributions of assets by courts and regulatory bodies in other states.<sup>116</sup> Specifically, the court discussed "the rule which is well established in other jurisdictions that contributions by a customer in aid of construction are properly excluded from the rate base. Under this rule the utility is not allowed to earn a rate of return on property acquired from or paid for by the rate payer."<sup>117</sup> The court ultimately held that "this rule is correct and here hold that consumer contributions in aid of

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<sup>110</sup> *Sunbelt Utilities v. Public Utility Commission*, 589 S.W.2d 392 (Tex. 1979).

<sup>111</sup> *Id.* at 393.

<sup>112</sup> *Id.* at 393-394.

<sup>113</sup> See Examiner's Report, *Petition of Sunbelt Utilities for Authority to Change Rates*, Docket No. 804, 3 P.U.C. Bull. 1167 (Mar. 22, 1978).

<sup>114</sup> *Id.*

<sup>115</sup> *Id.* at 392.

<sup>116</sup> *Id.* at 393.

<sup>117</sup> *Id.*

construction should be excluded from a utility's rate base."<sup>118</sup> Therefore, "the costs were properly excluded [by the Commission's examiner] as contributions in aid of construction."<sup>119</sup>

In this proceeding, the ALJ disagreed with the White Bluff Ratepayers Group's reading of *Sunbelt* and its holding. The ALJ concluded that the primary basis for the Commission's determination that the cost of the Sunbelt utility system should be removed from rate base was that the cost had been expensed by the Sunbelt developer against the amount it realized from the sale of the lots served by the utility system.<sup>120</sup> Therefore, according to the ALJ, the separate finding by the Commission in *Sunbelt* that the lot purchasers had paid the developer's cost of the utility system as part of the purchase price of the lots was not dispositive.<sup>121</sup>

The Commission agrees with the ALJ that the holding in *Sunbelt* is not controlling under the facts in this proceeding. However, the Commission reaches this decision for a different reason. In *Sunbelt*, the Supreme Court of Texas determined that the funds used to pay for the utility system originated with the customer and ultimately concluded that "consumer contributions in aid of construction should be excluded from a utility's rate base."<sup>122</sup> Unlike *Sunbelt*, the Commission in this proceeding has determined that the funds used to pay for the utility systems at White Bluff originated with the developer at White Bluff, not from White Bluff customers. Thus, the Commission concludes that *Sunbelt* is not controlling in this proceeding because the majority of the investment at White Bluff was contributed by the developer, not by customer contributions as was the case in *Sunbelt*.

#### K. Briefing Issues

After the Commission considered the proposal for decision, the Commission asked for briefing related to customer contributions in aid of construction and developer contributions to better inform its decision regarding the initial investment in the White Bluff systems.<sup>123</sup> Customer contributions in aid of construction and developer contribution are not defined in the Texas Water Code or Commission rules; nor are there any court decisions regarding the interpretation or application of these terms. In addition, there was no discussion by the parties in this proceeding

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<sup>118</sup> *Id.*

<sup>119</sup> *Id.* at 392.

<sup>120</sup> PFD at 47.

<sup>121</sup> PFD at 47–48.

<sup>122</sup> *Id.*

<sup>123</sup> Briefing Order (May 30, 2018).

regarding the meaning or application of these terms or whether the initial investments in this case were properly classified as developer contributions. Thus, the Commission deemed it appropriate to ask for briefing to assist its determination on the appropriate interpretation and application of these terms in this proceeding.

There is no difference in the treatment of customer and developer contributions when determining a utility's invested capital. Under Commission rules, all contributions in aid of construction, developer contributions, and other sources of cost-free capital must be deducted from rate base.<sup>124</sup> There is, however, a difference in the treatment of depreciation expense between customer-contributed property and developer-contributed property.<sup>125</sup> The depreciation expense claimed by a utility may not include depreciation on property provided by explicit customer agreements or funded by customer contributions in aid of construction.<sup>126</sup> However, a utility's claimed depreciation expense may include property contributed by a developer or governmental entity, so long as it is currently used and useful.<sup>127</sup>

After considering the parties' briefs and *Sunbelt*, the Commission concludes that it is appropriate to adopt a straightforward and common-sense interpretation of these terms based on the plain language of the Texas Water Code. In determining whether a contribution is a customer contribution in aid of construction or a developer contribution, the Commission will consider the source of the funds or assets and how the funds or assets ultimately reached the utility. Accordingly, the Commission concludes that developer contributions shall include monies or assets transferred from a developer to a utility for utility facilities, not including such items originally obtained from customers. Customer contributions in aid of construction shall include monies provided by customers to a utility for the express purpose of funding utility facilities, even if the funds pass through the hands of other persons before reaching the utility.

To reflect its decision on this matter and related procedures, the Commission adds new findings of fact 90A through 90C, 93B, and 93E, and conclusions of law 8A and 8B.

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<sup>124</sup> 16 TAC § 24.31(c)(2)(B)(v); 16 TAC § 24.31 (c)(3); *see also* TWC § 13.185(b).

<sup>125</sup> *See* TWC § 13.185(j).

<sup>126</sup> TWC § 13.185(j).

<sup>127</sup> *Id.*; 16 TAC § 24.31(b)(1)(B).



### L. Used and Useful Investment at White Bluff

Throughout the proceeding, the White Bluff Ratepayers Group argued that a large percentage of the water and sewer lines at White Bluff are not used and useful because the White Bluff systems were designed and built to serve many more lots than are currently served. Therefore, the costs associated with the water and sewer lines should not be included in rate base.

The ALJ concluded that the question of whether the water and sewer lines are used and useful was moot because the majority of the investment in the water and sewer lines at White Bluff were determined to be developer contributions, and thus removed from rate base.<sup>128</sup>

The Commission agrees with the ALJ that for purposes of rate base, the question of whether the water and sewer lines at White Bluff are used and useful is moot. However, because the Commission concluded that the initial investment at White Bluff—including the investment in the water and sewer lines—should be treated as developer contributions, the Commission must still determine whether the developer contribution at White Bluff is currently used and useful in accordance with TWC § 13.185(j) for purposes of depreciation.

TWC § 13.185(j) provides that “[d]epreciation on all currently used and useful developer or governmental entity contributed property shall be allowed in the cost of service.” Thus, Double Diamond Utilities is entitled to recover its depreciation expense on its developer-contributed property at White Bluff only if the property is currently used and useful in the provision of water service.

According to Double Diamond Utilities, there are approximately 65 miles of water lines and 60 miles of sewer lines at White Bluff, which were designed to serve 6,314 lots across over approximately 3,500 acres.<sup>129</sup> The White Bluff water and sewer systems were built in phases as the White Bluff subdivision developed. As new sections of development were opened, the distribution lines for those sections were installed and connected back to the original systems.<sup>130</sup> At the end of the 2015 test year, Double Diamond Utilities asserted that 85% to 90% of the lots at White Bluff had been sold.<sup>131</sup>

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<sup>128</sup> PFD at 53.

<sup>129</sup> Tr. at 196:1–197:6 (Harkins Cross) (Oct. 24, 2017).

<sup>130</sup> Direct Testimony of Randy Gracy at 8:7–8, 11:1–2 (Aug. 4, 2017).

<sup>131</sup> Tr. at 63:22–64:3 (Gracy Cross) (Oct. 24, 2017).

The sales contract used to sell lots in the White Bluff subdivision states that “potable water service will be provided to all lots in the subdivision” and “sewage collection and disposal will be provided to all lots in the subdivision.”<sup>132</sup> Therefore, the sales contract imposes an obligation to provide water and sewer service to any lot at White Bluff when requested. Further, because White Bluff is within Double Diamond Utilities’ certificated service area, the TWC also imposes such an obligation.<sup>133</sup>

Whether a developer contribution is used and useful is a fact-specific determination to be made in each case. Based on the specific facts in this case, the Commission concludes that Double Diamond Utilities’ investment at White Bluff is currently used and useful. It was reasonable for the White Bluff developer to build out the water and wastewater systems in phases as the subdivision developed such that, when any lot within White Bluff was sold and a new owner requested service, service could be immediately provided. In addition, Double Diamond Utilities is currently obligated to provide service if a lot owner decides to build a house on her lot. Therefore, Double Diamond Utilities is permitted to recover a depreciation expense on its developer-contributed assets at White Bluff in accordance with TWC § 13.185(j).

The original cost for developer-contributed assets for the White Bluff water system is \$429,978 and the net book value is \$209,877, resulting in accumulated depreciation of \$220,101. For the White Bluff sewer system the original cost for developer-contributed assets is \$97,380 and the net book value is \$55,780, resulting in accumulated depreciation of \$41,600.

To reflect its decision on this issue, the Commission modifies findings of fact 103 through 105, deletes finding of fact 107, adds new findings of fact 93A through 93F, 105A and 107A, and adds new conclusions of law 8C and 8D to reflect its determination that Double Diamond Utilities is permitted to recover a depreciation expense on its developer-contributed assets at White Bluff in accordance with TWC § 13.185(j). In addition, the Commission deletes conclusion of law 7 as moot.

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<sup>132</sup> White Bluff Subdivision Sale Contract, WBRG-1G, Direct Testimony and Workpapers of Nelisa Heddin, WBRG Ex. 1 at 90.

<sup>133</sup> TWC § 13.250(a).

### M. Return on Equity

The Commission's rate-filing package for class-B utilities permits a utility to request a return on equity based on a simplified formula. A return on equity calculated using the simplified formula will be presumed reasonable if no other party provides opposing testimony.<sup>134</sup> However, the rate-filing package also states that if parties to the case do not reach a settlement agreement, there is no presumed reasonable return.<sup>135</sup>

Double Diamond Utilities requested a return on equity of 11.49%, following the Commission's instructions for the simplified return-on-equity calculation.<sup>136</sup>

Commission Staff witness Ms. Sears provided testimony opposing Double Diamond Utilities' proposed return on equity. Ms. Sears calculated a return on equity for Double Diamond Utilities of 8.79% based on the discounted cash flow method, which is generally used to calculate returns on equity for companies.<sup>137</sup> The data for the components of the discounted cash flow analysis was taken from a group of water utilities acting as a proxy group for setting Double Diamond Utilities' overall rate of return. Ms. Sears also used the capital asset pricing model (CAPM) as a comparison.<sup>138</sup>

Double Diamond Utilities asserted that Commission Staff's lower return on equity does not account for the risks associated with smaller utilities and, therefore, Double Diamond Utilities would not earn a return equal to what is generally made on investments with corresponding risks and uncertainties. Further, Double Diamond Utilities also expressed concerns with Ms. Sears's failure to consider a small stock risk premium in her analyses.<sup>139</sup>

In response to Ms. Sears's discounted cash flow and CAPM analyses, Double Diamond Utilities witness Mr. Scheig developed a proposed return on equity using the CAPM, discounted cash flow, risk premium analysis, and expected earnings models using a comparable group of water utilities. He also adjusted his proposed return on equity based on Double Diamond Utilities' small capital size, lack of liquidity, and private ownership. His analysis yielded a return on equity

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<sup>134</sup> See Commission's Class B Investor-Owned Utilities Water and/or Sewer Instructions for Rate/Tariff Change Application 2015 at 9-10.

<sup>135</sup> *Id.* at 10.

<sup>136</sup> Rebuttal Testimony of Gregory Scheig at 32:5-32:16 (Oct. 16, 2017).

<sup>137</sup> Direct Testimony of Emily Sears at 33:2-33:4 (Sept. 22, 2017).

<sup>138</sup> Direct Testimony of Emily Sears at 36:1-36:15 (Sept. 22, 2017).

<sup>139</sup> Rebuttal Testimony of Gregory Scheig at 13:3-13:8 (Oct. 16, 2017).

of 11.50%.<sup>140</sup> This return on equity included a small stock risk premium of 1.67% to properly account for the “size, liquidity, capital structures, or other [Double Diamond Utilities] factors.”<sup>141</sup>

The ALJ recommended that the Commission approve a 9.84% return on equity for Double Diamond Utilities. The ALJ determined Double Diamond Utilities’ use of four different analyses to calculate its return on equity was more persuasive than the analyses performed by Commission Staff, who used only the discounted cash flow analysis and capital asset pricing model. However, the ALJ recommended that the Commission decline to add a small stock risk premium on top of the return on equity calculated by Mr. Scheig because Double Diamond Utilities failed to show that such a premium is appropriate in this case.

The Commission disagrees with the ALJ’s conclusion and instead adopts Commission Staff’s recommended return on equity of 8.79%. The discounted cash flow model is widely accepted by the regulatory industry and the Commission, and is often used to calculate the appropriate return on equity for a utility. In addition, the Commission adopted a return on equity of 8.48% calculated by Commission Staff using the discounted cash flow method in Docket No. 45720,<sup>142</sup> the only other contested water-rate case the Commission has considered.

However, the Commission agrees with the ALJ’s conclusion that the addition of a small stock risk premium is not appropriate in this proceeding. A small stock risk premium is not appropriate for water and sewer monopolies because water and sewer utilities are subject to regulatory oversight and a utility’s earnings are set by the ratemaking process. Further, it is unclear from Mr. Scheig’s testimony how he determined that the return on equity for Double Diamond Utilities should include a small stock risk premium.

To reflect its decision on this issue, the Commission deletes findings of fact 113 and 119, modifies findings of fact 110 through 114 and 126, modifies conclusion of law 10, and adds new findings of fact 110A, 114A, and 114B.

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<sup>140</sup> *Id.* at 13:15-14:8 (Oct. 16, 2017).

<sup>141</sup> *Id.* at 32:13-32:16 (Oct. 16, 2017).

<sup>142</sup> *Application of Rio Concho Aviation, Inc. for a Rate/Tariff Change*, Docket No. 45720, Order at 16 (Jun. 29, 2017).

## N. Other Matters

In its motion for rehearing, Double Diamond Utilities argues that the Commission did not comply with the requirements of TWC § 13.1871, which states that:

(d) When a statement of intent is delivered, the utility shall file with the regulatory authority an application to change rates. The application must include information the regulatory authority requires by rule and any appropriate cost and rate schedules supporting the requested rate increase. . . . If the utility fails to provide within a reasonable time after the application is filed the necessary documentation or other evidence that supports the costs and expenses that are shown in the application, the regulatory authority may disallow the nonsupported costs or expenses.

(e) Except as provided by Subsection (f) or (g), if the application or the statement of intent is not substantially complete or does not comply with the regulatory authority's rules, it may be rejected and the effective date of the rate change may be suspended until a properly completed application is accepted by the regulatory authority and a proper statement of intent is provided.<sup>143</sup>

Double Diamond Utilities argues that the Commission allowed Double Diamond Utilities application to proceed over two years at a “great expense [as if Double Diamond Utilities] filed the necessary documentation or other evidence that supports the costs and expenses that are shown in the application.”<sup>144</sup> Double Diamond Utilities argues that now, after the reasonable time period allowed for the Commission to disallow costs or expenses has passed, the Commission seeks to impose new requirements and arbitrarily disallow recovery of expenses and components of Double Diamond Utilities’ rate base.<sup>145</sup> Thus, Double Diamond Utilities argues that the Commission’s decision on this issue is arbitrary, capricious, and an abuse of discretion.

The Commission disagrees with Double Diamond Utilities’ reading of TWC § 13.1871. Double Diamond Utilities’ argument conflates the standard for administrative completeness with a utility’s burden of proof. A review of an application’s administrative completeness is performed to determine whether the Commission has received sufficient documentation to allow Commission Staff to evaluate the merits of an application. An application for a rate change must contain the certain specified information, including the rate-fling-package form, including each schedule,<sup>146</sup> and must be signed by an appropriate person who certifies that the information provided is true,

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<sup>143</sup> Double Diamond Utilities’ Motion for Rehearing at 3 (Sept. 24, 2018).

<sup>144</sup> *Id.*

<sup>145</sup> *Id.*

<sup>146</sup> 16 TAC § 24.27(b).

accurate and complete.<sup>147</sup> Further, the application is reviewed for administrative completeness and the applicant notified of such.<sup>148</sup> Double Diamond Utilities was notified on September 7, 2016 through Order No. 2 that its application was administratively complete.<sup>149</sup>

An application's merits are not evaluated in the review for administrative completeness. Even after an application is deemed administratively complete, a utility is still required to show that its proposed rate change is just and reasonable in accordance with the Texas Water Code and Commission rules. To evaluate an application's merits at the sufficiency phase, as Double Diamond Utilities suggests, would obviate the need for the filing of testimony by parties, the discovery process, or even a hearing on the merits. Further, the provision cited by Double Diamonds Utilities does not impose on the Commission an obligation to inform the utility that it has not provided information or evidence; it authorizes the Commission to disallow costs and expenses that are not supported by the evidence. Even though the Commission found its application administratively complete, Double Diamond Utilities was put on notice through the testimony and other actions of the parties in this case that its requested rate increase might not be legally sufficient. Double Diamond Utilities has opportunities to bring forth additional evidence to support its requested rate increase, but it did not. For the reasons discussed here, the Commission rejects Double Diamond Utilities' arguments on this matter.

#### **O. Other Changes**

The Commission adds new findings of fact 3A and 12A and conclusion of law 1A to more completely describe the applicant. The Commission adds findings of fact 126A through 126T to address the revenue requirement established for Double Diamond Utilities. The Commission adds findings of fact 80A through 80D to address invested capital and rate base established for Double Diamond Utilities. In addition, the Commission adds findings of fact 129 through 132 to address the filings of proposed tariffs for Double Diamond Utilities in this proceeding, and modifies findings of fact 127 and 128 to address changes to Double Diamond Utilities' rate schedules after Commission Staff's third number run.

Finally, the Commission makes additional changes to findings of fact and conclusions of law to correct citations, spelling, numbering, and punctuation and for stylistic purposes.

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<sup>147</sup> 16 TAC § 24.6.

<sup>148</sup> 16 TAC § 24.8(a).

<sup>149</sup> Order No. 2, Deeming Application Administratively Complete (Sept. 7, 2016).

The Commission adopts the following findings of fact and conclusions of law:

## II. Findings of Fact

### Applicant

1. Double Diamond Utilities is an investor-owned company that provides water and sewer utility service to several communities in North Texas through facilities and equipment it operates.
2. Double Diamond Utilities provides water and sewer utility service to The Cliffs development in Palo Pinto County and White Bluff development in Hill County under water certificate of convenience and necessity (CCN) number 12087 and sewer CCN number 20705.
3. Double Diamond Utilities has approximately 640 water customers and 567 sewer customers in White Bluff and approximately 287 water customers and 239 sewer customers in The Cliffs.
- 3A. Double Diamond Utilities has four existing tariffs, one for each of the water and sewer systems at White Bluff and The Cliffs.
4. White Bluff is a resort and residential development with amenities such as a golf course, marina, hotel, restaurant, conference center, spa, and swimming pools.
5. The White Bluff water system obtains its water from four wells in the Trinity aquifer, which is regulated by the Prairielands Groundwater Conservation District.
6. The Cliffs is a resort and residential development with amenities similar to those at White Bluff. The Cliffs water system obtains its water from Lake Possum Kingdom.
7. Double Diamond Utilities is a wholly-owned subsidiary of Double Diamond-Delaware, Inc.

### Application, Notice, and Protest

8. On August 1, 2016, Double Diamond Utilities filed two rate-filing packages, one for White Bluff and one for The Cliffs. Each rate-filing package requested a rate increase and related tariff changes for water and sewer rates.
9. The application is based on a test year of January 1, 2015 through December 31, 2015.

10. Double Diamond Utilities mailed notice of the proposed rate change to all of its customers in White Bluff and The Cliffs on or about August 10, 2016.
11. Between August 10, 2016 and September 1, 2016, more than 10% of Double Diamond Utilities' ratepayers in White Bluff and The Cliffs filed timely protests to the rate changes proposed by the application.
12. The application was found to be administratively complete on September 7, 2016.
- 12A. The application considered in this Order consists of the application filed by Double Diamond Utilities on August 1, 2016, as amended and supplemented by its filing on April 26, 2017.

**General and Procedural Findings**

13. On September 8, 2016, the Commission referred this docket to the State Office of Administrative Hearings (SOAH) for a contested case hearing.
14. On October 7, 2016, the Commission issued its preliminary order, identifying 41 issues to be addressed in this proceeding.
15. On October 18, 2016, a SOAH administrative law judge (ALJ) convened a prehearing conference in Austin, Texas. The following appeared and were admitted as the parties in this case: Double Diamond Utilities; the White Bluff Ratepayers Group; The Cliffs Utility Committee and Commission Staff.
16. By agreement between the parties, a SOAH order set the effective date for the proposed rate changes as April 1, 2018, and set February 21, 2018, as the relate-back date for purposes of determining refunds or surcharges.
17. The hearing on the merits convened on October 24, 2017 and concluded on October 26, 2017. The parties filed initial briefs on November 22, 2017, and reply briefs on December 15, 2017, which is when the record closed.
- 17A. On February 13, 2018, the SOAH ALJ issued the proposal for decision.
- 17B. Double Diamond Utilities, Commission Staff, the White Bluff Ratepayers Group, and The Cliffs Utility Committee filed exceptions to the proposal for decision on March 28, 2018.



- 17C. Double Diamond Utilities, Commission Staff, and the White Bluff Ratepayers Group filed replies to exceptions on April 12, 2018.
- 17D. The Commission granted Double Diamond Utilities request for oral argument, filed on May 1, 2018.
- 17E. On May 2, 2018, the SOAH ALJ filed a response to the exceptions and replies and supplemented the proposal for decision and made clarifications and corrections to the proposal for decision.
- 17F. The Commission heard oral argument at the May 10, 2018 open meeting.
- 17G. At the May 10, 2018 open meeting, the Commission instructed Commission Staff to conduct a number run to reflect the Commission's discussion at the open meeting.
- 17H. Commission Staff filed revised number-run schedules on May 21, 2018.
- 17I. On May 30, 2018, the Commission issued an order requesting briefing on the differences between customer contributions in aid of construction and developer contributions.
- 17J. Double Diamond Utilities, Commission Staff, and the White Bluff Ratepayers Group filed initial briefs on July 2, 2018.
- 17K. Double Diamond Utilities, Commission Staff, and the White Bluff Ratepayers Group filed reply briefs on July 9, 2018.
- 17L. The Commission issued its original order in this docket on August 30, 2018.
- 17M. The White Bluff Ratepayers Group and Double Diamond Utilities each filed a motion for rehearing on September 21, 2018 and September 24, 2018, respectively.
- 17N. On October 12, 2018, the Commission extended time to act on the motions for rehearing to the maximum extent allowed by law.
- 17O. At the October 25, 2018 open meeting, the Commission instructed Commission Staff to conduct a second number run to correct an error in its original order regarding Double Diamond Utilities' grinder-pump costs.
- 17P. On October 31, 2018, Commission Staff filed revised number-run schedules and updated tariffs for the White Bluff and The Cliffs water and sewer systems.

- 17Q. On November 8, 2018, the Commission granted rehearing to reconsider its decision.
- 17R. At the August 29, 2019 open meeting, the Commission discussed whether to proceed with the order on rehearing or hold an additional hearing to obtain more evidence to support the order on rehearing.
- 17S. At the September 12, 2019 open meeting, the Commission identified the specific issues to be addressed in the order on rehearing.
- 17T. Commission Staff filed revised number-run schedules and updated tariffs for the White Bluff and The Cliffs water and sewer systems on October 2, 2019.
- 17U. On October 31, 2019, a memorandum was filed requesting clarification on the number-run schedules filed by Commission Staff on October 2, 2019. Commission Staff was asked to clarify whether the annual depreciation amount for the grinder pumps for the White Bluff sewer system were inadvertently omitted or intentionally excluded from the revenue requirement in schedule 1.
- 17V. On November 5, 2019, Commission Staff filed a response to the memorandum requesting clarification on the number-run schedules and stated that the number run filed on October 2, 2019 includes the annual depreciation amount for grinder pumps for the White Bluff sewer system.

**Revenue Requirement**

**Operation and Maintenance (O&M) Expenses**

**Other Revenues**

18. Double Diamond Utilities received \$3,600 in revenue from Nextlink that should be added to White Bluff water's other revenues.

**Other Volume-Related Expenses**

19. Double Diamond Utilities included \$830 of White Bluff water expenses in the other volume-related expense account that were actually fixed expenses belonging in the other plant maintenance account.
20. A \$1,148 expense for chlorine gas cylinders should be added to the other volume-related expense account for White Bluff water.

21. Double Diamond Utilities included \$530 of White Bluff sewer expenses in the other volume-related expenses account that were actually fixed expenses belonging in the other plant maintenance account.

**Employee Labor Expense—Known and Measurable Change**

22. Deleted.

22A. Double Diamond Utilities requested a total of \$171,960 in employee labor expenses for its White Bluff water and sewer systems. This amount reflects the test-year salaries for its employees.

22B. Seven employees worked for the White Bluff systems at some point during the test year; however, not all seven employees worked the entire test year.

22C. Between August 4, 2017 and October 24, 2017, there were only four employees working for the White Bluff systems.

22D. The seven employees who worked for the White Bluff utility systems during the test year earned and were paid \$151,074 in salary during the test year; they did not earn and were not paid their full yearly salaries.

**Employee Labor Expense—Salaries of Mr. Whitworth and Mr. Keeton**

23. Deleted.

23A. Included in the \$151,074 Double Diamond Utilities requested for employee labor expenses for its White Bluff systems was \$20,800 for the salary of Jerry Whitworth and \$22,880 for the salary of Danny Keeton.

23B. The record reflects that Mr. Whitworth and Mr. Keeton were backhoe operators that were involved in all tap installations, but only spent a small proportion of time installing taps.

23C. Mr. Whitworth and Mr. Keeton spent their other remaining time performing other duties as needed.

23D. Double Diamond Utilities did not provide any evidence explaining or detailing what these other duties entail, whether any of these duties related to utility matters or the provision of utility service, or the amount of time spent working on utility matters.

- 23E. Double Diamond Utilities presented no evidence on whether any of these other duties required skill operating a backhoe, why Double Diamond Utilities needs more than one full-time backhoe operator, the market-salary rate for a backhoe and equipment operator, or the experience and skill level of these employees.
- 23F. There are no work orders, time sheets, or other evidence that would explain how Mr. Whitworth and Mr. Keeton spend the majority of their time completing other duties as necessary, the amount of time Mr. Whitworth and Mr. Keeton worked on either system, if any, or even what system they worked on, or even if they worked on either system.
- 23G. The only other evidence in the record regarding the job duties of Mr. Whitworth and Mr. Keeton is Double Diamond Utilities' witness Mr. Gracy's one-sentence statement that all employees are cross-trained in both water and sewer operations to work at both systems.
- 23H. A conclusory statement that Mr. Whitworth and Mr. Keeton spent an unspecified amount of time on other duties as needed does not show that these costs are related to the provision of utility service or that the costs are reasonable and necessary.
- 23I. Mr. Gracy's statement that all employees are cross-trained to work on both systems does not provide any explanation as to what specific tasks the employees completed or whether these tasks required the operation of a backhoe.
- 23J. The fact that a person was cross-trained to work on either system does not show that the person actually worked on a system.
- 23K. Aside from tap installations, Double Diamond Utilities has not shown that Mr. Whitworth and Mr. Keeton worked on any matter related to providing water and sewer service to its customers.
- 23L. Under Double Diamond Utilities' tariffs, customers are required to pay a charge to recover the cost of utility taps.
- 23M. The costs related to tap installations are recovered from customers from tap fees and should be removed from Double Diamond Utilities' cost of service.
- 23N. It is appropriate to remove the \$20,800 salary of Mr. Whitworth and the \$22,880 salary of Mr. Keeton from Double Diamond Utilities' cost of service.

- 23O. Double Diamond Utilities allocated the salaries of its employees evenly between the water and sewer systems, with the exception of one employee Clovis Wilhelm. Therefore, it is appropriate to allocate the removal of the salaries of Mr. Whitworth and Mr. Keeton evenly between the White Bluff water and sewer systems.
- 23P. Double Diamond Utilities' total employee labor expense that may be included in base rates is \$107,394.
- 23Q. Employee salaries totaling \$107,394 are reasonable and necessary expenses for Double Diamond Utilities to provide services to the White Bluff systems.
24. Deleted.
25. Deleted.
26. Deleted.
- 26A. With one exception, Double Diamond Utilities allocated the salaries of its employees evenly between the water and sewer systems because it claims its employees are cross-trained in both water and sewer operations and work between the water and sewer systems.
- 26B. The salary of Clovis Wilhelm was allocated 25% to the White Bluff water system and 75% to the White Bluff sewer system.
- 26C. The allocations of the \$171,960 in employee labor expenses resulted in expenses of \$80,520 for the White Bluff water system and \$91,440 for the White Bluff sewer system. These numbers do not reflect the disallowances of Mr. Whitworth and Mr. Keeton.
- 26D. Double Diamond Utilities did not provide any evidence on the amount of time each employee spent working on each system or even which system the employee worked on.
- 26E. The fact that all employees are cross-trained to work on both utilities does not mean that each employee worked on both utilities, or if they did, that their time was split evenly between the two systems.
- 26F. Given the absence of actual time records for the employees, the better approach is to allocate the employee salaries based on the type of license held by each employee and their actual job duties.

- 26G. Rates for each system must be set at a level that corresponds to each system's cost of service and must be based on the amount of time an employee actually spends working on a system and providing service to that system's ratepayers.
- 26H. The allocation method adopted by this Commission in this Order best achieves those goals and conformance with statutory and regulatory requirements.

**Contract Work**

27. Todd Dilworth, the White Bluff utility manager for Double Diamond Utilities, is on call at all times to respond to service calls at the White Bluff water and sewer systems.
28. It is reasonable to have Mr. Dilworth on call at all times in case issues arise that affect service, and it is a reasonable expense to allow Mr. Dilworth to have a mobile phone with cell service so that there can be effective and efficient communication regarding any such issues.
29. Double Diamond Utilities' phone allowance of \$900 for 12 months for Mr. Dilworth is a reasonable and necessary expense incurred to provide water and sewer services at White Bluff.
30. A total of \$890 for White Bluff water and \$790 for White Bluff sewer in general and administrative expenses attributable to security at the White Bluff resort should be reallocated from miscellaneous expenses to contract work as intercompany labor transfers.

**Transportation**

31. Mr. Dilworth and another employee have Double Diamond Utilities vehicles that they can use to respond at any time to a service call at White Bluff.
32. Mr. Dilworth drives one of the trucks to and from work daily, and the other truck is used by the Double Diamond Utilities employee assigned to be on call to drive to and from work during such assignment.
33. Mr. Dilworth and the on-call Double Diamond Utilities employee do not use the trucks for any personal reasons. Although they use the trucks to drive to and from work, this use is reasonable and necessary so that they can respond to a service call from home if such a call is made.

34. The fuel costs incurred by Double Diamond Utilities for Mr. Dilworth and the other employee driving to and from work in company trucks while on-call are not purely commuter miles and are reasonable and necessary expenses incurred by Double Diamond Utilities in providing service at White Bluff.
35. A vehicle lease expense (\$2,912 for both the water and sewer systems) and a tool box expense for White Bluff of \$850 should be removed from transportation expenses and added to the depreciation schedule.

**Other Plant Maintenance**

- 35A. Double Diamond Utilities requested a total of \$142,010 in expenses for other plant maintenance at its White Bluff systems. This amount includes a request of \$79,590.73 for grinder-pump expenses for the White Bluff sewer system.
36. Grinder pumps are part of the White Bluff wastewater system and installed at each service location in the White Bluff system.
- 36A. Grinder pumps have a service life of about ten years.
37. There are significant, typical, and recurring maintenance, repair, and replacement costs associated with the grinder pumps in the White Bluff sewer system.
38. Approximately 20 to 30 grinder pumps are replaced and approximately half of the pumps are repaired every year in the White Bluff sewer system.
- 38A. Double Diamond Utilities asserted that it treats costs related to grinder pumps as recurring annual expenses because these costs recur from year-to-year and are a constant maintenance issue in the operation of the White Bluff sewer system.
- 38B. The expenses Double Diamond Utilities seeks to recover include the maintenance and repair of existing grinder pumps and the purchase of new grinder pumps.
- 38C. Whether a type of expense is typical and recurring is not determinative of whether an expense is an ordinary expense or a capital expense.
- 38D. In general, maintenance and repair expense to keep an asset in its current operating condition or restore it to its previous operating condition are an ordinary expense that

- should be recorded in an expense account and included in the operation and maintenance expense category in setting rates.
- 38E. While some repairs may be such that the usefulness or efficiency of the asset is so enhanced that the expense should be capitalized, the evidence in this case does not show that the maintenance and repair expenses sought by Double Diamond Utilities are of this type.
- 38F. Double Diamond Utilities should expense its grinder-pump repair costs totaling \$3,181.73 for the test year for White Bluff sewer.
- 38G. The cost of new grinder pumps to replace pumps that are no longer operational or as additional pumps to meet system needs should not be expensed.
- 38H. Based upon the ten-year life of the pumps, the cost of the pumps, and the use of the pumps, grinder pump replacements are properly recorded in utility plant asset accounts for equipment and should be treated as invested capital for rate-making purposes.
- 38I. Because capital investments have a useful life, only a portion of the investment is properly recorded in the current year and the utility recovers that amount through its depreciation expense over the life of the asset.
- 38J. NARUC accounting standards specify that costs associated with the installation of pumping equipment (such as grinder pumps) should be added to a specific account associated with utility plant and equipment.
- 38K. In accordance with NARUC standards, Double Diamond Utilities should capitalize the costs associated with new and replacement grinder pumps at the White Bluff sewer system.
- 38L. There is no evidence that the Commission has approved a deviation from the NARUC system of accounts for Double Diamond Utilities.
- 38M. Double Diamond Utilities should capitalize its grinder-pump replacement costs totaling \$76,409 for the test year for White Bluff sewer.
39. Deleted.
40. The \$709 included in the trial balance for the White Bluff water system reflects costs incurred in the operation and maintenance of the water system at White Bluff and is appropriately included as other plant maintenance expense.



41. Deleted.
42. The invoice from Industrial Electric Repair and Sales referencing rewind 3 phase, machine work on pump, and pump repair, and reflecting charges for bearings and a pump seal pertains to repairs, and the costs reflected in this invoice are appropriately designated as other plant maintenance expenses.
43. The invoice from Wallace Controls & Electric referring to a call regarding a well not running and reflecting a burned-out motor protector and service wire and a motor protector replacement pertains to repairs, and the costs reflected in this invoice are appropriately designated as other plant maintenance expenses.

**Professional Services**

44. The cost of renewing Double Diamond Utilities' wastewater permit for White Bluff, which Double Diamond Utilities has historically incurred approximately every three years, should be allowed to be recovered in equal parts in Double Diamond Utilities' rates over three years.
45. Deleted.
46. Deleted.
- 46A. Double Diamond Utilities requested professional-services expenses of \$2,907 for obtaining its CCN amendment to provide sewer service at The Cliffs.
- 46B. Double Diamond Utilities' cost of \$2,907 associated with its CCN amendment for The Cliffs system is not a recurring expense and should not be included in its revenue requirement.
47. Double Diamond Utilities did not incur any cost to obtain a CCN amendment for White Bluff during the test year, and the costs of such amendment reflected in the White Bluff professional services account should be removed.

**Insurance**

48. The premiums paid by Double Diamond Utilities for worker's compensation insurance (\$1,444 for water and \$373 for sewer) are not recoverable insurance expenses.

49. Some portion of the premium paid by Double Diamond Utilities for an umbrella insurance policy is attributable to insurance coverage that is incurred as part of providing service and maintaining plant.
50. The amount of the umbrella premium attributable to coverage for providing utility service and maintaining plant does not correlate to the base premium for such coverage.
51. Double Diamond Utilities failed to prove the cost of the umbrella coverage that relates to Double Diamond Utilities' provision of water and sewer utility service.

**Salaries**

52. Renumbered as 22B.
53. Renumbered as 22D.
54. Renumbered as 22C.
55. Renumbered as 23Q.

**Regulatory Fees**

56. The Prairieland Groundwater District fees paid by Double Diamond Utilities for White Bluff should not be included in Double Diamond Utilities' revenue requirement, but should be included as a pass-through provision in Double Diamond Utilities' tariff.
57. Double Diamond Utilities' expenses related to water tests that occur every three years should be normalized such that Double Diamond Utilities recovers one-third of the expenses every year.

**Miscellaneous Expenses**

58. Equipment lease fees of \$19,728 for White Bluff water and \$20,148 for White Bluff sewer associated with automatic meter reading and the 50,000 gallon wastewater treatment plant should be removed from the miscellaneous expense accounts.
59. Sewer-tap-fee expenses of \$500 should be removed from the White Bluff sewer miscellaneous expense account.
60. Double Diamond Utilities' utility offices are located within the White Bluff and The Cliffs resorts' administrative buildings.
61. Deleted.

62. Deleted.
63. Deleted.
64. Deleted.
65. Deleted.
- 65A. Double Diamond Utilities requested total miscellaneous expenses of \$55,685 for its White Bluff systems and \$41,113 for its systems at The Cliffs. These requested amounts include expenses incurred by Double Diamond Utilities for resort overhead expenses billed from the White Bluff and The Cliffs resorts to the water and sewer systems at White Bluff and The Cliffs.
- 65B. The entities that own and operate the resorts are wholly-owned subsidiaries of Double Diamond-Delaware.
- 65C. Because the utility offices are located within the resorts' administrative buildings, the utility uses some of the resorts' resources, and is then billed by the resorts for the resources used.
- 65D. The expenses billed by the resorts to the utility systems include expenses related to the general manager and office manager at the resorts, employee compensation (including commissions and bonuses), payroll expenses, electricity, water and sewer, office space, phones, computers, copiers, uniforms, and small tools.
- 65E. The utility systems are billed a total of 3% of all overhead and general and administrative expenses incurred by each resort.
- 65F. The amounts billed to Double Diamond Utilities are not based on the Double Diamond Utilities' actual share of resort expenses that it directly uses; instead, it is an across-the-board charge of 3% of all overhead and general and administrative expenses incurred by the resort.
- 65G. The record reflects that the amount of resort overhead expenses billed to the White Bluff systems and The Cliffs systems includes the cost of items unrelated to the provision of utility service.

- 65H. Resort expenses, such as advertising for the resort, commissions and bonuses for resort employees, or uniforms for resort employees, cannot be allocated to the utility because these items are not used to utility services.
- 65I. Double Diamond Utilities' witness Mr. Gracy confirmed that some expenses included in the 3% charge are not used by the utility.
- 65J. Double Diamond Utilities provided no evidence regarding the amount of time amenities and resources were used at the resort buildings, or whether the amenities and resources were used for utility purposes, if at all.
- 65K. The record does not contain any work orders, time sheets, or other evidence that identify the amount of time the general manager and office manager spend working on utility matters, if any.
- 65L. No evidence was admitted showing what other entities or persons would pay the resorts for the same class of comparable amenities.
- 65M. No evidence was admitted establishing the market price for the same class of items provided to the systems.
- 65N. It is appropriate to remove \$8,380 for water and \$6,068 for sewer from White Bluff's requested miscellaneous expenses, and \$20,075 for water and \$18,270 for sewer from The Cliffs requested miscellaneous expenses.
66. Deleted.
67. Deleted.

**Depreciation Expense**

68. The \$80 expense for a truck bed mat should be removed from the White Bluff sewer depreciation schedule.

**Depreciation—Known and Measurable Changes**

68A. In its application, Double Diamond Utilities requested the following depreciation expenses for each of its four systems:

<b>Double Diamond Utilities' Requested Depreciation Expense</b>				
	<u>White Bluff</u>	<u>White Bluff</u>	<u>The Cliffs</u>	<u>The Cliffs</u>
	<u>Water</u>	<u>Sewer</u>	<u>Water</u>	<u>Sewer</u>
Test year (2015)	\$78,805	\$69,816	\$45,823	\$38,159
Known and Measurable Changes	\$31,272	\$14,884	\$32,620	(\$8,896)
<b>Adjusted Test Year Depreciation Expense</b>	<b>\$110,077</b>	<b>\$84,700</b>	<b>\$78,443</b>	<b>\$29,263</b>

68B. The known and measurable changes requested by Double Diamond Utilities reflects the difference between the value shown on Double Diamond Utilities' books and the trending study performed by Ms. Harkins.

68C. Double Diamond Utilities did not show that there were any known and measurable changes to the test-year depreciation expenses.

68D. The requested known and measurable changes in the amount of \$69,880 should be removed from Double Diamond Utilities' depreciation expense.

68E. Double Diamond Utilities' appropriate depreciation expenses are \$78,805 for the White Bluff water system, \$69,816 for the White Bluff sewer system, \$45,823 for The Cliff's water system, and \$38,159 for The Cliff's sewer system.

**Depreciation—Use of Trending Study to Determine Original Cost**

69. Double Diamond Utilities retained Victoria Harkins to perform an analysis of the utility assets at White Bluff and The Cliffs and determine the original cost of such assets.

70. To perform her analysis, Ms. Harkins looked only at invoices provided to her by Double Diamond Utilities for the utility assets and did not review any balance sheets or general ledgers.
71. The invoices reviewed by Ms. Harkins for purposes of determining the original cost of utility assets did not reflect the entirety of the pipe work for the White Bluff and The Cliffs systems.
72. Ms. Harkins performed a trending study to establish the original cost for certain White Bluff and The Cliffs assets for which no invoice was available.
73. Double Diamond Utilities' chief financial officer testified that the costs of Double Diamond Utilities' utility infrastructure are recorded in a balance sheet based on invoices for such expenses and he had no reason to doubt the book values for those assets.
- 73A. Ms. Harkins did not review the balance sheet or general ledgers of Double Diamond Utilities.
- 73B. Ms. Harkins testified that if she had reviewed the balance sheet and general ledges, and had those numbers been less than the costs she developed in her trending study, she would have used the balance sheet numbers.
74. The record is not clear on what historical records exist (or existed at the time the application was prepared) showing the original construction costs for the collection and distribution lines at White Bluff and The Cliffs.
- 74A. There were historical records available to verify the original costs of the collection and distribution lines at White Bluff and The Cliffs.
- 74B. It is not appropriate to use a trending study to establish the original cost of Double Diamond Utilities' assets; it is appropriate to use the test-year book values.
75. Deleted
76. Deleted.
77. Deleted.

**Depreciation—Fully Depreciated Assets**

78. All assets that have fully depreciated should be removed from Double Diamond Utilities' White Bluff depreciation schedules, as set forth in Tables NDH-14, NDH-15, NDH-16, and NDH-17 of the direct testimony of the White Bluff Ratepayers Group witness Nelisa Heddin.

**Federal Income Tax Expense**

79. Treating White Bluff and The Cliffs as separate entities when calculating federal income tax expense is not appropriate.

79A. The White Bluff and The Cliffs systems are both owned and operated by Double Diamond Utilities. Double Diamond Utilities is a subchapter S corporation, a pass-through entity.

79B. Double Diamond-Delaware is a subchapter S corporation.

79C. Double Diamond-Delaware is the parent company and sole shareholder of Double Diamond Utilities.

79D. R. Mike Ward is the majority shareholder of Double Diamond-Delaware, owner of 94.8% of the shares with an employee stock ownership plan owning 5.2%.

79E. Because Double Diamond-Delaware is also a subchapter S corporation, it is likely that the majority of tax expenses of Double Diamond Utilities are paid at the individual level by Mr. Ward, the majority shareholder of Double Diamond-Delaware.

79F. The record does not reflect what amount of Double Diamond Utilities' tax expense is paid by Mr. Ward or the applicable tax rate.

79G. It is appropriate to treat Double Diamond Utilities as a subchapter C corporation for the purpose of determining its federal income tax expense.

79H. A subchapter C corporation's applicable federal income tax rate is 21% for ratemaking purposes.

**Other Assessments and Taxes**

80. The sales and title taxes for the 2014 Ford truck are included in the asset depreciation schedule and therefore should be removed from taxes.

**Rate Base**

80A. The invested capital or rate base for is the White Bluff water system is:

Item	Amount
Plant in service – original cost	\$501,345
Accumulated depreciation	(\$223,113)
<b>Net plant in Service</b>	<b>\$278,232</b>
Working cash allowance	\$20,283
Developer contribution in aid of construction	(\$209,877)
ADFIT	(\$327,979)
<b>Total invested capital (rate base)</b>	<b>(\$239,341)</b>

80B. The invested capital or rate base for the White Bluff sewer system is:

Item	Amount
Plant in service – original cost	\$199,414
Accumulated depreciation	(\$45,105)
<b>Net plant in Service</b>	<b>\$154,308</b>
Working cash allowance	\$11,283
Developer contribution in aid of construction	(\$55,780)
ADFIT	(\$31,375)
<b>Total invested capital (rate base)</b>	<b>\$78,436</b>



80C. The invested capital or rate base for The Cliffs water system is:

Item	Amount
Plant in service – original cost	\$1,612,546
Accumulated depreciation	(\$826,559)
<b>Net plant in Service</b>	<b>\$785,987</b>
Working cash allowance	\$22,173
Developer contribution in aid of construction	(\$248,421)
ADFIT	(\$39,859)
<b>Total invested capital (rate base)</b>	<b>\$519,880</b>

80D. The invested capital or rate base for The Cliffs sewer system is:

Item	Amount
Plant in service – original cost	\$1,017,635
Accumulated depreciation	(\$442,907)
<b>Net plant in Service</b>	<b>\$574,728</b>
Working cash allowance	\$17,693
Developer contribution in aid of construction	(\$71,898)
ADFIT	(\$9,495)
<b>Total invested capital (rate base)</b>	<b>\$511,028</b>

**Corrections to Original Cost of Plant In Service**

81. The correct original cost of a 75,000 gallon gst, field erect with pad and 75,000 gallon gan, field erect mth pad is \$16,565, and the water depreciation schedule for The Cliffs system should be revised accordingly.

82. The original cost of the TK Crossbed Toolbox set forth on the White Bluff sewer depreciation schedule should be revised to \$850 to remove an \$80 expense for a truck bed mat that was also included in White Bluff's cost of service.

**Cash Working Capital**

83. A reasonable cash working capital allowance for the White Bluff utility system is 1/12 of the system's operation and maintenance expenses.
84. Double Diamond Utilities maintains cash balances for both White Bluff and The Cliffs systems under one CCN, filed one annual report for both developments, and filed a single rate case for both developments.
85. Both the White Bluff and The Cliffs systems are operated and maintained by Double Diamond Utilities and have access to the same capital.
86. A reasonable cash working capital allowance for The Cliffs utility system is 1/12 of the system's operation and maintenance expenses.

**Developer Contributions**

87. In determining the original cost of used and useful utility plant, property, and equipment for purposes of calculating its rate base, Double Diamond Utilities used an asset list prepared jointly by Double Diamond Utilities' president Randy Gracy and Double Diamond Utilities witness Ms. Harkins, which identifies certain assets to be 80% developer-contributed. The 80% portion of the cost of those assets was removed from Double Diamond Utilities' rate-base calculation.
- 87A. Double Diamond Utilities' identified developer contributions reduced its rate base amounts in its application by \$1,186,277 and \$137,457 for the White Bluffs water and sewer systems, respectively.
- 87B. Double Diamond Utilities erroneously applied its 80-20 split to the net book value of each asset—instead of applying the split to the original cost of each asset—thus, undercounting the amount of its developer-contributed costs.
- 87C. Double Diamond Utilities did not exist at the time the initial infrastructure at White Bluff was constructed,

- 87D. Double Diamond Utilities also applied its 80-20 split to the initial investment in the White Bluff systems even though Double Diamond Utilities did not exist at the time the initial infrastructure was constructed.
88. There is no contemporaneous accounting or other documentation showing that the assets on the asset list prepared by Mr. Gracy and Ms. Harkins were 80% developer-contributed.
89. Until December 1996, when Double Diamond Utilities was created, Double Diamond, Inc., another wholly-owned subsidiary of Double Diamond-Delaware, was the developer and the utility company at White Bluff and contracted for the construction of the original infrastructure of the White Bluff utility systems.
90. Before December 1996, most of the utility infrastructure was paid for by Double Diamond, Inc.
- 90A. All investments at White Bluff before December 30, 1996 are developer contributions.
- 90B. The net book value of the White Bluff water assets paid for by Double Diamond, Inc. is \$800.16.
- 90C. The net book value of the White Bluff sewer assets paid for by Double Diamond, Inc. is \$29.24.
91. In 1997, Double Diamond Properties Construction Co., also created in December 1996 as a wholly-owned subsidiary of Double Diamond-Delaware, began paying for most of the utility infrastructure.
92. Approximately 61% of the water system assets and 60% of the sewer system assets included in Double Diamond Utilities' requested rate base for White Bluff were constructed before December 1996.
93. Most of the White Bluff assets included in Double Diamond Utilities' requested rate base for White Bluff that were constructed after December 1996 were paid for by Double Diamond Properties Construction Co.
- 93A. The original cost of the White Bluff water assets paid for by Double Diamond Properties Construction Co. and Double Diamond Inc. is \$429,977.60

- 93B. The net book value of the White Bluff water assets paid for by Double Diamond Properties Construction Co. and Double Diamond Inc. is \$209,877.60.
- 93C. The accumulated depreciation amount for the developer-contributed assets for the White Bluff water system is \$220,101.
- 93D. The original cost of the White Bluff sewer assets paid for by Double Diamond Properties Construction Co. and Double Diamond Inc. is \$97,380.40.
- 93E. The net book value of the White Bluff sewer assets paid for by Double Diamond Properties Construction Co. and Double Diamond Inc. is \$55,780.04.
- 93F. The accumulated depreciation amount for the developer-contributed assets for the White Bluff sewer system is \$41,600.
- 93G. There is no documentation to determine who paid for 118 assets at White Bluff water. The net book value of these assets is \$579,996.75
- 93H. There is no documentation to determine who paid for 97 assets at White Bluff sewer. The net book value of these assets is \$585,296.01.
- 93I. The majority of White Bluff assets constructed after December 30, 1996 are developer contributions.
- 94. In December 1997, Double Diamond Utilities filed an application to change rates at White Bluff, The Cliffs, and Oakwood, another development that it serves. In that filing, there were no contributions in aid of construction identified.
- 95. In August 2007, Double Diamond Utilities filed an application to change water rates at White Bluff, The Cliffs, and the Retreat, another development that it serves. The application was amended in December 2007, but neither the August 2007 nor the December 2007 amendment indicated that a portion of Double Diamond Utilities' assets included in rate base was developer contributed.
- 96. In October 2008, Double Diamond Utilities filed another rate change application for the water systems at White Bluff, The Cliffs, and the Retreat, which identified the amount of developer contributions as approximately \$1.9 million.

97. In February 2009, Double Diamond Utilities filed another rate change application for the water systems at White Bluff, The Cliffs, and the Retreat, and the application indicated a total of \$1,119,399 in developer contributions for the three systems.
98. Deleted.
99. Double Diamond Utilities is in the best position to access and discover the evidence necessary to differentiate between plant, equipment, and property contributed by the developer and that invested by Double Diamond Utilities.
100. The net book value of the seven utility assets claimed as part of Double Diamond Utilities' rate base and paid for by Double Diamond Utilities are properly included in Double Diamond Utilities' invested capital.
- 100A. The original cost for the applicable White Bluff water assets is \$71,367.48.
- 100B. The net book value that should remain in invested capital for White Bluff water is \$68,355.48.
- 100C. The original cost for the applicable White Bluff sewer assets is \$25,624.64,
- 100D. The net book value that should remain in invested capital for White Bluff sewer is \$24,029.64.
101. Tract 2 in White Bluff was conveyed by Double Diamond, Inc. to the White Bluff Property Owners Association in December 1995, as well as certain facilities included on such tract, including a water well, the water plant, and the water storage tank.
102. Double Diamond Utilities' request for the net book value of Tract 2 and the facilities on Tract 2 of \$88,565 and an annual depreciation of \$2,060 to be included in its rate base should be denied.

**Developer Contribution - Used and Useful**

103. The White Bluff systems serve 6,314 lots.
104. There are approximately 65 miles of water lines and 60 miles of sewer lines at White Bluff.
105. Only approximately 10% of the lots at White Bluff development are actually receiving service from Double Diamond Utilities.

105A. The White Bluff water and sewer systems were built in phases as the White Bluff subdivision developed. As new sections of development were opened, the distribution lines for new sections were installed and connected back to the original systems.

106. Approximately 85 to 90% of the lots at White Bluff have been sold.

107. Deleted.

107A. The developer-contributed assets at White Bluff are currently used to serve residents and are available to serve any new residents.

**Accumulated Deferred Federal Income Tax (ADFIT)**

108. There is no accounting evidence that Double Diamond Utilities incurred a net operating loss or documentary proof in the record that Double Diamond Utilities did not defer payment of federal income taxes because of a net operating loss.

109. The estimate of the effect of the alleged net operating loss carryover on the ADFIT calculated by Commission Staff witness Debi Loockerman was unsupported.

**Rate of Return**

**Return on Equity**

110. A reasonable return on equity for Double Diamond Utilities, based on a discounted cash flow analysis employed with the capital asset pricing model is 8.79%.

110A. The discounted cash flow model is widely accepted by the regulatory industry and the Commission, and is often used to calculate the appropriate return on equity for a utility.

111. A return on equity of 8.79% is reasonably sufficient to assure confidence in Double Diamond Utilities' financial soundness and will be adequate to maintain and support its credit and allow it to raise necessary capital.

112. A return on equity of 8.79% will yield a fair return on Double Diamond Utilities' invested capital.

113. Deleted.

114. A small stock risk premium on top of Double Diamond Utilities' return on equity is not warranted.

- 114A. A small stock risk premium is not appropriate for water and sewer monopolies because water and sewer utilities are subject to regulatory oversight and a utility's earnings are set by the ratemaking process.
- 114B. It is unclear from Double Diamond witness Mr. Scheig's testimony how he determined that the return on equity for Double Diamond Utilities should include a small stock risk premium.
115. Approximately 40% of the unaccounted for water noted in the application is water loss due to brine discharge after water from the lake goes through a reverse osmosis plant, and thousands of gallons a day used to backwash sand filters.
116. Additional water is used to regularly flush out the lines at White Bluff and The Cliffs and is therefore unaccounted for.
117. Double Diamond Utilities employs various methods at The Cliffs to track down leaks, and Double Diamond Utilities has responded to and repaired, discovered, and reported leaks in a reasonable manner.
118. The utility crew at The Cliffs is instructed to respond to reports of leaks as quickly as possible and make the necessary repairs. Some leaks can be fixed in a few hours, and most leaks are repaired the same day or the day after they are reported.
119. Deleted.

**Cost of Debt**

120. A 4.91% cost of debt, which is Double Diamond-Delaware's overall weighted average cost of debt as of December 31, 2015, is an appropriate cost of Double Diamond Utilities' debt.

**Capital Structure**

121. Double Diamond Utilities took out a \$3 million loan secured by White Bluff utility assets, the proceeds of which Double Diamond-Delaware used to make capital improvements and for other purposes. Double Diamond-Delaware guaranteed repayment of the debt.
122. It is unclear how the \$3 million proceeds of the loan were accounted for.

- 123. Double Diamond, Inc. has been making the payments on the loan; if Double Diamond, Inc. did not make those payments and there was a default, the bank would look to Double Diamond-Delaware as guarantor, and not Double Diamond Utilities, for payment.
- 124. The \$3 million loan is not related to Double Diamond Utilities' debt financing and therefore cannot serve as the basis for the capital structure recommended by the White Bluff Ratepayers Group.
- 125. The appropriate capital structure for Double Diamond Utilities is 47.27% debt and 52.73% equity, which is representative of the capital structure of other companies in the water utility industry and reflects an efficient use of capital.

**Overall Rate of Return**

- 126. Double Diamond Utilities' overall rate of return should be set as follows:

<b>Component</b>	<b>Ratio</b>	<b>Cost Rate</b>	<b>Weighted Cost Rate</b>
<b>Debt</b>	47.27%	4.91%	2.32%
<b>Equity</b>	52.73%	8.79%	4.63%
<b>Overall</b>			6.95%

**Revenue Requirement - White Bluff Water**

- 126A. Double Diamond Utilities' revenue requirement used to set rates for White Bluff water is \$310,868.
- 126B. Double Diamond Utilities' recoverable test year operation and maintenance expense for White Bluff water is \$243,393.
- 126C. Double Diamond Utilities' recoverable test year depreciation and amortization expense for White Bluff water is \$13,507.
- 126D. Double Diamond Utilities' recoverable test year taxes other than income for White Bluff water is \$62,731.
- 126E. Double Diamond Utilities' return on invested capital for White Bluff water is \$0.



**Revenue Requirement - White Bluff Sewer**

- 126F. Double Diamond Utilities' revenue requirement used to set rates for White Bluff sewer is \$196,032.
- 126G. Double Diamond Utilities' recoverable test year operation and maintenance expense for White Bluff sewer is \$135,395.
- 126H. Double Diamond Utilities' recoverable test year depreciation and amortization expense for White Bluff sewer is \$6,586.
- 126I. Double Diamond Utilities' recoverable test year taxes other than income for White Bluff sewer is \$52,209.
- 126J. Double Diamond Utilities' return on invested capital for White Bluff sewer is \$5,451.

**Revenue Requirement - The Cliffs Water**

- 126K. Double Diamond Utilities' revenue requirement used to set rates for The Cliffs water system is \$358,088.
- 126L. Double Diamond Utilities' recoverable test year operation and maintenance expense for The Cliffs water is \$266,075.
- 126M. Double Diamond Utilities' recoverable test year depreciation and amortization expense for The Cliffs water is \$45,823.
- 126N. Double Diamond Utilities' recoverable test year taxes other than income for The Cliffs water is \$9,859.
- 126O. Double Diamond Utilities' return on invested capital for The Cliffs water is \$36,184.

**Revenue Requirement - The Cliffs Sewer**

- 126P. Double Diamond Utilities' revenue requirement used to set rates for The Cliffs sewer system is \$296,017.
- 126Q. Double Diamond Utilities' recoverable test year operation and maintenance expense for The Cliffs sewer is \$212,311.
- 126R. Double Diamond Utilities' recoverable test year depreciation and amortization expense for The Cliffs sewer is \$38,150.

126S. Double Diamond Utilities' recoverable test year taxes other than income for The Cliffs sewer is \$9,409.

126T. Double Diamond Utilities' return on invested capital for The Cliffs sewer is \$35,568.

**Rate Design**

127. The rate structures set forth in the tariffs filed on October 2, 2019, will recover Double Diamond Utilities' revenue requirements for White Bluff water and White Bluff sewer systems.

128. The rate structures set forth in the tariffs filed on October 2, 2019 will recover Double Diamond Utilities' revenue requirement for The Cliffs water and The Cliffs sewer systems.

**Tariffs**

129. On April 26, 2017, Double Diamond Utilities filed substitute pages for its water tariffs for its water system at White Bluff and The Cliffs to correct errors contained in the water tariffs filed with its application on August 1, 2016.

130. On August 29, 2018, Commission Staff filed its first set of updated tariffs for the White Bluff water and sewer systems and The Cliffs water and sewer system to reflect the rates generated by Commission Staff's number run, filed May 21, 2018, reflecting the decisions of the Commission at the May 10, 2018 open meeting.

131. On October 31, 2018, Commission Staff filed its second set of updated tariffs for the White Bluff water and sewer systems and The Cliffs water and sewer system to reflect the decisions described in the Commission's first final order, filed on August 30, 2018, and the discussion of the Commission at the October 25, 2018 open meeting.

132. On October 2, 2019, Commission Staff filed its third set of updated tariffs for the White Bluff water and sewer systems and The Cliffs water and sewer systems to reflect the decisions described in the Commission's first final order, filed on August 30, 2018, and the discussion of the Commission at the September 12, 2019 open meetings.

**III. Conclusions of Law**

1. Double Diamond Utilities is a utility and a public utility as defined in TWC § 13.002(23), and a retail public utility as defined in TWC § 13.002(19).

- 1A. Double Diamond Utilities is a class B utility as defined in TWC § 13.002(4-b).
2. The Commission has jurisdiction over the application under TWC §§ 13.041, 13.043(b), 13.181–.185, 13.1871, and 13.1872.
3. All required notices of the application and the contested case hearing were given as required by law in TWC § 13.1871 and Administrative Procedure Act<sup>150</sup> §§ 2001.051 through 2001.052.
4. The ALJ conducted a contested case hearing and proposed a decision on the application under the authority of chapter 2003 of the Texas Government Code and chapter 13 of the TWC.
- 4A. Double Diamond Utilities is required to maintain a uniform system of accounts in the manner and form prescribed by the Commission and to keep books, accounts, and other records accurately and faithfully. TWC § 13.131(e).
- 4B. Double Diamond Utilities is required to maintain its books and records in accordance with the uniform system of accounts adopted by the National Association of Regulatory Utility Commissioners, and to keep its books on a monthly basis so that for each month all transactions applicable thereto shall be entered into the books of the utility. 16 TAC § 24.127.
5. Double Diamond Utilities bears the burden of proof that its proposed rates are just and reasonable under TWC § 13.184(c).
- 5A. A utility may only include expenses that are reasonable and necessary to provide service to the ratepayers in its cost of service.
6. Deleted.
- 6A. Double Diamond Utilities did not meet its burden to show that the salaries for the positions held by Mr. Whitworth and Mr. Keeton are a reasonable and necessary expense for the provision of utility service.

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<sup>150</sup> Tex. Gov't Code Ann. §§ 2001.051–.052.

- 6B. Double Diamond Utilities did not meet its burden to show that use of a trending study was appropriate to establish the original cost of assets because historical records exist.
- 6C. The entities that own and operate the resorts are affiliates of Double Diamond Utilities under TWC § 13.002(2).
- 6D. The 3% charge of overhead and general and administrative expenses from the White Bluff and The Cliffs resorts to Double Diamond Utilities is an affiliate transaction under TWC § 13.185(e).
- 6E. Expenses paid from Double Diamond Utilities to the resorts are an affiliate payment under TWC § 13.185(e).
- 6F. Under TWC § 13.185(e), payments made to an affiliate may not be allowed either as capital cost or as expense except to the extent the Commission finds the payment to be reasonable and necessary.
- 6G. The record contains no evidence to permit the Commission to make findings setting forth the cost of each item to the affiliate, or findings that the price to the utility is no higher than prices charged by the affiliate to its other affiliates, or to unaffiliated persons or corporations in accordance with TWC § 13.185(e).
- 6H. The Commission may not include costs related to affiliate transactions in Double Diamond Utilities' rates based on the record in this docket.
- 7. Deleted.
- 8. Double Diamond Utilities failed to meet its burden to show how much of the original cost of the utility assets included in its proposed rate base for White Bluff were contributed by the utility under TWC § 13.184(c).
- 8A. All investments at White Bluff before December 30, 1996 are developer contributions.
- 8B. The majority of White Bluff assets constructed after December 30, 1996 are developer contributions.
- 8C. Double Diamond Utilities' developer contribution at White Bluff is currently used and useful.

- 8D. Double Diamond Utilities is permitted to recover a depreciation expense on its used and useful developer-contributed assets at White Bluff in accordance with TWC § 13.185(j).
9. In compliance with TWC § 13.183, and based on the findings of fact and conclusions of law, Double Diamond Utilities' overall revenues approved in this case permit Double Diamond Utilities a reasonable opportunity to earn a reasonable return on its invested capital used and useful in providing service to the public over and above its reasonable and necessary operating expenses.
10. An overall rate of return of 6.95% will permit Double Diamond Utilities a reasonable opportunity to earn a reasonable return on its invested capital in accordance with TWC § 13.184.
11. The rates approved in this Order are based on original cost, less depreciation, of property used and useful to Double Diamond Utilities' provision of service in accordance with TWC § 13.185.
12. The rates approved in this Order are just and reasonable, comply with the ratemaking provisions in TWC chapter 13, and are not unreasonably discriminatory, preferential, or prejudicial.
13. The increase in revenue that would have been generated by Double Diamond Utilities' proposed rates should be calculated using the proposed rates from the amended application, which were those upon which a contested hearing was held under 16 TAC § 24.33(b).

#### **IV. Ordering Paragraphs**

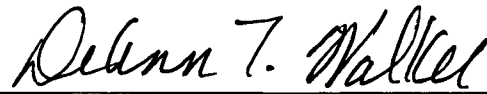
In accordance with these findings of fact and conclusions of law, the Commission issues the following orders:

1. The Commission adopts the proposal for decision as corrected and clarified, including findings of fact and conclusions of law, except as discussed in this Order.
2. Double Diamond Utilities' application for a rate increase at White Bluff and The Cliffs is approved, as amended by the proposal for decision and this Order.

3. Double Diamond Utilities must record its excess accumulated deferred federal income tax in a regulatory liability account for return to customers in Double Diamond Utilities' next base-rate case.
4. The Commission approves the tariffs filed on October 2, 2019.
5. Within 10 days of the issuance of this Order, Commission Staff must file a clean copy of Double Diamond Utilities' tariffs with Central Records to be marked *Approved* and kept in the Commission's tariff book.
6. Double Diamond Utilities must refund the amount by which the current rates exceeded rates approved by this Order for the time period between February 21, 2018, and the date the rates approved in this Order become effective. The refund must be made over the same time period in which the rates have been charged. Refunds related to Double Diamond Utilities' application in this docket must be implemented in Docket No. 48916, *Compliance Docket Related to Refunds and Surcharges in Docket No. 46245*.
7. Double Diamond Utilities must surcharge the amount by which the current rates did not meet the rates approved by this Order for the time period between February 21, 2018, and the date the rates approved in this Order become effective. The surcharge must be made over the same time period in which the rates have been charged. Surcharges related to Double Diamond Utilities' application in this docket must be implemented in Docket No. 48916, *Compliance Docket Related to Refunds and Surcharges in Docket No. 46245*.
8. Double Diamond Utilities must begin maintaining its records in accordance with the NARUC Uniform System of Accounts and record items related to its water system separately from items related to its sewer systems and that identify items related to each resort.
9. All other motions and any other requests for general or specific relief, if not expressly granted, are denied.

Signed at Austin, Texas the 12<sup>th</sup> day of December 2019.

**PUBLIC UTILITY COMMISSION OF TEXAS**




DEANN T. WALKER, CHAIRMAN



ARTHUR C. D'ANDREA, COMMISSIONER

I respectfully abstain.



SHELLY BOTKIN, COMMISSIONER