Water Supply Practices (7th ed. 2017) dealing with General Fund Transfer (GFT), and an excerpt from the Decision of the Texas Water Commission in 1989, also dealing with GFT.[1] Copies of the excerpts I referenced in the M1 Manual of Water Supply I are provided as Attachment DW-5 to this testimony. I was afforded pertinent information from AW on test year results of calculations of Debt Service Coverage (DSC).

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. In my testimony, I will demonstrate that in the Order in Docket No. 42857, the removal of the GFT from wholesale water and wastewater rates had an unintended consequence of reducing net revenues and therefore lowering the DSC provided by wholesale rates. I will show that it is both reasonable and necessary to include in rates additional revenues in order to prevent subsidies between the various classes of customers served by AW as well as affording AW a rate of return on its invested capital that is usual and ordinary for a provider of water services. These additional revenues after Docket No. 42857 rates were implemented would have prevented AW from having an insufficient revenue requirement and afforded AW equal or near equal DSC for all customer classes.

Q. WILL YOU ALSO BE ADDRESSING OTHER IMPORTANT ASPECTS OF DSC IN YOUR TESTIMONY?

A. Yes. I will show that there is an inherent risk to Austin residents when revenue bonds are sold for AW, and that this risk should not occur without some return for those

[1] American Water Works Association, M1 Manual of Water Supply Practices, *Principles of Water Rates, Fees, and Charges* (7th ed. 2017).

residents. I will also show that the wholesale rates with a GFT included would have provided some of the cash for DSC, and without the GFT the wholesale customers did not provide their appropriate share of DSC.

Q. WILL YOU BE ADDRESSING THE LACK OF DEBT SERVICE COVERAGE PRODUCED BY CURRENT WHOLESALE REVENUES?

A. Yes. I will show that the decision in Docket No. 42857 kept AW from having the ability to receive adequate revenues from its wholesale customers to obtain a DSC ratio equal to that provided by AW's retail customers. Thus, the retail customers have subsidized the wholesale customers. This outcome may not have been intended by the decision in Docket No. 42857.

III. OVERVIEW OF AUSTIN WATER

Q. WHAT ARE THE IMPORTANT FACTS ABOUT AUSTIN WATER WITH RESPECT TO YOUR TESTIMONY?

A. Austin Water is a municipal corporation with the responsibility to serve approximately 255,000 retail customers in Travis County with water and wastewater services. AW also serves ten wholesale customers with wastewater services, and sixteen with water services. For those wholesale customers, AW does the long-range planning to have sufficient resources to serve its customer base as well as carry out the operation and maintenance of its systems on a day-to-day basis. It relies upon other City departments to complete these functions, such as billing services provided by Austin Energy. AW operates three water treatment plants and two wastewater treatment plants, which, along with the pressure system for water and a collection system for wastewater, require constant monitoring, maintenance, and planning. AW must also expand the systems to meet the needs of the growing communities. This expansion requires the

planning for capital investment and the sale of revenue bonds. Both of these activities entail financial planning and the ability to collect necessary revenues through rates. No part of this endeavor can be easily or perfectly forecast.

Q. IS AUSTIN WATER ONE OF SEVERAL DEPARTMENTS IN THE CITY OF AUSTIN?

A. Yes. AW is one of about twenty-five departments within the City. AW relies on many of these departments to complete its mission of serving the water and wastewater customers of AW. For instance, it relies upon the billing services provided by Austin Energy to bill and receive payments for its services. AW utilizes Financial Services to sell bonds and keep its accounting records. It uses Purchasing to buy the material it needs for operations and maintenance. By having many departments share support services, the City reaches high economies of scale with resultant savings that it passes along to all of its customers.

Q. IS THE REQUIREMENT TO PROVIDE ADEQUATE WATER RESOURCES A DIFFICULT ONE?

A. Yes. The State of Texas has experienced a steady population growth for decades. The goal of municipalities to ensure adequate water resources into the future is a daunting one. AW has worked with water planning entities within the State to ensure that the customers of AW can have the water they will need. Water is life itself, so this task is both essential and difficult. In procuring the needs of the future, there is risk both in procuring more resources than necessary and in not procuring enough. AW has taken this responsibility very seriously.

Q. ARE THERE ALSO CHALLENGES IN PROVIDING WASTEWATER SERVICES?

A. Yes. Regulatory agencies, both State and Federal, are continually updating and changing the requirements for discharging water into rivers and streams, and for the disposal of sludge. AW must make operational changes and capital expenditures in order to comply. These continual changes, which represent cost increases in many instances, must be covered by rate changes to ensure adequate cash flow. All of this is occurring in an economic climate that has allowed Travis County and the counties around it to grow rapidly.

IV. RATE OF RETURN IN MOU CONTEXT

Q. HAS THE COMMISSION HAD REASON TO CONSIDER WHETHER ELECTRIC MUNICIPALLY-OWNED UTILITIES (MOUS) SHOULD BE PERMITTED A RETURN ON THEIR INVESTMENT, OR ITS EQUIVALENT?

A. Yes, it has. A number of municipal utilities participate in the ERCOT transmission cost recovery regime established by the Commission.

Q. ARE MUNICIPAL ELECTRIC TRANSMISSION OWNERS ALLOWED A RATE OF RETURN IN THEIR TRANSMISSION COST OF SERVICE?

A. Yes, they are. When the Commission created the design for transmission rates in 1996 it included a rate of return for all transmission owners. Over the course of the next seven years the final form of the rate design was vetted at the Commission and in the courts. Ultimately, municipal electric transmission owners were allowed a return, or its equivalent, on their prudently invested capital. The calculation of the rate of return is based on the municipality's DSC. For more than fifteen years now, Austin Energy

and all other municipal transmission owners, have earned a rate of return from all of the electric transmission customers in ERCOT.

Q. IS THE RATE OF RETURN MONITORED IN ANY WAY TO SEE HOW THE INCOME IS USED?

A. No. The transmission owner is allowed to use the return for operating cash, dividends, capital expenditures, salary enhancements, or any way it sees fit. The municipal electric utilities who own transmission facilities may transfer some or all of the return to their respective General Funds. The principal of a return on investment is in no way tied to how the money is used, but instead is seen as a necessary part of business.

Q. IS THE RATE OF RETURN IN TCOS APPROPRIATE?

A. Absolutely. As in the discussion above, each entity who owns transmission facilities in ERCOT is allowed a reasonable return, set by the Commission, in order to incentivize and compensate owners who accept the risk of building and owning the facilities. There is no guarantee that this ownership would yield more than a loss or break even, excepting the return calculated in TCOS.

Q. WHAT IS THE RELEVANCE OF THE TREATMENT OF THIS ISSUE IN THE ELECTRIC UTILITY SPHERE TO THIS CASE?

A. The principles are the same between water and electric utility regulation. Most importantly, absent the ability to earn a return, AW is being required to serve the wholesale customers at issue at cost.

A. Effect of Removal of the GFT from Wholesale Rates on AW's Debt Service Coverage

Q. DID THE REMOVAL OF THE GFT FROM AW WHOLESALE RATES IN DOCKET NO. 42857 AFFECT AW'S TOTAL REVENUES AND DEBT SERVICE COVERAGE?

A. Yes. In the calculation of the DSC ratio, operating and maintenance (O&M) expenses are subtracted from total revenues. This produces Operating or Net Revenues. In a municipality, these Revenues are used to fund capital expenditures, debt payments, and the GFT, among other items. The DSC ratio is calculated by dividing the Net Revenues by that year's debt service amount. The calculated ratios among various municipalities can vary from about 1.25 to as high as 3.0. Since the sum of capital, debt service, and GFT are approximately equal to Net Revenues, eliminating the GFT in rates also reduces the DSC. In other words, when income is reduced because GFT is not permitted, the DSC ratio drops.

Q. DID AW'S WHOLESALE CUSTOMERS PROVIDE THEIR FAIR SHARE OF DSC DURING THE TEST YEAR?

A. No, they did not. When the wholesale water rates for the four petitioners were decreased in 2015 to remove the GFT from wholesale rates, the cash available for calculation of the DSC ratio was reduced below the DSC ratio provided by cash from AW's retail customers. The wholesale customer contribution to DSC was less than that of other AW customers. The wholesale customers did not pay an equitable portion of DSC for either water or wastewater service.

Q. DOES THE CALCULATION OF DSC RATIO IN THE YEARS SINCE THE 2015 ORDER AT THE COMMISSION DEMONSTRATE THIS?

A. Yes. Since the Order on Rehearing in Docket No. 42857 was put into effect, the wholesale water and wastewater revenue requirements of AW for the four petitioners have not included a GFT. I asked AW to separate the revenue and expenses for the Petitioners in the Test Year and calculate their individual DSC ratios. The overall DSC ratio for retail water customers in the adjusted 2018 test year is 1.58, and for the retail wastewater customers the coverage is 1.80. The calculated coverage for the four petitioners as a stand-alone group ranges from 0.74 to 0.84 for water service with an average of .8075. For wastewater service the coverage for the petitioners ranges from 1.36 to 1.42 with an average of 1.38. These figures are summarized in Attachment DW-3 to my testimony.

Q. DID THE DSC PROVIDED BY THE RELEVANT WHOLESALE CUSTOMERS MEET THE REQUIREMENTS OF AUSTIN WATER'S FINANCIAL POLICY?

A. No. AW has a financial target of 1.85 DSC ratio and the wholesale customers only provided a DSC ratio of about 0.8 for water and 1.38 for wastewater. The other customers of AW had to subsidize the revenue necessary to meet AW's targeted DSC ratio. Furthermore, the wholesale customers did not provide the same level of DSC as the retail customers. When the DSC ratio is less than 1.0, as has been the case for water service to the Petitioners, those customers did not pay sufficient revenues to recover the costs to serve them.

Q. IS THE LACK OF DSC FROM THE WHOLESALE CUSTOMERS SURPRISING?

A. No. After AW's previous Commission wholesale rate appeal, the GFT was removed from the rates charged to the Petitioners, and a large share of the income which produces the DSC was removed. Without some replacement for this income, there was no practical way that the Petitioners would contribute to the needed DSC ratio.

Q. IN SHORT, DO THE RETAIL AND WHOLESALE CUSTOMERS OF AW SUBSIDIZE THE PETITIONERS?

A. Yes. The retail customers have had to subsidize the Petitioners in two ways. First, with respect to water service, the revenues of the Petitioners do not cover the cost to serve them. When the DSC ratio is less than one (as is the case with the Petitioners), there is not enough net income to pay Petitioner's fair share of debt service. Second, for both water and wastewater service, Petitioners fell far short of the DSC ratio that was provided by retail customer revenues. Therefore, a shortfall of revenue from Petitioners reduced a key financial metric used by the rating agencies to determine the financial strength of AW. AW witness Dennis Whaley provides testimony on this point in more detail. Thus, Petitioners are currently benefiting from two subsidies in the water and wastewater rates required by the Commission's Order on Rehearing in Docket No. 42857.

V. THE ARGUMENTS AGAINST A GFT IN DOCKET NO. 42857

Q. GIVEN THAT AW QUANTIFIES ITS REVENUE REQUIREMENTS ON THE BASIS OF THE DSC METHOD IN THIS PROCEEDING, WHAT IS THE RELEVANCE OF THE GFT ISSUE THAT WAS ADDRESSED IN DOCKET NO. 42857?

A. In my view, none. AW's wholesale water and wastewater revenue requirements are computed on a different basis than the one that the Commission essentially rejected in that proceeding. Even so, the PFD and, therefore, theCommission's Order on Rehearing based upon it, contains errors that should be noted.

Q. DID THE PROPOSAL FOR DECISION IN DOCKET NO. 42857 ARGUE THAT THE M1 MANUAL DOES NOT ALLOW A GFT IN AW'S WHOLESALE REVENUE REQUIREMENTS?

A. Yes. On page 34 of the PFD there is a statement that the M1 Manual indicates "...the amount and appropriateness of any PILOT can be an issue in rate cases," and that some regulatory commissions "only [allow] payments for actual services rendered." This formed part of the conclusion in the PFD that the GFT should not be included in AW's wholesale water rates unless it was for services rendered.

Q. DO YOU AGREE WITH THIS CONCLUSION?

A. No. The PFD relies upon only a partial quotation from the Manual. In the sentences of the Manual directly above the quote used in the PFD, the M1 Manual states, "In some cases, however, a municipal water utility may make payments in lieu of taxes to the municipality that owns the utility. Such payments may be calculated as though the utility is privately owned and subject to property and franchise taxes...." In other

words, the M1 Manual does not prohibit the inclusion of transfers to a general fund in a magnitude which resembles franchise fees and property taxes, but recognizes that, "the amount and appropriateness" can be an issue.[2] As shown above, transfers for all customer classes were both appropriate and necessary to prevent subsidies from AW's retail customers to its wholesale customers.

The M1 Manual also discusses Debt Service Coverage, stating, "Coverage requirements are a test of the adequacy of utility revenues and do not represent a specific cash requirement, unless debt service coverage is the controlling factor in terms of the overall revenue needs of the utility...." This is exactly the case for AW which does not have adequate revenue from the wholesale customers for DSC. Also, in the Manual where the need for bondholder security is discussed, it states, "...coverage requirements must also be considered in determining the total annual revenue needed to comply with the utility's debt covenant agreements."[3] Again, AW needs to receive adequate revenues from the wholesale customers in order to meet its DSC goals. The rates set for the Petitioners in Docket No. 42857, however, do not provide adequate DSC.

In short, the M1 Manual was used in the arguments against AW, when indeed, the Manual contains language supporting the need for more revenues from the wholesale customers in order for them to provide their share of DSC.

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2 Attachment DW-4, M1 Manual of Water Supply Practices at 33.

3 *Id.* at 13.

Q. DID THE PFD ARGUE THAT THE TEXAS WATER COMMISSION HAD HELD THAT GFT APPLICABILITY WAS LIMITED?

A. Yes. The cited ruling by the Texas Water Commission (TWC) in 1989 stated, "The transfer amounts should be subfunctionalized within the water utility and are justifiable only to the extent necessary for the provision of adequate debt service coverage." On page 35, the PFD took the words of the TWC Order and used them to conclude that a GFT for anything other than reimbursement of administrative expenses should not be used. This conclusion ignored the phrase, "...to the extent necessary for the provision of debt service coverage." In fact, what AW is attempting to do is exactly that: design rates that provide adequate debt service coverage from the Petitioners. Wholesale water and wastewater rates should provide revenues that result in DSC from the Petitioners that equal that of AW's retail customers.

Q. DO YOU AGREE WITH THE TEXAS WATER COMMISSION'S RULING?

A. Yes, in part. The TWC was partially correct, as demonstrated above, that the GFT is necessary in wholesale water rates to provide the necessary DSC.

Q. SHOULD THE TWC ORDER HAVE BEEN USED IN DOCKET NO. 42857 TO ARGUE AGAINST THE GFT IN AUSTIN WATER'S RATE CASE?

A. No. Again, the disallowance based on the GFT in that case prevented the wholesale customers from providing their share of AW's DSC ratio, and in any event the language from the TWC Order did not support the exclusion of a GFT from wholesale water rates. It should have been recognized that the cash flow necessary to produce the required DSC was partially produced by the income from the GFT.

VI. IS THE FINANCIAL PLAN OF AUSTIN WATER RELATED TO DSC APPROPRIATE?

Q. SHOULD AUSTIN WATER TRY TO MAINTAIN A DSC RATIO OF 1.85?

A. Yes. Though I present brief testimony below on this subject based on my thirty years of experience with rating agencies, Mr. David Anders provides more testimony on this subject. The AW policy of having a target DSC ratio of 1.85 is both reasonable and good financial practice. Our goal in Bryan was a DSC ratio of 2.0. 2.0 is considered a midrange target and 2.5 would be considered even stronger. The rating agencies always looked at this metric first and with the most care to determine the financial health of the bond issuer. The exact goal of the policy over time is determined by working with the rating agencies and taking into account the specific challenges of each municipality.

Q. HAS AUSTIN WATER HAD PAST COMMUNICATION WITH RATING AGENCIES ABOUT DSC?

A. Yes. I have read excerpts from the 2016 and 2017 ratings from all three agencies. The written reviews all mention financial metrics and particularly DSC. In 2017 S&P for instance suggested that AW could strengthen its coverage more in line with what would be expected from an AA+ rated entity. The two practical ways I found to do this are to reduce O&M expenses or to increase rates. Either should increase net revenues. When the latter path is chosen then the cash flow must be incorporated into a long-range plan to either pay for more capital with the cash or defease debt. If reduction of expenses is the chosen path, services may suffer or capital expenses may rise. Care must be taken in in either path and AW has incorporated plans for managing expenses, maintaining a good debt-to-equity ratio, and paying down debt when appropriate.

Q. WHY IS THE DSC RATIO SO IMPORTANT IN RATING BONDS?

A. The amount of cash generated by an entity shows its ability to pay debt obligations. If there is just enough net revenue to pay only the debt, then capital replacement will suffer and ultimately more debt will become necessary. This cycle can become very damaging financially and has become the downfall of many businesses and cities. In such a scenario, the risk to bond investors is increased, and the bonds are rated downward. When this happens, the debt instrument which has been downgraded has a higher interest rate to offset the increased risk. The coverage ratio is also a simple metric to calculate and then compare to other issuers. For this reason, in my reviews with rating agencies, they always start with this metric to assess financial health.

Q. HAS THE DSC POLICIES OF AUSTIN WATER BEEN GOOD FOR ITS RATEPAYERS?

A. Yes. By keeping a good coverage ratio, AW's borrowing costs have been lower than they would have been otherwise as interest rates are at their lowest. All ratepayers, both retail and wholesale, have benefited from AW's financial policy. In the long run, it is best for the Petitioners if AW remains financially healthy and all customers contribute equally to DSC.

Q. COULD THE RULING BY THE COMMISSION IN DOCKET NO. 42857 HAVE AN ADVERSE EFFECT ON THE COST OF FUTURE BONDS THUS RAISING COSTS FOR ALL CUSTOMERS?

A. Yes. The ruling in Docket No. 42857 reduces the cash provided by wholesale customers for DSC. It is possible over the long run that this lack of cash flow from wholesale customers would cause bond ratings to suffer. If bond ratings were eventually lowered because of an insufficient DSC, bonds would become more

expensive and all customers would pay higher water and wastewater rates. Again, in my reading of the testimony, the PFD, and the Order on Rehearing, I did not find that there was a consideration of the effect on DSC of removing the GFT from wholesale rates. The focus of the GFT was otherwise, and the reduction of revenues which support DSC was an unintended consequence.

VII. CONCLUSION

Q. PLEASE SUMMARIZE YOUR CONCLUSIONS CONCERNING THE APPROPRIATENESS OF INCLUDING ADDITIONAL REVENUES IN THE 2018 WHOLESALE RATES OF AUSTIN WATER TO INCREASE DSC.

A. As stated above, the Commission would be right in testing the reasonableness of the amount of cash sought by AW so that DSC is not subsidized by one customer group or class to the benefit of another, but to deny the GFT altogether in 2015 had a consequence of creating insufficient DSC. An amount for DSC must be added to wholesale water and wastewater rates for the wholesale customers at issue in this case to insure that those customers contribute the same DSC ratio as retail customers. A tenet of ratemaking is that every provider of services which comes before the Commission, whether the service is (or has been, under prior regulatory regimes) telephone, electric, water, or wastewater, is allowed a rate of return, or its equivalent, on investments made to provide the service. Austin Water provides such a service and has made significant investment in order to do so, and its DSC is a reasonable way of receiving what is analogous to a rate of return. Without adequate DSC levels, AW will be required to serve the wholesale customers at cost, despite having borne the risks involved in serving those customers.

VIII. RATE CASE EXPENSES

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS SECTION?

A. In this section of my testimony, I will quantify the expenses arising from my work on this case, and support their recovery as being consistent with the applicable standards and other guidance.

Q. WHAT STANDARDS DO YOU APPLY IN EVALUATING THE RATE CASE EXPENSES ASSOCIATED WITH YOUR WORK?

A. First, I reviewed the Commission's rule that addresses water utilities' rate case expenses, 16 Tex. Admin. Code (TAC) § 24.44. That rule establishes that a utility may recover rate case expenses, including attorney's fees that were incurred as a result of the filing of an application or rate change. Rule 22.44 states that recoverable rate case expenses must be "just, reasonable, necessary and in the public interest."

For additional guidance, I reviewed 16 TAC § 25.245, which addresses rate case expenses for electric utilities and for municipalities participating in electric rate case proceedings. While this rule does not apply to this case, as AW is a water utility, it still provides helpful guidance in evaluating AW's rate case expense request, and offers a number of more detailed criteria that I use to consider the rate case expenses I quantify in this testimony.

Q. HOW SHOULD RATE CASE EXPENSES BE CONSIDERED IN THIS CASE?

A. As detailed in the Direct Testimony of David Anders, AW has submitted testimony and documentation in support of its rate case expenses through February 28, 2019. This includes invoices from my firm, Associated Power Analysts, Inc., for my own work on this matter. AW's preference is that rate case expenses be severed from this proceeding and considered in a separate matter that would proceed after the conclusion of this case.

That way, the entirety of my expenses incurred in this proceeding can be considered by the Commission. However, if the issue is not severed, AW has requested the ability to update its rate case expenses to reflect amounts incurred from the filing of the case to its completion.

Q. WHAT AMOUNT HAVE YOU INCURRED ON BEHALF OF AW THROUGH FEBRUARY 28, 2019?

A. To date my invoices have totaled $7,909.00. This includes travel to Austin and return by automobile at an expense of $109.00. A copy of my firm's invoices are provided in Schedule II-E-4.4 of the rate filing package.

Q. PLEASE IDENTIFY THE PARTICULAR CONSULTANT THAT CHARGED YOUR FIRM'S EXPENSES, YOUR HOURLY RATE, AND THE TOTAL HOURS BILLED.

A. I am the only person from our firm who has billed expenses to this rate case. My hourly rate is $300 an hour for rate work and $150 an hour for travel. To date I have billed for twenty-four hours of rate work and four hours of travel.

Q. UNDER RULE 25.245, WHAT CRITERIA DOES THE COMMISSION APPLY TO ELECTRIC UTILITY RATE CASE EXPENSES?

A. This rule establishes more detailed standards than the rule applicable to water utilities. In the electric context, the Commission considers:

- Whether the fees paid to, tasks performed by, or time spent on a task by an attorney or other professional were extreme or excessive;
- Whether the expenses incurred for lodging, meals and beverages, transportation, or other services or materials were extreme or excessive;

- Whether there was duplication of services or testimony;
- Whether the utility's proposal on an issue in the rate case had no reasonable basis in law, policy, or fact and was not warranted by any reasonable argument for the extension, modification, or reversal of Commission precedent;
- Whether rate-case expenses as a whole were disproportionate, excessive, or unwarranted in relation to the nature and scope of the rate case addressed by the evidence pursuant to subsection (b)(5) of this section; or
- Whether the utility failed to comply with the requirements for providing sufficient information pursuant to subsection (b) of this section.

Q. IN CONSIDERING THE RULE'S FIRST CRITERION RECITED IN YOUR PREVIOUS ANSWER, IS YOUR BILLING RATE AND THE TIME SPENT ON THE TASKS IN THIS CASE TO DATE REASONABLE?

A. Yes. Our firm recently undertook a survey of experts in our field of work to determine the various hourly rates that were charged by other experts. We found a range of $250 an hour up to $450 an hour. My rate of $300 an hour was below the median. As for the time spent on the case to research background, research data, communicate with attorneys and AW, this has been done efficiently by telephone except for a single meeting in Austin. The time spent to date is forty percent below my original estimate. Compared to other cases I have done, the work has gone quickly and the cooperation is excellent. I have been able to pull together information for my testimony with no time wasted waiting for information from others.

Q. HAVE YOU REQUESTED ANY EXPENSES FOR LODGING, MEALS AND BEVERAGES, TRANSPORTATION, OR OTHER SERVICES OR MATERIALS THAT ARE EXTREME OR EXCESSIVE?

A. No. My only expenses to date include driving to Austin and I charged the Internal Revenue Service rate for mileage in 2018. I do not anticipate lodging to be necessary unless required during testimony at the Commission later. My meals will be held to $25 a day or less if meals are required during direct testimony.

Q. DID YOUR WORK ON THIS MATTER RESULT IN ANY DUPLICATION OF SERVICES OR TESTIMONY?

A. No. The coordination among experts and attorneys in this rate case has been for the express intent that we cover all of the necessary facts while not duplicating any testimony. I believe there has been no duplication.

Q. DO THE ISSUES RAISED IN YOUR TESTIMONY HAVE A REASONABLE BASIS IN LAW, POLICY, OR FACT?

A. Yes. The exclusion of a GFT in Docket No. 42857 created class subsidies as explained above which I believe are prohibited in rate proceedings when subsidies can be prevented. It is also the policy of the Commission to allow a reasonable rate of return in rate cases, and the unintended effect of Docket No. 42857 was to deny AW any return from its wholesale customers.

Q. WHAT IS YOUR CONCLUSION REGARDING YOUR ACTUAL CHARGES?

A. My actual charges meet the test of being just, reasonable, necessary and in the public interest. As explained above it is certainly in the public interest to remove all water

and wastewater subsidies and to ensure that the bond ratings of Austin's utility services are not adversely affected in any way.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.

Dan Wilkerson

Principal

Associated Power Analysts, Inc.

Education, Licenses and Professional Associations

Mr. Wilkerson received a BS in Mechanical Engineering from Texas A&M University in 1972. He is a Member of the American Society of Mechanical Engineering. He is a Past President of the Texas Public Power Association (TPPA), and Past Section Chair of the American Public Power Association. Texas Public Power awarded him their Distinguished Service Award in 1998 and 2008.

Professional History and Experience

1972-1978: Field Engineer, General Electric Corp., Schenectady, NY. In this period he worked in the installation, inspection, and maintenance of gas turbines, steam turbines, generators, and mechanical drive steam turbines. The equipment serviced was owned by utilities, chemical plants, refineries, and universities in the Gulf Coast Region.

1978-1984: Division Manager of Electric Production for the City of Bryan. In this capacity Mr. Wilkerson was responsible for the reliable operation of two power plants, the Atkins Power Plant, 130MW, and the Dansby Power plant, 110MW. Both utilized gas fired steam electric units as well as one gas turbine. His respnsibilities included weatherization of units for winter operation. He was also responsible for fuel acquisition and pipeline contracts.

1984-2012:

Director of Electric Utilities, then in 2001, General Manager of Bryan Texas Utilities. In this capacity Mr. Wilkerson had the overall responsibility for the generation, transmission, distribution, billing, and wholesale sales of electricity for the Municipal Electric System owned by the City of Bryan. This included fuel procurement and wholesale sales both as bilateral contracts and in the daily market. Retail rate design for electric, water, and wastewater was a major responsibility to insure adequate revenues, bond covenant coverage, and equitable charges. Billing and rate administration was also a major responsibility for all of these services. Testimony at the Public Utility Commission was given on Transmission Cost of Service and at the Federal Energy Regulatory Commission on the same subject. Mr. Wilkerson represented the Municipal Sector at ERCOT in the following capacities; Operating Subcommittee, Technical Advisory Committee (two separate stints), Board of Texas Regional Entity, and ERCOT Board, as well as a number of working groups. He was President of TPPA during the writing of Senate Bill 7, the Deregulation Bill, and helped with its drafting. During his tenure the system grew more than fifty percent, adding 100MW of gas turbines and thirty miles of 138KV transmission.

Three industrial parks were expanded or started during his career. In all three parks, Mr. Wilkerson was responsible for developing the long range electrical service plans. Sales to new wholesale customers increased revenue, and technology was utilized to lower costs so that over the twenty eight years of his tenure, actual retail rates declined. Reliability indices improved so that outage lengths were reduced by two thirds. Preparations for high winter load were improved so that cold load pick up problems were addressed, and system improvements strengthened year round load carrying capability.

During his career Mr. Wilkerson worked with customers to explain billing questions or correct billing errors. These customers ranged from residential to commercial, industrial to wholesale. These activities helped to solidify the need for good rate design and transparent costs.

2012-present:

Principal of Associated Power Analysts, Inc. Activities to date include:

- Power and energy procurement for a major retail restaurant.
- Investigation of a gas turbine fire
- Rate analysis and expert testimony of wholesale electric rates
- Incident investigation of a gas turbine fire
- Rate proceedings at the PUC for wires charges for regulated companies
- Transmission ownership dispute proceedings at the PUC
- Accident investigation of an electrocution by a generator
- Engineering contract dispute resolution
- Consultation with a transmission owner of ERCOT transmission plans
- Working with industrial park developer to minimize electrical construction costs
- Analysis of multiple generator failures in Mexico
- Investigation of the death of a homeowner
- Investigation of accident related to transmission lines
- Investigation of line worker accident on transmission tower
- Investigation of repeated outages on chicken production facility
- Outage investigation leading to injury
- Investigation of an electrocution of a member of the public

Publications, Reports and Presentations

Mr. Wilkerson has authored or co-authored papers and reports on power generation and the enhancements of new technology for generation, particularly in boiler controls. He has taught classes on utility management for the American Public Power Association, and has given many presentations concerning utility practice.

Wilkerson History of Testimony

1996, Transmission Rate dispute between the City of College Station, City of Bryan, and Texas Municipal Power Agency; testified in Federal District Court in Houston, testimony and Affidavits before FERC, and testimony before the Public Utility Commission.

1999-2011, Transmission Rate Dispute between the City of Bryan and the Texas Municipal Power Agency; Written testimony at the Public Utility Commission; deposition given and testimony at Travis County District Court. Case found in favor of City of Bryan.

1999, Application for Installation of gas turbines in Weatherford Texas; Represented land owners opposing the site selection for the gas turbines; deposition, written and oral testimony before the Texas Commission on Environmental Quality. Gas turbines never constructed

2004, Public Utility Commission Project to implement a Nodal Market Design-Testimony before the Public Utility Commission on the Nodal Market; written and oral testimony at the PUC in favor of the Nodal Markets; Market design ultimately approved

2012-2014, Lower Colorado River Authority v. City of Georgetown, Texas, City of Boerne, Texas, City of Seguin, Texas, City of Kerrville, Texas, Acting By and Through Kerrville Utility Board; Central Texas Electric Cooperative, Inc.; Fayette Electric Cooperative, Inc.; and San Bernard Electric Cooperative, Inc.; Cause No. D-1-GN-12-002156, Travis , County; Attorney- Lambeth Townsend ;case was settled

2014, CenterPoint Energy Houston Electric LLC's Appeal and complaint against the Electric Reliability Council of Texas; written and oral testimony at the Public Utility Commission on behalf of Garland to allow Garland to construct and own certain transmission lines; Docket No. 42476; Attorney- Lambeth Townsend; PUC upheld Garland's position to build and own

2012-2015, El Paso Independent School District; Soccoro Independent School District; El Paso Community College; Cinco Sisters Properties, LP; and Juarez Boot Company Inc.; v. El Paso Electric Company; Cause No. 2013DCV0341; El Paso County; Attorney James K. LaRoe ;complaint against El Paso Electric because of freeze damage caused by rolling black outs in February 2011; written reports and deposition; case settled

2014-2015, James Andrew Brenek Individually and as the anticipated Administrator of the Estate of James Andrew "Drew" Brenek II, Deceased, and Rhonda Brenek, Individually vs. Aggreko, LLC and Rutherford Oil Corporation; Cause No. E-196, 603; Jefferson County, Texas; Attorney- Ronnie Penton; case was settled

2015-2016, Mott McDonald, LLC vs. EEG Power Distribution Corp., a dispute over engineering services provided in the construction of modular electric substations; attorney was Scott Kinzel; case was settled

2017-2018, Eduardo Munoz Jr. , and Kasandra Girela Munoz Individually and Next of Friend of Joshlynn Munoz, a Minor vs. Southwestern Public Services Company; Excel Energy Inc.; and Excel Energy Services Inc.; Cause No. C-4964-16-I; 398th District Court in Hidalgo County Texas; Attorney-Bruce Jamison; Mr. Munoz was injured in an electrical contact

2018 Thomas and Leslie Griffin vs Center Point Energy Houston Electric, LLC; In the 270th Judicial District Court, Harris, County, Texas; Attorney Jud Walton

Austin Water
Water Utility Cost of Service Model
Debt Service Coverage Analysis
Adjusted Test Year

Debt Service Coverage Analysis

Customer Class	Col 1 From COS Model Service Revenues at Existing Rates (excludes PUC ordered refunds)	Col 2 From COS Model Adjusted Test Year Gross O&M w/ OC Adjustments	Col 3 (Col 1 - Col 2) Adjusted Test Year Net Revenue Available for Debt Service After O&M	Col 4 From COS Model Adjusted Test Year Debt Service Allocation w/ OC Adjustments	Col 5 (Col 3 / Col 4) Adjusted Test Year Debt Service Coverage at Existing Rates
Inside City Retail					
Total Inside City Retail	276,029,203	128,342,065	147,687,139	93,573,831	1.58
Petitioners					
North Austin MUD	1,097,717	580,205	$517,511	613,755	0.84
Northtown MUD	903,356	496,509	$406,847	489,774	0.83
Water District 10	2,738,552	1,494,988	$1,243,565	1,671,774	0.74
Wells Branch MUD	1,504,939	819,696	$685,243	834,650	0.82

Austin Water
Wastewater Utility Cost of Service Model
Debt Service Coverage Analysis
Adjusted Test Year

Table 83 - 1
Debt Service Coverage Analysis

Customer Class	Col 1 From COS Model Service Revenues at Existing Rates (excludes PUC ordered refunds)	Col 2 From COS Model Adjusted Test Year Gross O&M w/ OC Adjustments	Col 3 (Col 1 - Col 2) Adjusted Test Year Net Revenue Available for Debt Service After O&M	Col 4 From COS Model Adjusted Test Year Debt Service Allocation w/ OC Adjustments	Col 5 (Col 3 / Col 4) Adjusted Test Year Debt Service Coverage at Existing Rates
Inside City Retail					
Total Inside City Retail	255,903,817	111,684,114	144,219,703	80,169,938	1.80
Petitioners					
North Austin MUD	$1,101,064	$585,000	$516,064	$362,271	1.42
Northtown MUD	$1,129,180	$611,451	$517,729	$378,653	1.37
Wells Branch MUD	$1,763,829	$957,668	$806,161	$593,073	1.36

supplies, small equipment that does not extend the useful life of major facilities, and general overhead expenses. For a government-owned utility, other elements of O&M expense might also include the costs of support services rendered by the municipality to the utility, such as the use of computer facilities, assistance in collecting water bills, procurement activities, human resources administration, fleet management, and other support services.

Taxes or transfer payments. A utility may be required to pay certain taxes as part of their normal operations (e.g., a state utility tax on gross revenues). A utility may have several tax payments for their locality. In contrast to a tax payment, a transfer payment may be for items such as a payment in lieu of taxes (PILOT). AWWA's policy statement on Financing, Accounting, and Rates states that "Water and wastewater utility funds should not be diverted to uses unrelated to water and wastewater utility services. Reasonable taxes, payments in lieu of taxes, and/or payments for services rendered to the water utility by a local government or other divisions of the owning entity may be included in the utility's revenue requirements after taking into account the contribution for fire protection and other services furnished by the utility to the local government or to other divisions of the owning entity" (AWWA 2015). Accordingly, payments made to a municipality's general fund should reimburse the general fund for the necessary cost of goods and/or services required by the water utility to provide water service. Transfers from the water fund to a municipal general fund, in addition to those specifically identified above, may be applicable to unique local situations and should be considered in conjunction with legal requirements and in conformance with the previously referenced AWWA policy statement.

Debt-service payments and specified reserves. The debt-service component of the cash-needs approach usually consists of principal and interest payments on bonds or other outstanding debt instruments. It may also include debt-service reserve requirements as established by the indenture or covenant. Other reserves are often required to provide for operating working capital, emergency repairs and replacements, as well as for routine replacements and extensions. In addition to debt service and payments to reserve fund accounts, many utilities are required to provide net revenues sufficient to cover the bonded debt, particularly if revenue bonds are involved. Typically, debt-service coverage requirements specify that revenues be sufficient to meet O&M expenses and taxes and, at a minimum, to equal or exceed a stated percentage of the annual debt-service payments. Coverage requirements are a test of the adequacy of utility revenues and do not necessarily represent a specific cash requirement, unless debt-service coverage is the controlling factor in terms of the overall annual revenue needs of the utility, which may be the case in a particular year. The coverage requirements are intended to provide a measure of security for bondholders. As such, coverage requirements must also be considered in determining the total annual revenue needed to comply with the utility's debt covenant agreements.

Rate-funded capital expenditures. This component of the cash-needs approach is not all capital expenditures, but rather, only that portion of the capital expenditures to be paid during the test year from current rate revenues. Capital expenditures may be classified into three broad categories: normal annual (routine) replacement of existing facilities, normal annual extensions and improvements, and major capital replacements and improvements. A utility should periodically review and update its needs in each of these areas to recognize changing conditions. Projections for such needs are essential in developing overall revenue requirement projections. These projections of total capital needs should be accompanied by estimates of contributions received from developers or customers, government grants, and other nonutility sources.

Government-owned utilities commonly use current revenues to finance

- normal annual replacements,
- extensions, and

Chapter II.4

Taxes

Investor-owned water utilities are responsible for paying taxes to local, state, and federal authorities. These taxes may include property and franchise taxes paid to local authorities; gross receipts, income, capital stock, and franchise taxes paid to state authorities; and income taxes and payroll taxes paid to the federal government. Although municipally owned water utilities are generally not subject to taxation by the local, state, or federal governments, municipal water utilities sometimes make payments in lieu of property taxes to the local municipalities that own them.

This manual makes no attempt to fully cover the subject of taxation for utilities. This chapter is intended to alert the reader to the complexities of utility taxes and the need for specific tax expertise in considering tax obligations when determining the utility's need for adequate revenues.

LOCAL TAXES

The most common form of local tax is the property tax, but franchise taxes may also be levied. A franchise tax may be a flat fee or based on the utility's gross or net revenues. Property taxes are based on the assessed value of utility property located within the jurisdiction of the taxing authority. Therefore, the water utility must maintain property records in a manner that enables the tax authority to determine the book value of utility plant investment (which is subject to taxation) within individual local taxing jurisdictions. Where multiple municipalities or taxing districts are involved, separate investment records must be maintained. Each local taxing authority will also have its own individual tax rates, making it complicated to calculate total property tax.

Although, municipally owned utilities are not normally subject to taxation by local, state, or federal authorities, they may be subject to local taxes for property that is owned outside the owning community (such as watershed land). In some cases, however, a municipal water utility may make payments in lieu of taxes to the municipality that owns the utility. Such payments may be calculated as though the utility is privately owned and subject to property or franchise taxes or may be established at some lesser amount. For municipal utilities regulated by a state regulatory commission, the amount and appropriateness of any payments in lieu of property taxes can be an issue in rate cases. Some commissions only allow payments for actual services received.

DOCKET NO. 49189

APPLICATION OF THE CITY OF AUSTIN DBA AUSTIN WATER FOR AUTHORITY TO CHANGE WATER AND WASTEWATER RATES	§ § § § §	BEFORE THE PUBLIC UTILITY COMMISSION OF TEXAS

DIRECT TESTIMONY
OF
DENNIS P. WALEY

ON BEHALF OF THE CITY OF AUSTIN
D/B/A AUSTIN WATER

APRIL 2019

TABLE OF CONTENTS

ATTACHMENTS

I. INTRODUCTION

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Dennis P. Waley. My business address is 221 West Sixth Street, Suite 1900, Austin, Texas 78701.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT POSITION?

A. I am employed by PFM Financial Advisors, LLC (PFM), and serve as Managing Director of my firm's Austin office.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

A. I am testifying on behalf of the City of Austin (City) doing business as Austin Water (AW).

Q. DID YOU PREPARE THIS TESTIMONY?

A. Yes. This testimony was prepared by me or under my direct supervision.

Q. PLEASE GIVE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. My resume is attached as DPW-1. I earned a Bachelor of Business Administration, with a major in finance, from the University of Texas at Austin. I am a Certified Public Accountant and a registered Municipal Advisor Representative (Series 50 licensed). I joined PFM in 2005 and serve as a Managing Director in the Austin Office.

Prior to joining PFM, I worked for the City for over twenty years and served as City Treasurer for the last eight years of my tenure. I have over thirty years'

experience in public finance and have worked as financial advisor on the issuance of over $20 billion in debt obligations.

Q. WOULD YOU PLEASE CLARIFY YOUR REFERENCES TO THE CITY AND AW?

A. Yes. AW is a water and wastewater utility, owned by the City of Austin, a home-rule city. When I refer to AW, I am referring to the utility, which is a department functioning within the City.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to place AW's requested wholesale rate increase into the context of its credit ratings and the guidance provided by the three major credit rating agencies. As I will discuss, those rating agencies have approvingly citied AW's debt service coverage (DSC) ratio targets. Establishing rates that achieve those targets will be key to avoiding a downgrade, an event which would have a negative impact on AW's ability to access the credit market, and which would ultimately result in higher rates to the wholesale customers affected by this case.

AW witness Dan Wilkerson provides specific quantification of the DSC ratios provided through the rates paid by the wholesale customers at issue in this case (which, as Mr. Wilkerson testifies, are below 1.0 for water and below any reasonable target for wastewater). My testimony addresses the rating agencies' view of AW and the importance of adequate DSC ratios in general.

III. SIGNIFICANCE OF AGENCY RATINGS TO AW

Q. WHY ARE SOUND CREDIT RATINGS IMPORTANT TO AW?

A. While AW is a city-owned water utility, it still must regularly access capital markets to obtain debt financing for various purposes. AW's credit ratings are therefore important to it, as they are key drivers of the availability of debt financing and its cost. While I will detail certain factors that influence AW's credit ratings, in general, they are based on the fiscal health of the utility.

Q. HOW CAN FISCAL HEALTH BE MEASURED?

A. There are many ways to measure the fiscal health of a utility. The primary of these are financial ratios and credit ratings. The credit rating agencies use analyses of past financial performance, future projections, and an assessment of management to provide an overall view on the creditworthiness of a particular entity. Strong financial metrics lead to strong credit ratings, which in turn lead to lower debt costs when accessing the capital markets. Accordingly, a utility ideally maintains strong financial ratios. Financially strong utilities are more likely to increase rates incrementally as necessary over time, whereas weak utilities may resist raising rates until very large increases are needed to maintain solvency. AW has, over the past few years, undertaken the prudent approach of setting financial targets and incrementally increasing rates to achieve strong financial metrics. Notably, the wholesale customers at issue in this case have been excused from that process, as their rates have not increased since 2016.

Q. IS AW SUBJECT TO RATING BY THE THREE MAJOR NATIONAL RATING AGENCIES?

A. Yes. AW maintains credit ratings on its bonds from three of the major national rating agencies: Moody's Investors Service (Moody's), S&P Global Ratings (S&P), and Fitch Ratings (Fitch).

IV. AW'S CURRENT CREDIT RATINGS; AW'S EFFORTS TO MAINTAIN RATINGS

Q. HOW DO THE THREE AGENCIES CURRENTLY RATE AW?

A. The current outstanding ratings for AW's separate (working) lien revenue bonds are Aa2 (stable outlook) from Moody's, AA (stable outlook) from S&P and AA- (stable outlook) from Fitch. A stable outlook implies that rating agencies do not predict a rating change in the next one to two years. The stable outlook from all three rating agencies is a result of actions AW has taken since 2012 to increase revenues, thereby improving its debt and liquidity metrics. It is important that AW continue to monitor and adjust rates to maintain its financial metrics or risk a possible downgrade.

Q. WHAT WOULD THE CONSEQUENCES BE TO AW OF A CREDIT DOWNGRADE?

A. The consequences would be harmful to AW and it customers. Credit ratings correspond to borrowing costs and the availability of debt financing. All else equal, a utility with a lower credit rating will obtain debt financing at a higher cost, impairing the ability of the utility to execute its capital improvement plans at the lowest possible cost, and potentially resulting in service of a lesser quality or at higher cost to its customers. For these reasons, AW has established financial metrics at certain targeted levels to support its credit ratings.

Q. WHY DID AW ADOPT POLICIES AND TARGETS TO SUPPORT ITS CREDIT RATING?

A. AW's policies to maintain financial metrics at certain target levels were first implemented during a period of relative financial distress. In 2012, AW was facing decreased revenues due to a severe drought. Over this period, revenues decreased enough that AW's financial metrics were not in line with its highly rated peers. This set of factors put AW's creditworthiness at risk. Management worked to create a set of rate increases that, over time, restored financial health to the utility. Maintaining this financial health over time is the best way to keep capital costs low. This rate proceeding should properly be viewed as a part of that process.

Q. WHAT ARE THE BENEFITS OF AW MANAGEMENT'S APPROACH SINCE THAT TIME?

A. The use of incremental rate adjustments supported by COS analyses indicating a need for those adjustments is a prudent course, and avoids ratepayer shock due to large rate adjustments. In that same vein, as detailed by AW witness Joseph Gonzales in his direct testimony, AW is requesting a modest rate adjustment for the affected wholesale customers through this rate case.

Q. WHAT FINANCIAL POLICIES SUPPORT AW'S CURRENT CREDIT RATINGS?

A. Rating agencies have noted the formal and informal policies adopted by AW's management as a positive credit factor. S&P notes that "management already had a number of best practices to support the utility's financial performance, such as maintaining cash reserves equivalent to at least 60 days of operating expenses, and

targeting total debt service coverage (DSC) of all liens at least at 1.5x; internal targets are even more robust at 245 days and 1.85x, respectively."[1]

Maintaining revenues at a level to support these targets is an important part of preserving AW's fiscal health and strong credit ratings. Adherence to its financial goals resulted in AW's rating outlook from Fitch improving to "stable" from "negative" in 2016. Fitch noted that its "revision of the Outlook to Stable from Negative reflects modest but notable improvement in AWU's financial performance ... financial metrics for the City of Austin's (TX) combined water and wastewater system remain weak for the rating category but are forecast to continue strengthening."[2]

Q. HOW DO THE RATING AGENCIES VIEW DEBT SERVICE COVERAGE?

A. Two metrics targeted in AW's financial policies are based on factors that are important to credit rating agencies. Although many factors contribute to the final credit rating, the rating agencies place emphasis on the debt service coverage ratio, as well as the level of reserves (commonly measured as days-cash-on-hand) when evaluating the financial strength of a utility.

Q. IS DEBT SERVICE COVERAGE A KEY METRIC USED BY THE RATINGS AGENCIES?

A. Yes. It is an important data point that each ratings agency considers in arriving at a credit rating. Debt service coverage is calculated slightly differently by each rating agency, but the concept essentially represents the ratio of net revenues available for

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[1] Austin, Texas; Water/Sewer, S&P Global, July 24, 2017.

[2] Fitch Rates Austin's (TX) Water and Wastewater Rev Rfdg Bonds 'AA-'; Outlook Revised to Stable, Fitch Ratings, May 3, 2016. https://www.fitchratings.com/site/pr/1003824.

debt service (operating revenues less operating requirements, not including depreciation or amortization) to annual debt service requirements (the sum of principal and interest). The debt service coverage metric provides an indication of a utility's ability to pay its obligations as well as overall financial flexibility. Additionally, investors and rating agencies evaluate the trend of this ratio over time to determine changes in the financial health of a utility system.

Q. HOW HAVE THE RATING AGENCIES VIEWED AW'S DEBT SERVICE COVERAGE?

A. With respect to AW, Moody's noted in its 2017 report that "after declining debt service coverage and liquidity levels from fiscal 2011 to 2014, annual rate increases along with strong expenditure management helped boost annual financial metrics in fiscal 2015 and 2016."[3] Moody's further noted in the same report that a factor that could lead to a downgrade of AW's credit rating is "poor operating performance leading to a decline or prolonged weakness in reserve levels and debt service coverage." Fitch also discusses coverage trends in its most recent report on AW, noting that "Fitch calculated all-in debt service coverage improved to 1.84x in FY16 ... following a low-point of 1.25x in FY14."[4]

Of course, it must be noted that the ratings agencies' review, and the metrics that they utilize, are utility-wide. To my knowledge, the rating agencies have never quantified any of their metrics with respect to the Petitioners. Dan Wilkerson, who provides testimony for AW in this case, details the DSC ratios provided by those specific customers, all of whom provide revenues well beneath AW's targeted level,

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[3] Austin, TX Water & Wastewater System: Credit Opinion, Moody's Investors Service, July 20, 2017.

[4] Austin, Texas; Water Revenue Bonds; New Issue Report, Fitch Ratings, July 27, 2017.

beneath any level favorably discussed by any rating agency on an AW-wide basis, and even—in the case of water service—beneath 1.0.

Q. HOW HAS AW'S CREDIT RATINGS CHANGED IN RECENT YEARS?

A. The table below provides a history of the credit ratings and rating outlook for AW's Separate Lien Revenue Bonds since 2012:

Austin Water Utility's Separate Lien Revenue Bond Rating History[5]

Year	Moody's	Moody's Outlook	S&P	S&P Outlook	Fitch	Fitch Outlook
2018	Aa2	Stable	AA	Stable	AA-	Stable
2017	Aa2	Stable	AA	Stable	AA-	Stable
2016	Aa2	Stable	AA	Stable	AA-	Stable
2015	Aa2	**Negative**	AA	Stable	AA-	**Negative**
2014	Aa1	Stable	AA	Stable	AA-	Stable
2013	Aa1	Stable	AA	**Positive**	AA-	Stable
2012	Aa1	Stable	AA	Stable	AA-	Stable

As shown above, in 2014–2015 AW's ratings from Fitch and Moody's were under pressure due to weak financial metrics caused by decreased revenues, which led to lower debt service coverage and reserve levels. Further, S&P pulled back its "positive" outlook to "stable" on AW in 2014 in recognition of the deteriorating position of the utility's coverage and liquidity. Fiscal year 2014 coverage declined to 1.25x, which is the minimum coverage allowable to comply with AW's bond covenants. Thereafter, AW began implementing policies to improve financial metrics through budgeting for higher coverage and establishing reserve funds to bolster cash balances. As Days Cash on Hand and coverage increased, rating outlooks stabilized.

[5] *Municipal Advisory Council of Texas, accessed December 10, 2018.*

Q. HOW DID THE RATINGS AGENCIES VIEW THE DEBT SERVICE COVERAGE DECLINE OF 2014?

A. Unfavorably; as I describe above. This caused Moody's and Fitch to place AW's credit ratings on negative outlook. In a May 27, 2014 press release, Fitch Ratings stated, "The revision on Outlook to Negative from Stable on the water and wastewater bonds reflects the diminishing prospect of any material improvement in AWU's financial profile over the near term, due in part to ongoing drought conditions." Such a negative outlook is either followed by a downgrade or corrective action is taken by rated entity to resolve the concerns. If the rating agency determines that sufficient changes have occurred to remedy the issues, the outlook can be returned to Stable.

AW's DSC improved from 2015 through 2017. Fitch rating stated in its July 27, 2017 New Issue Report that "AW's financial margins improved during the past two fiscal years. Following a multi-year period of weakened financial performance in FY 12 through FY 14, driven principally by weather conditions, the cumulative effects of annual rate increases and rate restructuring efforts resulted in improved debt service coverage levels and improved liquidity." Although AW has made good progress, AW must remain vigilant in its efforts to maintain and strengthen debt service coverage in order to avoid further negative rating actions.

Q. HAVE THE RATING AGENCIES PUBLISHED GUIDANCE ON DSC TRENDS FOR COMPARABLY-RATED ENTITIES AS AW?

A. Yes, they have. The Fitch debt service coverage median for AA credits is 2.3x and the S&P target for strong rating criteria is 1.6x.[6] The 1.6x target set by S&P is for "All-in Coverage." Meaning that in addition to debt service, the calculation will include other fixed costs such as the general fund transfer. AW's target of 1.85x DSC is within the range of these benchmarks, and indeed, is substantially below Fitch's published average for AA credits. And, as discussed in the direct testimony of AW's witness Dan Wilkerson, AW's revenues from the Petitioners are substantially below either of these benchmarks. None of these customers provide a level of debt service coverage meeting the rating agency targets. None of these customers provide even 1.0 DSC for water service

Q. WHAT DO YOU CONCLUDE FROM THIS REVIEW OF AW'S HISTORICAL CREDIT RATINGS?

A. It is imperative that AW continue to monitor and adjust rates to avoid the situation that occurred in 2014–2015. Any indication of declining metrics could put AW's rating in jeopardy of downward rating pressure.

Q. HOW DO AW'S CREDIT RATINGS COMPARE TO THOSE OF OTHER MUNICIPALITIES' WATER UTILITIES?

A. Avoidance of a downgrade has been key to AW's ratings remaining consistent with those of the largest municipal water utilities in Texas. What follows is a table of the credit ratings of the water utility systems of the five most populous Texas cities:

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[6] 2017 Fitch Water and Sewer Medians Report; 2016 S&P Utilities Rating Methodology and Assumptions.

Utility	Moody's	S&P	Fitch
Austin Water Utility	Aa2	AA	AA-
San Antonio Water System (SAWS)	Aa1 Aa2 (Junior Lien)	AA+ AA (Junior Lien)	AA+ AA (Junior Lien)
City of Dallas Waterworks & Sewer System	Aa1	AAA	AA+
City of Fort Worth Waterworks & Sewer System	Aa1	AA+	AA
City of Houston Utility System	Aa2 Aa1 (Junior Lien)	AA AA+ (Junior Lien)	AA AA+ (Junior Lien)

As the table demonstrates, AW's ratings are slightly lower than its peer utilities, although roughly consistent with them.

Q. IF AW HAD ITS CREDIT RATINGS DOWNGRADED IN THE 2014–2015 TIMEFRAME, WHAT WOULD HAVE BEEN THE IMPACT ON AW AND ITS CUSTOMERS?

A. Had AW been downgraded by Fitch in 2015, it would have been the only major Texas city—among the top five most populous—with a utility system with a rating in the A category. Ratings in this lower category generally translate into higher interest rates and higher debt service costs that must be passed on to the ratepayers.

Q. IS THE POTENTIAL EFFECT OF A DOWNGRADE FROM "AA" TO "A" ON THE ABILITY OF AW TO OBTAIN DEBT FINANCING SIGNIFICANT?

A. Yes. Over the past five years, credit spreads for a twenty year bond between an "AA" rated and an "A" rated credit averaged 35 basis points.[7] An additional 35 basis points in the interest rate would add $7 million in interest costs to a $100 million bond over

[7] Average daily difference of Municipal Market Data AA GO 20 year spot rate and Municipal Market Data A GO 20 year spot rate from December 10, 2013 – December 10, 2018. Data accessed via The Municipal Market Monitor (TM3), accessed December 10, 2018.

twenty years. The cost of a lower rating increases as credit spreads widen. Municipal bond issuers such as AW have enjoyed a period of historically low interest rates and narrow credit spreads in the past five years; however, as interest rates increase, credit spreads tend to widen, and the cost of a credit rating downgrade could become more expensive.

Q. IS AW HAVING A STRONG CREDIT RATING IN THE INTEREST OF ITS CUSTOMERS?

A. Yes, it is. Strong credit ratings provide the best access to the debt market and lower borrowing costs. It is critical that AW monitor credit metrics and make rate decisions that will maintain its credit ratings and rating outlook.

Q. WHAT DOES THIS LEAD YOU TO CONCLUDE REGARDING AW'S DEBT SERVICE COVERAGE PRESENTED IN THIS CASE?

A. I conclude that it is appropriate for AW to set its wholesale water and wastewater rates with a target debt service coverage ratio of 1.85. As I have discussed, debt service coverage is a critical factor upon which the agencies base their ratings. Indeed, AW's specific 1.85x target ratio has been approvingly citied by S&P. And, as discussed by AW witness Dan Wilkerson, AW is not currently recovering rates that produce that ratio from the wholesale customers at issue in this case. From the perspective I present in this testimony, AW's proposed rates are appropriate, and target an appropriate level of debt service coverage.

V. RATE CASE EXPENSES

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS SECTION?

A. In this section of my testimony, I will describe the expenses arising from my work on this case, and support AW's recovery of those expenses as complying with the applicable standards and other guidance.

Q. WHAT STANDARDS DO YOU APPLY IN EVALUATING THE RATE CASE EXPENSES ASSOCIATED WITH YOUR WORK?

A. I reviewed the Commission's rule that addresses water utilities' rate case expenses, 16 Tex. Admin. Code (TAC) § 24.44. The rule states that recoverable rate case expenses must be "just, reasonable, necessary and in the public interest."

I also reviewed 16 TAC § 25.245, which addresses rate case expenses for electric utilities and for municipalities participating in electric rate case proceedings. While this rule does not apply to this case, since AW is a water utility, it still provides useful guidance in considering AW's rate case expense request. This rule specifies more detailed criteria that I will use to evaluate the rate case expenses I quantify in this testimony.

Q. WHAT AMOUNT HAVE YOU INCURRED ON BEHALF OF AW THROUGH MARCH 26, 2019?

A. I have incurred $8,150.00. A copy of my firm's invoice is provided in Schedule II-E-4.4 of the rate filing package.

Q. PLEASE IDENTIFY THE PARTICULAR CONSULTANT THAT CHARGED YOUR FIRM'S EXPENSES, YOUR HOURLY RATE, AND THE TOTAL HOURS BILLED.

A. As the testifying witness in this case, I have billed approximately 17 hours, through March 26, 2019, at a rate of $350 per hour. Blake Roberts and Jen Arndt, both Senior Managing Consultants at PFM, each billed four hours on their work in support of my testimony and each at a rate of $275 per hour.

Q. UNDER RULE 25.245, WHAT CRITERIA DOES THE COMMISSION APPLY TO ELECTRIC UTILITY RATE CASE EXPENSES?

A. This rule establishes more detailed standards than the rule applicable to water utilities. In the electric context, the Commission considers:

- Whether the fees paid to, tasks performed by, or time spent on a task by an attorney or other professional were extreme or excessive;
- Whether the expenses incurred for lodging, meals and beverages, transportation, or other services or materials were extreme or excessive;
- Whether there was duplication of services or testimony;
- Whether the utility's proposal on an issue in the rate case had no reasonable basis in law, policy, or fact and was not warranted by any reasonable argument for the extension, modification, or reversal of Commission precedent;
- Whether rate case expenses as a whole were disproportionate, excessive, or unwarranted in relation to the nature and scope of the rate case addressed by the evidence pursuant to subsection (b)(5) of this section; or
- Whether the utility failed to comply with the requirements for providing sufficient information pursuant to subsection (b) of this section.

Q. IN CONSIDERING THE RULE'S FIRST CRITERION RECITED IN YOUR PREVIOUS ANSWER, IS YOUR BILLING RATE AND THE TIME SPENT ON THE TASKS IN THIS CASE TO DATE REASONABLE?

A. Yes. I charged PFM's contracted rates for our work on this case. Those rates—$350 per hour, and $275 per hour for my associates—are the same rates that PFM charges for its other work for AW, and the same rates charged for our work for other clients.

Q. HAVE YOU REQUESTED ANY EXPENSES FOR LODGING, MEALS AND BEVERAGES, TRANSPORTATION, OR OTHER SERVICES OR MATERIALS THAT ARE EXTREME OR EXCESSIVE?

A. No, I have not.

Q. DID YOUR WORK ON THIS MATTER RESULT IN ANY DUPLICATION OF SERVICES OR TESTIMONY?

A. No. No other witness for AW performs a review of AW's ratings, in the context of AW's DSC ratio, as I have done.

Q. DO THE ISSUES RAISED IN YOUR TESTIMONY HAVE A REASONABLE BASIS IN LAW, POLICY, OR FACT?

A. Yes. My testimony is based on guidance provided by the rating agencies, guidance that is routinely relied upon by professionals in my field, and by regulators of rated entities.

Q. WHAT IS YOUR CONCLUSION REGARDING YOUR ACTUAL CHARGES?

A. My firm's charges for the provision of my testimony are reasonable, consistent with the available guidance, and are properly recovered by AW in this case (or a separate proceeding, should rate case expenses be severed and addressed in another matter).

VI. CONCLUSION

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes it does.

RESUMES OF KEY PROFESSIONALS

pfm

Dennis P. Waley, CPA

Managing Director
PFM Financial Advisors LLC

Dennis Waley joined PFM in July 2005 and serves as a managing director in the firm's Austin office. Prior to joining PFM, Dennis served the City of Austin for 20 years, as City Treasurer for the last eight of those years. He was responsible for cash management, debt management and the investment management of a $1.2 billion portfolio for the City.

Dennis' financing experience includes debt issuance for General Obligation, Electric Utility, Water and Wastewater Utility, Airport, Convention Center and other not-for-profit agencies. He has participated in over $10 billion in financings using both fixed- and variable-rate structures, and has extensive experience working with rating agencies and insurance providers. He assisted in developing the plan of finance for Austin Bergstrom International Airport. Dennis also served on several city boards, including the Employees Retirement System, Firefighters Retirement System, and the Deferred Compensation Committee.

Dennis is a member of the Government Treasurers' Organization of Texas (GTOT) and Government Finance Officers' Association of Texas (GFOAT). He served as GTOT president in 2003, and also as a board member and legislative committee chair.

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DOCKET NO. 49189

APPLICATION OF THE CITY OF AUSTIN DBA AUSTIN WATER FOR AUTHORITY TO CHANGE WATER AND WASTEWATER RATES	§ § § § §	BEFORE THE PUBLIC UTILITY COMMISSION OF TEXAS

Austin WATER

DIRECT TESTIMONY
OF
STEPHEN J. COONAN

ON BEHALF OF THE CITY OF AUSTIN
D/B/A AUSTIN WATER

APRIL 2019

TABLE OF CONTENTS

ATTACHMENTS

I. INTRODUCTION, BACKGROUND, PROFESSIONAL EXPERIENCE, AND PURPOSE

Q. PLEASE STATE YOUR NAME FOR THE RECORD.

A. Stephen James Coonan.

Q. WHERE ARE YOU CURRENTLY EMPLOYED, AND WHAT IS YOUR PRESENT JOB TITLE?

A. I am currently employed by Alan Plummer Associates, Inc. (APAI) and am a Principal in the firm. I have been employed by APAI since May 1992. My business address is 6300 La Calma Drive, Suite 400, Austin, Texas 78752. My phone number is (512) 452-5905.

Q. WHAT KIND OF COMPANY IS APAI?

A. APAI is a consulting engineering firm that specializes in water resource planning and design. The firm has been in business since 1978 and provides planning and design services to municipalities in the area of water, wastewater, reclaimed water, and storm water.

Q. WHAT JOBS DID YOU HOLD BEFORE GOING TO WORK AT APAI?

A. Prior to joining APAI, I was employed by Dannenbaum Engineering Corporation for seven years. Prior to that I was employed by the Missouri Highway Department for two years.

Q. WHAT DUTIES DO YOU PERFORM IN YOUR PRESENT POSITION WITH APAI?

A. In addition to being a Principal in the firm, I am the Area Leader for our Central Texas Operation, which means that I oversee the business in our Austin office. In this

capacity I am involved in developing work as well as directing the completion of the work.

Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND.

A. I graduated from the University of Missouri – Rolla (now called Missouri University of Science & Technology) in 1982 with a B.S. in Civil Engineering.

Q. DO YOU HOLD ANY PROFESSIONAL REGISTRATIONS?

A. Yes. I am a Licensed Professional Engineer in the States of Texas and North Carolina.

Q. IS YOUR EDUCATIONAL BACKGROUND AND WORK HISTORY SET FORTH IN DETAIL ON ATTACHMENT SJC-1?

A. Yes.

Q. HAS YOUR WORK IN WATER RESOURCES BEEN RECOGNIZED BY THE INDUSTRY?

A. Yes. In the mid-1990s I was selected to serve on the Stakeholder Committee that helped the predecessor to the Texas Commission on Environmental Quality (TCEQ) write the original rules governing the use of reclaimed water in the State of Texas. My expertise and contribution to the industry have also been recognized through my election to numerous leadership roles in the Capital Area Chapter of the Water Environment Association of Texas (WEAT), culminating in my election as President in 2005. Following my service at the local level, I was elected to several leadership roles for WEAT at the State level, culminating in my election as President in 2015. I am currently serving as the Senior Delegate from the State of Texas to the Water Environment Federation, an international federation dedicated to the protection and development of water resources.

Q. WHAT IS YOUR PURPOSE IN TESTIFYING IN THIS RATE APPLICATION?

A. The purpose of my testimony is to provide an expert opinion concerning the use of reclaimed water as a water supply source in the City of Austin (City or Austin).

Q. WHAT ARE YOUR FINDINGS?

A. I have two findings. First, it is prudent for the City to have a reuse system as part of its overall water supply portfolio. Second, the City's customers, including their wholesale customers, benefit from the City's reuse system.

II. WATER REUSE AS A WATER SUPPLY RESOURCE

Q. CAN YOU EXPLAIN WHAT WATER REUSE IS?

A. The basic concept of water reuse is the beneficial reuse of highly treated wastewater. It is also important to note that water reuse has several different names. In addition to water reuse, people sometimes refer to it as water recycling or reclaimed water, among other names. These all describe essentially the same activity.

Q. WHY DO UTILITIES TYPICALLY DEVELOP REUSE SYSTEMS?

A. There are typically two alternative reasons utilities decide to develop reuse systems. The first reason utilities develop reuse systems is as an alternative water supply. By providing reuse water to non-potable customers, they offset demand for potable water; thereby delaying the need to invest in and develop new sources of water. In addition, reclaimed water is a drought resistant supply that has become increasingly important to utilities considering climate uncertainty and the severe droughts recently experienced in Texas. The second reason utilities develop reuse systems is as an alternative disposal mechanism. In some instances, stringent requirements on the discharge of treated effluent make it more economical to reuse the water.

Q. IN YOUR EXPERIENCE, WHICH OF THESE REASONS IS THE MORE TYPICAL DRIVER IN THE STATE OF TEXAS?

A. In my experience, water supply is the dominant reason that utilities in Texas decide to develop a reuse system. Water supplies are limited in most areas of the state and the state continues to see significant growth in both population and the demand for water. Additionally, the state has experienced recurring periods of significant drought. All of these factors contribute to the development of reuse systems.

Q. HOW MUCH WATER DOES THE CITY CURRENTLY USE?

A. During the 2018 test year, Austin Water (AW) diverted 151,028 acre-feet of water from the Colorado River for use by its customers.

Q. IS THIS HOW MUCH WATER THE CITY BILLED ALL OF ITS CUSTOMERS?

A. No. This is the amount of water the City diverted from the Colorado River. Some of this water is used during the treatment process and is not available for consumption by customers. There is also an amount of water that is lost from the distribution system before it can be delivered to customers' meters.

Q. HOW MUCH POTABLE WATER WAS DELIVERED TO THE CITY'S CUSTOMERS?

A. During the 2018 test year, AW delivered approximately 41.4 billion gallons of water or 127,025 acre-feet of water to its customers.

Q. DOES THIS INCLUDE WATER USED BY WHOLESALE CUSTOMERS OF THE CITY?

A. Yes, it does.

Q. HOW MUCH POTABLE WATER DID AW DELIVER TO ITS WHOLESALE CUSTOMERS DURING THE 2018 TEST YEAR?

A. AW delivered approximately 2.5 billion gallons or 7,547 acre-feet of water to its wholesale customers during the 2018 test year.

Q. DOES THE 127,025 ACRE-FEET OF POTABLE WATER DELIVERED TO AW CUSTOMERS INCLUDE WATER REUSE AMOUNTS?

A. No. The total water demand within AW's service area would include both the potable water delivered to its customers plus the amount of reuse water provided to customers. During the 2018 test year, AW delivered 4,465 acre-feet of reuse water to its customers. As a result, the total amount of water used by AW customers during the 2018 test year was 42.9 billion gallons or 134,572 acre-feet.

Q. DO THE WHOLESALE WATER CUSTOMERS HAVE DIRECT ACCESS TO REUSE WATER?

A. Not to my knowledge.

Q. DO THE WHOLESALE WATER CUSTOMERS HAVE THEIR OWN WATER RIGHTS?

A. Not to my knowledge.

Q. WHO IS RESPONSIBLE FOR WATER SUPPLY PLANNING FOR THE WHOLESALE WATER CUSTOMERS?

A. Under the current wholesale contracts, the City has planned water supplies for the wholesale customers.

Q. ARE THERE ANY LIMITATIONS ON HOW MUCH WATER AUSTIN MUST BE PREPARED TO SUPPLY TO ITS WHOLESALE CUSTOMERS OR FOR HOW LONG THOSE SUPPLIES MUST BE AVAILABLE?

A. Currently most of the wholesale customer contracts do not contain limits on the volume of water for which Austin is contracted to deliver. A few of the newer contracts may contain limitations on the volume of water that Austin is to deliver. All the contracts have an expiration date beyond which Austin is not obligated to plan for the wholesale customer's water supply.

Q. HOW MUCH WATER DOES AUSTIN HAVE AVAILABLE TO PROVIDE TO ITS CUSTOMERS?

A. The City has the right to divert run-of-river water from the Colorado River at various diversion points. However, this is water that is subject to availability under the Texas water rights priority system and may not always be available in the quantities needed by the City. In 1999, the City entered into a contract with the Lower Colorado River Authority (LCRA) to make stored water from the Highland Lakes, or other sources, available to Austin such that the City would have firm water supplies up to 325,000 acre-feet per year. The City prepaid for the reservation and use of this firm water. Under the agreement, AW paid $100 million to LCRA. In return, LCRA agreed that the City would not be charged again for water diversions from the Colorado River by the City until those diversions exceeded 201,000 acre-feet per year for two consecutive years. The City and LCRA entered a separate agreement in 2007 and agreed that the two entities would jointly plan for water supplies of an additional 250,000 acre-feet per year to increase the available water to Austin to 575,000 acre-feet per year.

Q. IF THE CITY HAS A FIRM SUPPLY OF 325,000 ACRE-FEET PER YEAR AND ONLY DIVERTED 151,028 ACRE-FEET DURING FY 2018, WHY DOES AW CONTINUE TO PLAN FOR AND DEVELOP NEW WATER SUPPLIES?

A. Austin continues to plan for and develop new water supplies to prepare for continued growth, more severe droughts, and climate uncertainties. Drought response in particular is one of the main reasons AW is pursuing the use of reclaimed water. Reclaimed water is a drought resistant supply of water. As an example of the importance of reclaimed water, LCRA notified its firm customers in 2011 that it was preparing for the potential of declaring a twenty percent pro-rata curtailment in the amount of water allotted to its firm customers in response to the historic drought conditions occurring at that time. The reductions were to be based off the consumption rates for the prior year, as opposed to contracted rates. The fact that the City had paid in advance for a firm supply of water did not protect it from the possibility of running low on water during the severe drought, thus emphasizing the value of developing its own, drought resistant supplies, such as reclaimed water.

Q. WOULD THE WHOLESALE CUSTOMERS HAVE BEEN AFFECTED BY THE PRO-RATA CURTAILMENT?

A. Yes, the wholesale customers would have been required to reduce their consumption by the same percentage as the City was required to reduce.

Q. HOW WAS AW GOING TO ACHIEVE THE REDUCTION IN WATER DEMANDS TO MATCH THE PROPOSED CURTAILMENT?

A. Fortunately, AW had proactively begun several programs to reduce water demands even before the drought began. AW intensified these efforts as the drought deepened. LCRA recognized that some of their firm customers, like AW, had already done a lot

to conserve water, and that it was inappropriate for LCRA to require an equal reduction from those customers that had already invested in on-going water conservation or reuse while other customers might have done very little in these categories. As a result, the City was able to demonstrate that they had already reduced their demands during the referenced baseline year through conservation and reuse by 26,266 acre-feet per year. Based on this demonstration, Austin's prorate curtailment was set at 6 percent by LCRA.

Q. WOULD THE WHOLESALE CUSTOMERS HAVE BENEFITED FROM AUSTIN'S PROACTIVE DECISIONS TO REDUCE WATER CONSUMPTION?

A. Yes, the wholesale customers would have had to reduce their consumption by 6 percent as opposed to 20 percent because Austin had been proactive in their efforts to reduce water consumption through conservation and reuse.

Q. IS THE WATER REUSE PROGRAM ONE OF THE WAYS AUSTIN REDUCED CONSUMPTION?

A. Yes. LCRA specifically identified reuse as one of the activities that could be credited, and the benefit of this activity was available to the wholesale customers even though they did not have direct access to the reuse water.

Q. HOW DO UTILITIES DECIDE HOW MUCH WATER THEY NEED AND WHEN THEY NEED IT?

A. Planning for water supply varies from one utility to the next based on their population growth rates and current water supplies available to the utility. Utilities that are experiencing high growth rates need to look out further in determining their water

supply needs. Likewise, utilities where water resources are scarce or where there is competition for limited water resources also need to look further into the future. Finally, utilities have to take into account the reliability of their water supply resources in determining how much supply to develop and when it needs to be available. This is particularly true given the uncertainties of climate change and the severity of recent droughts experienced in the State of Texas.

In the State of Texas, many utilities are facing both rapid growth and scarce water resources. In response to these common conditions, the Texas Legislature passed legislation that requires a 50-year planning horizon for water supply in the State of Texas.

Q. ARE YOU FAMILIAR WITH THE CITY'S WATER SUPPLY PLAN?

A. Yes, I am. AW retained the services of APAI to assist them in establishing projected water needs as well as to evaluate alternative water supplies. I lead this planning activity for APAI. In addition, we were retained to assist AW with evaluating specific drought management alternatives in response to the significant drought the state experienced between 2008 and 2016.

Q. ARE YOU FAMILIAR WITH OTHER WATER SUPPLY PLANNING ACTIVITIES FOR THE REGION?

A. Yes, I am. APAI participated as a subconsultant in the development of the first Regional Water Plan for Region K, which includes Austin and the Lower Colorado River Basin. I lead APAI's work effort in this regard. Since that time, I have followed the development of updates to the plan and have reviewed the current plan, which was adopted in 2016.

I am also familiar with the Water Management Plan developed by LCRA and approved by the TCEQ.

Q. ARE THESE WATER SUPPLY PLANS REQUIRED TO INCLUDE WATER REUSE AS A COMPONENT?

A. The 75th Legislature adopted language concerning the Regional Water Planning process. The language requires that each regional water planning group consider reuse as an alternative water supply.[1] The law does not require that the Regional Water Planning Groups adopt water reuse as one of their water supply alternatives; although each of the 16 Regional Water Planning Groups does include water reuse as part of their regional water plan. In fact, the Regional Water Plans indicate that approximately 14 percent of the water needs in the State of Texas will be met by water reuse.[2]

Q. DO THESE WATER SUPPLY PLANNING DOCUMENTS CONSIDER WATER REUSE BY THE CITY?

A. Yes, all of the planning documents include direct, non-potable reuse by the City as a component of the overall water supply plan for the City and the region.

Q. DID THE CITY INITIATE WATER REUSE IN RESPONSE TO THESE PLANS AND THE LEGISLATIVE REQUIREMENTS FOR THE PLANS?

A. No. The City began water reuse activities in 1974, approximately 20 years before Senate Bill 1 requirements were promulgated.

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[1] See Attachment SJC-2.

[2] See Attachment SJC-3.

Q. HOW MUCH WATER IS AUSTIN CURRENTLY REUSING AND HOW MUCH DO THEY PLAN ON REUSING IN THE FUTURE?

A. Currently the City reuses approximately 1.5 billion gallons of water per year, or approximately 4,465 acre-feet of water per year. The City intends to expand the use of reuse to as much as 54,600 acre-feet per year as detailed in AW's Water Forward Plan.

Q. IS THERE A BENEFIT TO AUSTIN TO DEVELOP ITS REUSE SYSTEM NOW AS OPPOSED TO WAITING UNTIL THEIR WATER DEMAND IS CLOSER TO THE 325,000 ACRE-FEET IDENTIFIED IN THE CONTRACT WITH LCRA?

A. Yes, there is. The reduction in potable water demand resulting from the reuse system should help delay when the City will exceed the 201,000 acre-feet trigger where the City will begin paying LCRA for water diverted above 150,000 acre-feet. At the current LCRA rate for water of $145 per acre-feet, this is estimated to represent an annual cost of at least $7.4 million.

Q. ARE THERE OTHER REASONS THE CITY IS INTERESTED IN EXPANDING ITS REUSE SYSTEM NOW AS OPPOSED TO LATER?

A. Yes. The development of a new utility system can take many years to accomplish. This is both from the need to finance and construct the infrastructure that is needed, but also to identify and develop the customer base needed to achieve the goals of the system. In addition, decisions concerning water supplies and the possibility of using reclaimed water are typically made by developers and other large water customers as they plan their projects as it is generally more expensive to go back and retrofit the plumbing within a property to utilize reclaimed water. As a result, the sooner reclaimed water is available in an area, the larger the potential customer base will be in the future

as new development occurs. Waiting to develop the reclaimed water system would result in lost opportunities.

Q. HOW DOES THE VOLUME OF WATER REUSE IN AUSTIN COMPARE TO THE USE OF WATER BY WHOLESALE WATER CUSTOMERS AND THE PETITIONERS IN THIS CASE?

A. Austin delivered approximately 2.5 billion gallons or 7,547 acre-feet of water to its wholesale customers during the 2018 test year. The following is a list of the four petitioners involved in this case along with their water use in the 2018 test year.

1. North Austin MUD – 326.5 million gallons or 1,002 acre-feet
2. Northtown MUD – 291.8 million gallons or 895 acre-feet
3. WCID #10 – 827.4 million gallons or 2,539 acre-feet
4. Wells Branch MUD – 481.3 million gallons or 1,477 acre-feet

The total water supplied to the four petitioners in this case was 5,913 acre-feet in the 2018 test year.

The 4,465 acre-feet of water supply conserved by AW through reuse represents 75 percent of the water used by the petitioners in this case and 59.2 percent of the total wholesale water demand of 7,547 acre-feet.

Q. DO OTHER UTILITIES TRANSFER COSTS FROM THEIR REUSE SYSTEMS TO THEIR WATER FUND?

A. Yes, it is relatively common for this to happen. The AWWA Manual of Practice, M1 Principles of Water Rates, Fees, and Charges, 7th Edition includes the following:

> The addition of reuse can be beneficial to existing water and wastewater systems, serving as an alternative for effluent disposal and either "freeing" existing sources of water supply or avoiding/deferring additional water supply investment. As such,

> it is common for many utilities to subsidize a portion of reuse water costs from their water and/or wastewater systems, recognizing the net financial impact of reuse water to these systems.[3]
>
> Is the reuse facility needed to augment water supply or reduce current potable water usage per capita? If so, there is a logical argument that the deficit should be met by the water utility. *Although that would increase the cost to all potable customers, they also benefit from reuse through lower alternative supply costs.*[4]

Q. IN YOUR PROFESSIONAL OPINION, DO THE WHOLESALE CUSTOMERS RECEIVE A BENEFIT FROM THE REUSE SYSTEM?

A. Yes, they do. The wholesale customers have contracted with the City to provide for their water supply needs. The City has chosen to incorporate reuse as a part of their overall water supply portfolio and the wholesale customers indirectly benefit from the reuse system as a result.

Q. IF THE WHOLESALE CUSTOMERS ARE UNHAPPY WITH THE MANNER IN WHICH AUSTIN IS PLANNING FOR THEIR WATER NEEDS, DO THEY HAVE ALTERNATIVES AVAILABLE TO THEM?

A. Yes, the wholesale customers could obtain their own raw water supplies and contract with the City to treat and transport that water.

Q. DOES THIS CONCLUDE YOUR PREFILED TESTIMONY?

A. Yes.

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[3] American Water Works Association, Manual of Practice, M1, Principles of Water Rates, Fees, and Charges, 181 (7th ed. 2017).

[4] *Id.* at 183-84 (emphasis added).

Stephen J. Coonan, PE
Alan Plummer Associates, Inc.

Years of Experience with APAI: 27
Total Years of Experience: 36

Education:
Bachelor of Science, Civil Engineering, Missouri University of Science & Technology (U of MO- Rolla),1982

Registration:
Professional Engineer,NC, No.044230 2016
Professional Engineer,TX, No.65516 1989

Memberships/Associations:
Water Environment Association of Texas
Served as President 2014-2015
Current Senior Texas Delegate to WEF
Water Environment Federation

Honors and Awards:
WEAT – Arthur Sidney Bidell Award - 2019

General Summary
Steve, a principal in the firm and manager of the Austin office, has over 36 years of professional engineering experience in the various aspects of wastewater treatment, wastewater management, reclaimed water use, potable water production/distribution, water supply planning and drainage improvements. He currently serves as the Senior Delegate from the State of Texas to the Water Environment Association and has previously contributed to the industry through serving as the past President of the Water Environment Association of Texas, member of the Texas Commission on Environmental Quality Task Force to write the rules governing the use of reclaimed water in Texas, and numerous paper presentations at Technical Conferences. The following are samples of the projects that Steve has lead.

City of Austin Water Conservation Planning

As project manager, Steve evaluated potential new water conservation programs for both short-term and long-term water savings for the City of Austin's Water Conservation Evaluation. More than 100 potential water conservation measures were screened for

short- and long-term water savings potential, evaluation of the potential water savings, estimation of potential costs, and discussion of implementation issues.

Regional Water Planning – Region K
Steve was the APAI project manager for the Region K Regional Planning Project. He was responsible for developing water management strategies, a conceptual design, and an opinion of cost. The project involved determining the current and future regional population and water demands, verifying available water supplies, identifying water surpluses and shortages, and developing water management strategies.

City of Austin Drought Feasibility Engineering Assessment
Steve served as APAI's project manager for the evaluation of four alternative water supply projects for the City of Austin. These projects all involved the use of reclaimed water. Three of the projects involved indirect potable reuse while the fourth alternative involved using reclaimed water to augment environmental flows so that stored water could be conserved.

City of San Marcos Water Master Plan
Steve has served the City of San Marcos on numerous Water Master Planning projects. He has completed Master Plans of the City's treatment and distribution systems as well as the overall water supply for the City.

City of San Marcos Reuse Master Plan
Steve served as the Project Manager for the development of reclaimed water master plan for the City of San Marcos. In this project he identified potential uses for reclaimed water as well as the infrastructure that would be needed to provide the service to the customers.

City of San Marcos TXI Reclaimed Water Line
Steve was the manager in charge of the design of approximately 17,000 linear feet of 12-inch diameter pipeline to provide reclaimed water to several industries south of the City. The project also included improvements at the wastewater treatment plant to facilitate the delivery of the reclaimed water.

Lower Valley Water District Water and Wastewater Master Plans
Steve was the project manager for the development of Water and Wastewater Master Plans for the Lower Valley Water District. The District provides service to approximately 35,000 residents southeast of El Paso. As part of the study, Steve evaluated alternatives for indirect potable reuse as a water supply option for the District.

Windmill Ranch Wastewater Treatment Plant Reclaimed Water Use, Lower Colorado River Authority
Steve served as principal-in-charge for the new 0.25-mgd Windmill Ranch Wastewater Treatment Plant. This was the second MBR plant in the State. This design project

included a lift station, force main, administration building, ultraviolet disinfection, and a reclaimed water pump station and line to serve a new resort development in Bastrop County.

San Angelo Reclaimed Water Feasibility Study, City of San Angelo
Steve served as the project manager for the development of a reclaimed water master plan for the City of San Angelo. The project involved identifying potential users of a reclaimed system, developing projections of demands for reclaimed water, and identifying the improvements needed to supply the reclaimed water to the customers. The City undertook the reclaimed water master plan as one of several strategies to meet the demands for water in the arid environment.

Las Colinas Urban System Model, Dallas County Utility and Reclamation District
Steve was responsible for the master plan for the Dallas County Utility and Reclamation District reclaimed water distribution system. The plan was developed using Cybernet computer software. He was also project manager for the D/FW International Airport Raw Water Study. This project was a cooperative study undertaken by the Dallas County Utility and Reclamation District and the D/FW International Airport Board. The study evaluated alternative sources of water to meet the nonpotable demands at the airport and its major tenants surrounding the airport.

Lake Buchanan Regional Water Planning Projects, Lower Colorado River Authority
Steve served as project manager for the feasibility study and preliminary engineering study for a regional water system on Lake Buchanan. Several small utilities surrounding Lake Buchanan were experiencing water quality problems with their established groundwater supplies. This project included the development of a regional surface water system to supply the needs of these entities. Steve evaluated existing and future demands within the proposed service area. Based on the future demands, a single water treatment plant was recommended. The project also included approximately 25 miles of pipeline as well as a 3,500-linear-foot crossing of Lake Buchanan and two storage tanks.

Kerr County Regional Water System, Upper Guadalupe River Authority
Steve served as the project manager for the feasibility study and the preliminary engineering phase of the Kerr County Regional Water System project. This project included the development of a new surface water treatment plant and distribution system to provide potable water to communities in Kerr County. These communities were experiencing failing groundwater supplies with continued growth. Steve evaluated a feasible service area for the regional system and developed demand projections for the proposed system as well as planning for the raw water intake, treatment plant, booster pump station, and distribution system.

remedy or prevent the violation. A cause of action brought under this subsection must be filed in a district court in Travis County or in the county in which the action is proposed or occurring.

(i) For purposes of this section, the acquisition of fee title or an easement by a political subdivision for the purpose of providing retail public utility service to property in the reservoir site or allowing an owner of property in the reservoir site to improve or develop the property may not be considered a significant impairment that prevents the construction of a reservoir site under Subsection (g). A fee title or easement acquired under this subsection may not be considered the basis for preventing the future acquisition of land needed to construct a reservoir on a designated site.

Amended by Acts 1977, 65th Leg., p. 2207, ch. 870, Sec. 1, eff. Sept. 1, 1977; Acts 1985, 69th Leg., ch. 795, Sec. 1.046, eff. Sept. 1, 1985; Acts 1991, 72nd Leg., ch. 516, Sec. 4, eff. Sept. 1, 1991; Acts 1997, 75th Leg., ch. 1010, Sec. 1.01, eff. Sept. 1, 1997; Acts 1999, 76th Leg., ch. 456, Sec. 4, eff. June 18, 1999; Acts 1999, 76th Leg., ch. 979, Sec. 4, eff. June 18, 1999; Acts 1999, 76th Leg., ch. 1223, Sec. 2, eff. June 18, 1999; Acts 2001, 77th Leg., ch. 966, Sec. 2.16, eff. Sept. 1, 2001.
Amended by:

Acts 2007, 80th Leg., R.S., Ch. 1430 (S.B. 3), Sec. 3.01, eff. September 1, 2007.

Acts 2007, 80th Leg., R.S., Ch. 1430 (S.B. 3), Sec. 4.01, eff. June 16, 2007.

Acts 2011, 82nd Leg., R.S., Ch. 1233 (S.B. 660), Sec. 8, eff. September 1, 2011.

Acts 2017, 85th Leg., R.S., Ch. 921 (S.B. 1511), Sec. 2, eff. September 1, 2017.

Sec. 16.053. REGIONAL WATER PLANS. (a) The regional water planning group in each regional water planning area shall prepare a regional water plan, using an existing state water plan identified in Section 16.051 of this code and local water plans prepared under Section 16.054 of this code as a guide, if present, that provides for the orderly development, management, and conservation of water

resources and preparation for and response to drought conditions in order that sufficient water will be available at a reasonable cost to ensure public health, safety, and welfare; further economic development; and protect the agricultural and natural resources of that particular region.

(b) No later than September 1, 1998, the board shall designate the areas for which regional water plans shall be developed, taking into consideration such factors as river basin and aquifer delineations, water utility development patterns, socioeconomic characteristics, existing regional water planning areas, political subdivision boundaries, public comment, and other factors the board deems relevant. The board shall review and update the designations as necessary but at least every five years.

(c) No later than 60 days after the designation of the regions under Subsection (b), the board shall designate representatives within each regional water planning area to serve as the initial coordinating body for planning. The initial coordinating body may then designate additional representatives to serve on the regional water planning group. The initial coordinating body shall designate additional representatives if necessary to ensure adequate representation from the interests comprising that region, including the public, counties, municipalities, industries, agricultural interests, environmental interests, small businesses, electric generating utilities, river authorities, water districts, and water utilities. The regional water planning group shall maintain adequate representation from those interests. In addition, the groundwater conservation districts located in each management area, as defined by Section 36.001, located in the regional water planning area shall appoint one representative of a groundwater conservation district located in the management area and in the regional water planning area to serve on the regional water planning group. In addition, representatives of the board, the Parks and Wildlife Department, the Department of Agriculture, and the State Soil and Water Conservation Board shall serve as ex officio members of each regional water planning group.

(d) The board shall provide guidelines for the consideration of existing regional planning efforts by regional water planning

groups. The board shall provide guidelines for the format in which information shall be presented in the regional water plans.

(e) Each regional water planning group shall submit to the development board a regional water plan that:

(1) is consistent with the guidance principles for the state water plan adopted by the development board under Section 16.051(d);

(2) provides information based on data provided or approved by the development board in a format consistent with the guidelines provided by the development board under Subsection (d);

(2-a) is consistent with the desired future conditions adopted under Section 36.108 for the relevant aquifers located in the regional water planning area as of the most recent deadline for the board to adopt the state water plan under Section 16.051 or, at the option of the regional water planning group, established subsequent to the adoption of the most recent plan; provided, however, that if no groundwater conservation district exists within the area of the regional water planning group, the regional water planning group shall determine the supply of groundwater for regional planning purposes; the Texas Water Development Board shall review and approve, prior to inclusion in the regional water plan, that the groundwater supply for the regional planning group without a groundwater conservation district in its area is physically compatible, using the board's groundwater availability models, with the desired future conditions adopted under Section 36.108 for the relevant aquifers in the groundwater management area that are regulated by groundwater conservation districts;

(3) identifies:

(A) each source of water supply in the regional water planning area, including information supplied by the executive administrator on the amount of modeled available groundwater in accordance with the guidelines provided by the development board under Subsections (d) and (f);

(B) factors specific to each source of water supply to be considered in determining whether to initiate a drought response;

(C) actions to be taken as part of the response; and

(D) existing major water infrastructure facilities that may be used for interconnections in the event of an emergency shortage of water;

(4) has specific provisions for water management strategies to be used during a drought of record;

(5) includes but is not limited to consideration of the following:

(A) any existing water or drought planning efforts addressing all or a portion of the region and potential impacts on public health, safety, or welfare in this state;

(B) approved groundwater conservation district management plans and other plans submitted under Section 16.054;

(C) all potentially feasible water management strategies, including but not limited to improved conservation, reuse, and management of existing water supplies, conjunctive use, acquisition of available existing water supplies, and development of new water supplies;

(D) protection of existing water rights in the region;

(E) opportunities for and the benefits of developing regional water supply facilities or providing regional management of water supply facilities;

(F) appropriate provision for environmental water needs and for the effect of upstream development on the bays, estuaries, and arms of the Gulf of Mexico and the effect of plans on navigation;

(G) provisions in Section 11.085(k)(1) if interbasin transfers are contemplated;

(H) voluntary transfer of water within the region using, but not limited to, regional water banks, sales, leases, options, subordination agreements, and financing agreements;

(I) emergency transfer of water under Section 11.139, including information on the part of each permit, certified filing, or certificate of adjudication for nonmunicipal use in the region that may be transferred without causing unreasonable damage to the property of the nonmunicipal water rights holder; and

(J) opportunities for and the benefits of developing large-scale desalination facilities for:

(i) marine seawater that serve local or regional entities; and

(ii) seawater or brackish groundwater that serve local or regional brackish groundwater production zones identified and designated under Section 16.060(b)(5);

(6) identifies river and stream segments of unique ecological value and sites of unique value for the construction of reservoirs that the regional water planning group recommends for protection under Section 16.051;

(7) assesses the impact of the plan on unique river and stream segments identified in Subdivision (6) if the regional water planning group or the legislature determines that a site of unique ecological value exists;

(8) describes the impact of proposed water projects on water quality; and

(9) includes information on:

(A) projected water use and conservation in the regional water planning area; and

(B) the implementation of state and regional water plan projects, including water conservation strategies, necessary to meet the state's projected water demands.

(e-1) On request of the Texas Water Advisory Council, a regional planning group shall provide the council a copy of that planning group's regional water plan.

(f) No later than September 1, 1998, the board shall adopt rules:

(1) to provide for the procedures for adoption of regional water plans by regional water planning groups and for approval of regional water plans by the board; and

(2) to govern procedures to be followed in carrying out the responsibilities of this section.

(g) The board shall provide technical and financial assistance to the regional water planning groups in the development of their plans. The board shall simplify, as much as possible, planning requirements in regions with abundant water resources. The board, if requested, may facilitate resolution of conflicts within regions.

(h)(1) Prior to the preparation of the regional water plan, the regional water planning group shall, after notice, hold at least

one public meeting at some central location readily accessible to the public within the regional water planning area to gather suggestions and recommendations from the public as to issues that should be addressed in the plan or provisions that should be considered for inclusion in the plan.

(2) The regional water planning group shall provide an ongoing opportunity for public input during the preparation of the regional water plan.

(3) After the regional water plan is initially prepared, the regional water planning group shall, after notice, hold at least one public hearing at some central location readily accessible to the public within the regional water planning area. The group shall make copies of the plan available for public inspection at least one month before the hearing by providing a copy of the plan in the county courthouse and at least one public library of each county having land in the region. Notice for the hearing shall include a listing of these and any other location where the plan is available for review.

(4) After the regional water plan is initially prepared, the regional water planning group shall submit a copy of the plan to the board. The board shall submit comments on the regional water plan as to whether the plan meets the requirements of Subsection (e) of this section.

(5) If no interregional conflicts exist, the regional water planning group shall consider all public and board comments; prepare, revise, and adopt the final plan; and submit the adopted plan to the board for approval and inclusion in the state water plan.

(6) If an interregional conflict exists, the board shall facilitate coordination between the involved regions to resolve the conflict. If conflict remains, the board shall resolve the conflict. On resolution of the conflict, the involved regional water planning groups shall prepare revisions to their respective plans and hold, after notice, at least one public hearing at some central location readily accessible to the public within their respective regional water planning areas. The regional water planning groups shall consider all public and board comments; prepare, revise, and adopt their respective plans; and submit their

plans to the board for approval and inclusion in the state water plan.

(7) The board may approve a regional water plan only after it has determined that:

(A) all interregional conflicts involving that regional water planning area have been resolved;

(B) the plan includes water conservation practices and drought management measures incorporating, at a minimum, the provisions of Sections 11.1271and 11.1272; and

(C) the plan is consistent with long-term protection of the state's water resources, agricultural resources, and natural resources as embodied in the guidance principles adopted under Section 16.051(d).

(8) Notice required by Subdivision (1), (3), or (6) of this subsection must be:

(A) published once in a newspaper of general circulation in each county located in whole or in part in the regional water planning area before the 30th day preceding the date of the public meeting or hearing; and

(B) mailed to:

(i) each mayor of a municipality with a population of 1,000 or more that is located in whole or in part in the regional water planning area;

(ii) each county judge of a county located in whole or in part in the regional water planning area;

(iii) each special or general law district or river authority with responsibility to manage or supply water in the regional water planning area;

(iv) each retail public utility that:

(a) serves any part of the regional water planning area; or

(b) receives water from the regional water planning area; and

(v) each holder of record of a permit, certified filing, or certificate of adjudication for the use of surface water the diversion of which occurs in the regional water planning area.

(9) Notice published or mailed under Subdivision (8) of this subsection must contain:

(A) the date, time, and location of the public meeting or hearing;

(B) a summary of the proposed action to be taken;

(C) the name, telephone number, and address of the person to whom questions or requests for additional information may be submitted; and

(D) information on how the public may submit comments.

(10) The regional water planning group may amend the regional water plan after the plan has been approved by the board. If, after the regional water plan has been approved by the board, the plan includes a water management strategy or project that ceases to be feasible, the regional water planning group shall amend the plan to exclude that water management strategy or project and shall consider amending the plan to include a feasible water management strategy or project in order to meet the need that was to be addressed by the infeasible water management strategy or project. For purposes of this subdivision, a water management strategy or project is considered infeasible if the proposed sponsor of the water management strategy or project has not taken an affirmative vote or other action to make expenditures necessary to construct or file applications for permits required in connection with the implementation of the water management strategy or project under federal or state law on a schedule that is consistent with the completion of the implementation of the water management strategy or project by the time the water management strategy or project is projected by the regional water plan or the state water plan to be needed. Subdivisions (1)-(9) apply to an amendment to the plan in the same manner as those subdivisions apply to the plan.

(11) This subdivision applies only to an amendment to a regional water plan approved by the board. This subdivision does not apply to the adoption of a subsequent regional water plan for submission to the board as required by Subsection (i). Notwithstanding Subdivision (10), the regional water planning group may amend the plan in the manner provided by this subdivision if the executive administrator makes a written determination that the proposed amendment qualifies for adoption in the manner provided by this subdivision before the regional water planning group votes on

adoption of the amendment. A proposed amendment qualifies for adoption in the manner provided by this subdivision only if the amendment is a minor amendment, as defined by board rules, that will not result in the overallocation of any existing or planned source of water, does not relate to a new reservoir, and will not have a significant effect on instream flows or freshwater inflows to bays and estuaries. If the executive administrator determines that a proposed amendment qualifies for adoption in the manner provided by this subdivision, the regional water planning group may adopt the amendment at a public meeting held in accordance with Chapter 551, Government Code. The proposed amendment must be placed on the agenda for the meeting, and notice of the meeting must be given in the manner provided by Chapter 551, Government Code, at least two weeks before the date the meeting is held. The public must be provided an opportunity to comment on the proposed amendment at the meeting.

(12) Each regional water planning group and any committee or subcommittee of a regional water planning group are subject to Chapters 551and 552, Government Code.

(i) The regional water planning groups shall submit their adopted regional water plans to the board by January 5, 2001, for approval and inclusion in the state water plan. In conjunction with the submission of regional water plans, each planning group should make legislative recommendations, if any, to facilitate more voluntary water transfers in the region. Subsequent regional water plans shall be submitted at least every five years thereafter, except that a regional water planning group may elect to implement simplified planning, no more often than every other five-year planning cycle, and in accordance with guidance to be provided by the board, if the group determines that, based on its own initial analyses using updated groundwater and surface water availability information, there are no significant changes to the water availability, water supplies, or water demands in the regional water planning area. At a minimum, simplified planning will require updating groundwater and surface water availability values in the regional water plan, meeting any other new statutory or other planning requirements that come into effect during each five-year planning cycle, and formally adopting and submitting the regional

water plan for approval. Public participation for revised regional plans shall follow the procedures under Subsection (h).

(j) The board may provide financial assistance to political subdivisions under Subchapters E and F of this chapter, Subchapters C, D, E, F, J, O, Q, and R, Chapter 15, and Subchapters D, I, K, and L, Chapter 17, for water supply projects only if:

(1) the board determines that the needs to be addressed by the project will be addressed in a manner that is consistent with the state water plan;

(2) beginning January 5, 2002, the board:

(A) has approved a regional water plan as provided by Subsection (i), and any required updates of the plan, for the region of the state that includes the area benefiting from the proposed project; and

(B) determines that the needs to be addressed by the project will be addressed in a manner that is consistent with that regional water plan; and

(3) the board finds that the water audit required under Section 16.0121 has been completed and filed.

(k) The board may waive the requirements of Subsection (j) of this section if the board determines that conditions warrant the waiver.

(l) A political subdivision may contract with a regional water planning group to assist the regional water planning group in developing or revising a regional water plan.

(m) A cause of action does not accrue against a regional water planning group, a representative who serves on the regional water planning group, or an employee of a political subdivision that contracts with the regional water planning group under Subsection (l) for an act or omission in the course and scope of the person's work relating to the regional water planning group.

(n) A regional water planning group, a representative who serves on the regional water planning group, or an employee of a political subdivision that contracts with the regional water planning group under Subsection (l) is not liable for damages that may arise from an act or omission in the course and scope of the person's work relating to the regional water planning group.

(o) The attorney general, on request, shall represent a regional water planning group, a representative who serves on the regional water planning group, or an employee of a political subdivision that contracts with the regional water planning group under Subsection (l) in a suit arising from an act or omission relating to the regional water planning group.

(p) If a groundwater conservation district files a petition with the development board stating that a conflict requiring resolution may exist between the district's approved management plan developed under Section 36.1071 and an approved state water plan, the development board shall provide technical assistance to and facilitate coordination between the district and the involved region to resolve the conflict. Not later than the 45th day after the date the groundwater conservation district files a petition with the development board, if the conflict has not been resolved, the district and the involved region shall mediate the conflict. The district and the involved region may seek the assistance of the Center for Public Policy Dispute Resolution at The University of Texas School of Law or an alternative dispute resolution system established under Chapter 152, Civil Practice and Remedies Code, in obtaining a qualified impartial third party to mediate the conflict. The cost of the mediation services must be specified in the agreement between the parties and the Center for Public Policy Dispute Resolution or the alternative dispute resolution system. If the district and the involved region cannot resolve the conflict through mediation, the development board shall resolve the conflict not later than the 60th day after the date the mediation is completed as provided by Subsections (p-1) and (p-2).

(p-1) If the development board determines that resolution of the conflict requires a revision of an approved regional water plan, the development board shall suspend the approval of that plan and provide information to the regional water planning group. The regional water planning group shall prepare any revisions to its plan specified by the development board and shall hold, after notice, at least one public hearing at some central location readily accessible to the public within the regional water planning area. The regional water planning group shall consider all public and development board comments, prepare, revise, and adopt its plan, and

submit the revised plan to the development board for approval and inclusion in the state water plan.

(p-2) If the development board determines that resolution of the conflict requires a revision of the district's approved groundwater conservation district management plan, the development board shall provide information to the district. The groundwater district shall prepare any revisions to its plan based on the information provided by the development board and shall hold, after notice, at least one public hearing at some central location readily accessible to the public within the district. The groundwater district shall consider all public and development board comments, prepare, revise, and adopt its plan, and submit the revised plan to the development board.

(p-3) If the groundwater conservation district disagrees with the decision of the development board under Subsection (p), the district may appeal the decision to a district court in Travis County. Costs for the appeal shall be set by the court hearing the appeal. An appeal under this subsection is by trial de novo.

(p-4) On the request of the involved region or groundwater conservation district, the development board shall include discussion of the conflict and its resolution in the state water plan that the development board provides to the governor, the lieutenant governor, and the speaker of the house of representatives under Section 16.051(e).

(q) Each regional planning group shall examine the financing needed to implement the water management strategies and projects identified in the group's most recent approved regional plan and, not later than June 1, 2002, shall report to the board regarding:

(1) how local governments, regional authorities, and other political subdivisions in the region propose to pay for water infrastructure projects identified in the plan; and

(2) what role the regional planning group proposes for the state in financing projects identified in the plan, giving particular attention to proposed increases in the level of state participation in funding for regional projects to meet needs beyond the reasonable financing capability of local governments, regional authorities, and other political subdivisions involved in building water infrastructure.

Text of subsection as added by Acts 2005, 79th Leg., R.S., Ch. 1200 (H.B. 578), Sec. 1

(r) Information described by Subsection (e)(3)(D) that is included in a regional water plan submitted to the board is excepted from required disclosure under the public information law, Chapter 552, Government Code.

Text of subsection as added by Acts 2005, 79th Leg., R.S., Ch. 1097 (H.B. 2201), Sec. 8 and amended by Acts 2007, 80th Leg., R.S., Ch. 1430 (S.B. 3), Sec. 2.15

(r) The board by rule shall provide for reasonable flexibility to allow for a timely amendment of a regional water plan, the board's approval of an amended regional water plan, and the amendment of the state water plan. If an amendment under this subsection is to facilitate planning for water supplies reasonably required for a clean coal project, as defined by Section 5.001, the rules may allow for amending a regional water plan without providing notice and without a public meeting or hearing under Subsection (h) if the amendment does not:

(1) significantly change the regional water plan, as reasonably determined by the board; or

(2) adversely affect other water management strategies in the regional water plan.

Amended by Acts 1977, 65th Leg., p. 2207, ch. 870, Sec. 1, eff. Sept. 1, 1977; Acts 1985, 69th Leg., ch. 795, Sec. 1.047, eff. Sept. 1, 1985; Acts 1997, 75th Leg., ch. 1010, Sec. 1.02, eff. Sept. 1, 1997; Acts 1999, 76th Leg., ch. 456, Sec. 5, eff. June 18, 1999; Acts 1999, 76th Leg., ch. 979, Sec. 5, eff. June 18, 1999; Acts 1999, 76th Leg., ch. 1180, Sec. 1, eff. June 18, 1999; Acts 1999, 76th Leg., ch. 1222, Sec. 2, eff. June 18, 1999; Acts 1999, 76th Leg., ch. 1223, Sec. 3, eff. June 18, 1999; Acts 2001, 77th Leg., ch. 966, Sec. 2.17 to 2.19, eff. Sept. 1, 2001; Acts 2001, 77th Leg., ch. 1234, Sec. 25, eff. Sept. 1, 2001; Acts 2003, 78th

Leg., ch. 744, Sec. 2, eff. Sept. 1, 2003; Acts 2003, 78th Leg., ch. 1057, Sec. 5, eff. June 20, 2003; Acts 2003, 78th Leg., ch. 1275, Sec. 3(45), eff. Sept. 1, 2003.

Amended by:

Acts 2005, 79th Leg., Ch. 970 (H.B. 1763), Sec. 1, eff. September 1, 2005.

Acts 2005, 79th Leg., Ch. 1097 (H.B. 2201), Sec. 8, eff. June 18, 2005.

Acts 2005, 79th Leg., Ch. 1200 (H.B. 578), Sec. 1, eff. September 1, 2005.

Acts 2007, 80th Leg., R.S., Ch. 1430 (S.B. 3), Sec. 2.14, eff. September 1, 2007.

Acts 2007, 80th Leg., R.S., Ch. 1430 (S.B. 3), Sec. 2.15, eff. September 1, 2007.

Acts 2011, 82nd Leg., R.S., Ch. 595 (S.B. 181), Sec. 1, eff. June 17, 2011.

Acts 2011, 82nd Leg., R.S., Ch. 1233 (S.B. 660), Sec. 9, eff. September 1, 2011.

Acts 2015, 84th Leg., R.S., Ch. 756 (H.B. 2031), Sec. 9, eff. June 17, 2015.

Acts 2015, 84th Leg., R.S., Ch. 990 (H.B. 30), Sec. 2, eff. June 19, 2015.

Acts 2015, 84th Leg., R.S., Ch. 1180 (S.B. 1101), Sec. 1, eff. September 1, 2015.

Acts 2017, 85th Leg., R.S., Ch. 7 (S.B. 347), Sec. 1, eff. September 1, 2017.

Acts 2017, 85th Leg., R.S., Ch. 324 (S.B. 1488), Sec. 19.001, eff. September 1, 2017.

Acts 2017, 85th Leg., R.S., Ch. 471 (H.B. 2215), Sec. 1, eff. June 9, 2017.

Acts 2017, 85th Leg., R.S., Ch. 921 (S.B. 1511), Sec. 3, eff. September 1, 2017.

Acts 2017, 85th Leg., R.S., Ch. 921 (S.B. 1511), Sec. 4, eff. September 1, 2017.

Acts 2017, 85th Leg., R.S., Ch. 921 (S.B. 1511), Sec. 5, eff. September 1, 2017.

Figure ES.6 - Share of recommended water management strategies by water resource in 2070

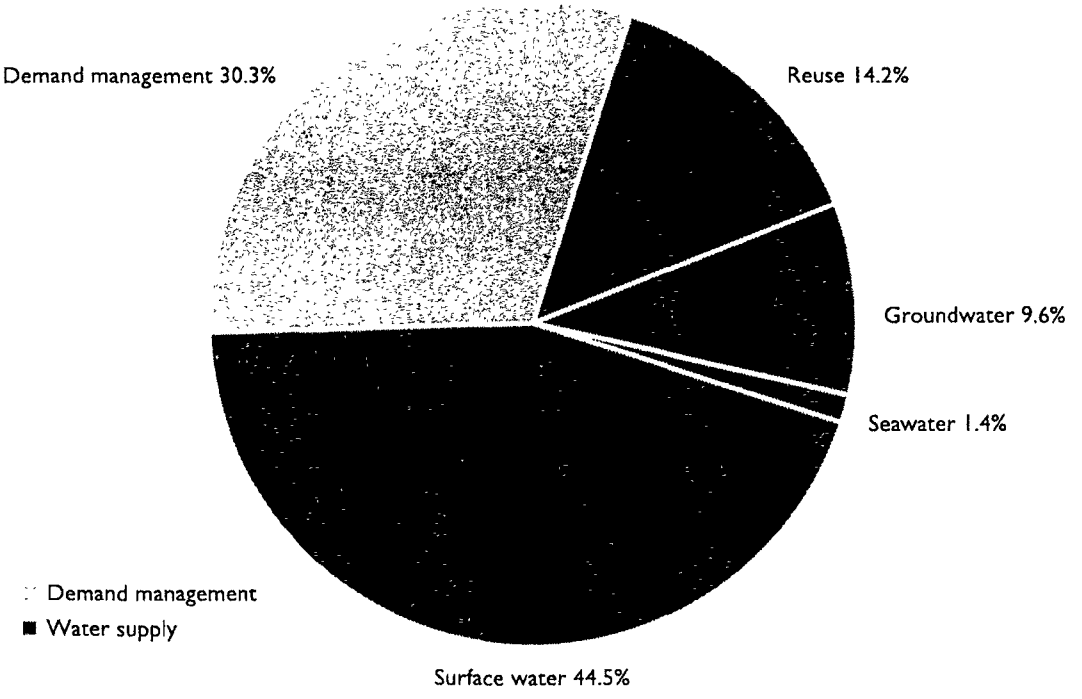
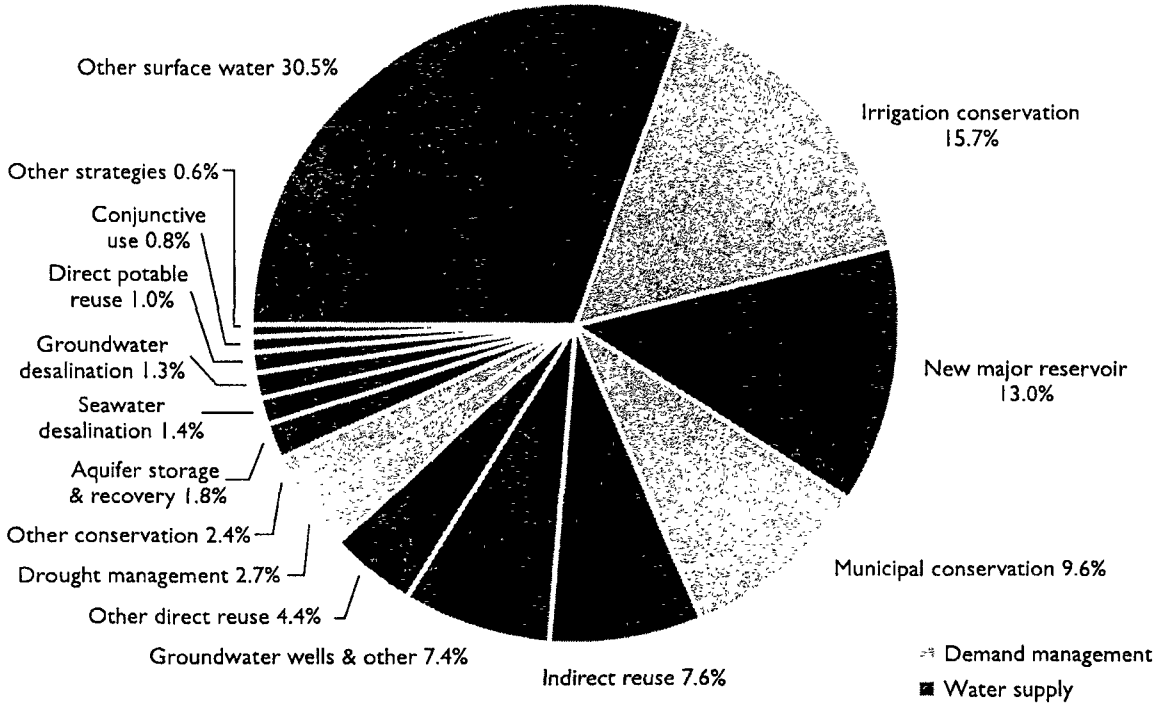


Figure ES.7 - Share of recommended water management strategies by strategy type in 2070



One option for utilities interested in providing reuse water is to connect the most economically feasible customers first. Generally, the most economically feasible reuse customers are high-volume users that use water for nonpotable purposes and are located near the reuse water source point. Examples of these types of customers could be golf courses, athletic facilities, large green spaces, and power generation facilities requiring cooling water. Connecting these customers first allows the greatest volume of reuse water distribution with the least capital investment. After the initial transmission mains are constructed to connect these customers, additional reuse customers can be added to the existing reuse transmission infrastructure. Additionally, as discussed further below, providing reuse water to high-volume users that are not currently purchasing potable water from the utility enhances the economic feasibility of providing reuse, because it will not affect potable water and/or wastewater revenues of the utility.

A utility must carefully evaluate and balance the targeted customer base with governing policies that promote water reuse. There are instances where a reuse customer may be a beneficial addition to the reuse system; however, the policies that govern reuse system rules and standards do not provide financial benefits to the customer. In addition, utilities need to have governing policies for the needs of both types of customers: the developer building the facility and the customer who will own the facility. The policies will affect these customers differently. For example, requiring a developer to pay for extending reuse infrastructure to the property while paying an impact fee is cost prohibitive, especially when potable water may be readily available. This policy may be balanced with a lower-than-potable-rate incentive to encourage use. However, the developer does not benefit from that; the end-use customer will see the savings.

Because of the high initial cost of installing reuse infrastructure, debt is an important component in the financial planning process. Infrastructure must be constructed and operational before customers can connect and revenues are generated. Utilities will often use debt as a means to offset the initial construction costs and spread these costs over future years when revenues are forecasted to be available.

Although the use of debt is the most commonly used funding option, there are other sources of available funding. Other common sources of funding include grants, special assessments, and developer-contributed assets or impact fees. Several grant programs are available for water reuse projects at the federal, state, regional, and local levels. The primary federal and state-level funding program includes the Clean Water State Revolving Fund and the Drinking Water State Revolving Fund. At the state level, grants may be available from regulatory bodies, such as local water management districts, with an interest in promoting reuse. Special assessments can also be used to fund reuse projects where these projects would benefit a specific service area of the system. Utilities may require the developer to construct reuse systems within new developments and dedicate these assets to the utility after construction. In some instances, a utility may provide loan assistance to the developer to mitigate up-front capital costs. Other special assessments may include an availability charge for all customers who have reuse service available in their area.

The addition of reuse can be beneficial to existing water and wastewater systems, serving as an alternative for effluent disposal and either "freeing" existing sources of water supply or avoiding/deferring additional water supply investment. As such, it is common for many utilities to subsidize a portion of reuse water costs from their water and/or wastewater systems, recognizing the net financial impact of reuse water to these systems.

An aspect of reuse water that all utility providers should consider in the financial planning process is the revenue impact of substituting reuse water for potable water. As reuse water is introduced, customer's consumption of potable water is replaced and potable water revenue will subsequently decline. From a financial perspective, the transition of service will not likely result in a positive financial outcome. Because of the difference in quality and to encourage reuse water usage, reuse water is often priced at a level that is

allocation, and distribution of costs for potable water discussed in sections II and III would be applicable to reuse.

If water reuse costs are part of the water or wastewater utility enterprise fund, the reuse revenue requirement may be part of the total utility revenue requirement rather than a stand-alone utility. The embedded reuse costs can be specifically assigned in the cost allocation process. Additional cost components for reuse water may be required to specifically identify costs associated with reuse. Table V.1-2 illustrates allocation of operation and maintenance (O&M) costs and nonrate revenue for utilities with combined potable and reuse costs. In this example, cost components are separated into cost pools: common-to-all, common-to-potable, and common-to-reuse customers. A cost pool captures costs that are specific to a particular group of customers. The common-to-all cost components include costs that are incurred by all potable and reuse customers. Common-to-potable cost components include costs incurred only by potable customers, and common-to-reuse cost components include costs incurred only by reuse water customers. This allocation method also applies to the other revenue requirement line items such as capital costs, taxes, transfers, debt service, and change in reserves.

The common-to-reuse columns would apply to a wastewater utility cost allocation process. If the utility plans to have only one class of reuse customers, the base, maximum-day, and maximum-hour columns can be replaced with one column representing total demand costs. This cost allocation method explicitly shows which costs are attributable to potable water and reuse water. Similar to wholesale cost allocation, the units of service for the common-to-reuse would only include reuse customer demands.

Subsidies

The cost allocation method described above is based on full-cost pricing. Using this method may result in the unit cost of reuse water being higher than potable (see Line 26 in Table V.1-2). Reuse systems are typically newer compared with most potable systems whose costs benefit from significant depreciation on past treatment and distribution system investments. Conversely, reuse systems incur additional costs, such as higher per-unit pumping costs due to locations at lower elevations, influent water quality, and brine disposal requirements. Reuse water also requires a separate distribution system. Densely populated areas already benefit from a potable distribution system. Installing a new reuse distribution system alongside other utility services in built-up areas is costly.

As discussed in more detail in the other sections of this chapter, reuse water is an imperfect substitute for potable water. Customer preferences will dictate the price at which they are willing to use reuse water over potable water. The perception of lower quality and availability of reuse water generally shapes these customer preferences. As a result, reuse water must be priced at a level that will favor the use of reuse over potable in the absence of a utility charging the full cost of reuse water service. The difference between the full-cost rate of reuse and the actual rate is the subsidy to be recovered from other sources.

There are many considerations in determining which utility provides the deficit or subsidy in funding. This determination requires a closer look at the drivers behind the need for the reuse system. Is the reuse facility needed to meet certain discharge requirements regardless of whether there is an end user? If the utility is required to meet discharge regulations that require incremental treatment, such as secondary or tertiary treatment, allocating all or a portion of advanced treatment costs to wastewater is appropriate. Regulations require this treatment, and all wastewater customers contribute wastewater discharge.

Is the reuse facility needed to augment water supply or reduce current potable water usage per capita? If so, there is a logical argument that the deficit should be met by the water utility. Although that would increase the cost to all potable customers, they also

Table V.1-2 Operation and maintenance expense, allocation to cost components—Combined potable and reuse costs

Line No.	Item	Total	Common to Potable Customers				Common to Reuse Customers			Common to All Customers	
				Extra Capacity				Extra Capacity		Customer	
			Base	Maximum Day	Maximum Hour	Direct Fire Protection Costs	Base	Maximum Day	Maximum Hour	Meters & Services	Billing & Collection
1	**Source of Supply**	270,000	270,000								
	Pumping										
2	Purchase Power	832,000	699,300	77,700			50,000	5,000			
3	Other	639,000	376,350	202,650			10,000	50,000			
	Water Treatment										
4	Chemicals	463,000	363,000				100,000				
5	Other	471,000	306,150	164,850							
	Transmission and Distribution										
6	Storage	78,000	7,800		70,200						
7	Transmission Mains	156,000	101,400	54,600							
8	Distribution Mains	234,000	105,300	58,500	70,200						
9	Reuse Transmission Mains	125,000					75,000	50,000			
10	Reuse Distribution Mains	200,000					90,000	50,000	60,000		
11	Meters and Services	465,000								465,000	
12	Hydrants	39,000				39,000					
13	Other	216,000	41,040	21,600	41,040	8,640				103,680	
	Customer Accounting										
14	Meter Reading and Collections	741,000							0	741,000	
15	Uncollectable Accounts	132,000	62,040	18,480	7,920	1,320				18,480	23,760
	Administration and General										
16	Salaries	582,000	196,279	80,466	29,264	7,566	27,045	23,181	9,272	205,255	3,672
17	Employee Benefits	531,000	179,079	73,415	26,699	6,903	24,675	21,150	8,460	187,268	3,350
18	Insurance	405,000	136,586	55,995	20,364	5,265	18,820	16,131	6,452	142,832	2,555
19	Other	798,000	269,125	110,330	40,125	10,374	37,082	31,784	12,714	281,432	5,035
20	Total O&M Expense	7,377,000	3,113,449	918,586	305,812	79,069	432,621	247,246	96,899	2,144,947	38,372
21	Nonrate Revenue	(78,000)	(26,305)	(3,637)	(183)	(2)	(0)	(0)	(0)	(0)	(0)
22	*Reuse Subsidy*	*0*	*0*	*0*	*0*						
23	Net Revenue Requirements	7,299,000	3,087,143	914,949	305,629	79,067	432,621	247,246	96,899	2,144,947	38,372
24	Units of Service		1,000 gal	1,000 gpd	1,000 gpd		1,000 gal	1,000 gpd	1,000 gpd	Equiv. Meters	Bills
25	Total System		2,766,000	8,402	12,243		276,600	840	1,224	17,695	200,868
26	*Unit Cost*		*1.12*	*108.90*	*24.96*		*1.56*	*294.27*	*79.15*	*121.22*	*0.19*

benefit from reuse through lower alternative water supply costs. Subsidies for reuse system costs are further complicated if the water and wastewater systems are separate agencies. A wastewater utility setting reuse rates may be constrained by the maximum potable rate from their water utility provider, and may face challenges from the water provider because the introduction of reuse could affect its water revenues. Cost structures between agencies can vary significantly based on several factors, such as size, age of facilities, and

DOCKET NO. 49189

APPLICATION OF THE CITY OF AUSTIN DBA AUSTIN WATER FOR AUTHORITY TO CHANGE WATER AND WASTEWATER RATES	§ § § § §	BEFORE THE PUBLIC UTILITY COMMISSION OF TEXAS

DIRECT TESTIMONY
OF
TAB R. URBANTKE

WITNESS FOR THE CITY OF AUSTIN
D/B/A AUSTIN WATER

APRIL 2019

TABLE OF CONTENTS

ATTACHMENTS

WORKPAPERS

I. INTRODUCTION

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

A. My name is Tab R. Urbantke. I am an attorney and partner in the law firm of Hunton Andrews Kurth LLP (HAK). My business address is 1445 Ross Avenue, Suite 3700, Dallas, Texas 75202.

II. PURPOSE OF DIRECT TESTIMONY

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A. I am testifying on behalf of the City of Austin (City), doing business as Austin Water, a municipal water and sewer utility.

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

A. The purpose of my direct testimony is to discuss and express my opinion regarding the reasonableness, necessity, and recoverability of the rate case expenses incurred by the City in this proceeding for outside legal counsel. I will not offer an opinion as to the reasonableness of outside consultants' fees, other than my own. My understanding is that each consultant will provide individual testimony concerning the reasonableness of his or her respective fees. My testimony describes the standards for recovery of legal fees and expenses, including those that are recoverable rate case expenses, and the methodology that I have used in analyzing the reasonableness and recoverability of these expenses. I also apply those standards to the facts and circumstances of this rate case, and based on my full review and evaluation, I support the City's recovery of its reasonable legal fees and expenses that have been or will be incurred for this case.

Consistent with Public Utility Commission of Texas (Commission) practice, if the rate case expense issue does not settle, I expect to file supplemental direct testimony or an affidavit at the appropriate time to update this direct testimony and provide a review of rate case expenses actually incurred as the case moves along.

Q. ARE YOU SPONSORING ANY ATTACHMENTS OR COST-OF-SERVICE SCHEDULES IN CONNECTION WITH YOUR DIRECT TESTIMONY?

A. Yes. I sponsor the attachments listed in the table of contents of this testimony, and I co-sponsor legal invoices contained in Schedule II-E-4.4 of the rate filing package (RFP).

Q. WERE YOUR TESTIMONY, THE ATTACHMENTS THERETO, YOUR WORKPAPERS, AND THE SCHEDULES YOU CO-SPONSOR, PREPARED BY YOU OR UNDER YOUR DIRECT SUPERVISION AND CONTROL?

A. Yes. My direct testimony is also organized consistent with the topics set forth above and, along with my attachments, workpapers, and schedules, it was prepared by me or under my direction, supervision, or control and is, to the best of my knowledge and belief, true and correct.

III. QUALIFICATIONS

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND RELEVANT PROFESSIONAL ASSOCIATIONS.

A. I graduated from Baylor University in 1998 with a Bachelor of Arts degree in political science. I later received a Master of Public Policy and Administration and my Juris Doctor degrees from Baylor University and Baylor Law School in February of 2002. I was subsequently admitted to the State Bar of Texas in 2002 and since

then have been continuously licensed to practice law in the State of Texas (State Bar No. 24034717). I am a member of the Public Utility Law and the Administrative and Public Law Sections of the State Bar of Texas.

Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.

A. I have practiced public utility and energy regulatory law, almost exclusively, for seventeen years for three different law firms. From April 2002 through June 2008, I was an associate with Hunton & Williams LLP on the Regulated Industries & Governmental Relations team. From June 2008 through June 2012, I was an associate and then counsel (effective June 2012) in the Energy Regulatory practice group at Vinson & Elkins LLP. In June 2018, I joined HAK as a partner on the Energy and Infrastructure team. I provide additional detail regarding my educational and professional background in my Attachment TRU-1.

During my practice, I have represented utilities in numerous proceedings before the Commission, municipal regulatory authorities, the Railroad Commission of Texas, and the Federal Energy Regulatory Commission. Although I have not previously represented a water utility in a rate case, I have been involved with ratemaking and rate-related issues since I began my practice. I have represented the largest electric utility in Texas in connection with several system-wide cost-of-service rate cases before the Commission and municipal regulatory authorities, as well as a transmission-only utility in rate cases before the Commission. Additionally, I have handled rate case expense issues on behalf of utilities and, at one time or another, most of the major issues that are often contested in a typical rate case. I will not, however, offer any opinions or substantive analysis of these more general rate case issues unless relevant to the determination of the recoverability of rate case expenses.

Specifically, I have led and/or actively participated as legal counsel in numerous rate and prudency proceedings, including the following:

- *Application of Oncor Electric Delivery Company LLC for Approval to Amend its Distribution Cost Recovery Factor*, Docket No. 49427 (Apr. 8, 2019);
- *Application of Oncor Electric Delivery Company LLC for Authority to Decrease Rates Based on the Tax Cuts and Jobs Act of 2017*, Docket No. 48325, Order (Apr. 4, 2019);
- *Application of Oncor Electric Delivery Company LLC for Interim Update of Wholesale Transmission Rates*, Docket No. 49160 (pending), and several prior Interim Transmission Cost of Service cases, including Docket Nos. 48559, 47988, 46825, 46210, 44968, 44363, 42706, 42267, 41706, 41166, 40603, 40142, and 39644;
- *Application of Oncor Electric Delivery Company LLC for a Distribution Cost Recovery Factor*, Docket No. 48231, Order (Aug. 30, 2018);
- *Application of Oncor Electric Delivery Company LLC for Authority to Change Rates*, Docket No. 46957, Order (Oct. 13, 2017);
- *Application of Cross Texas Transmission, LLC for Authority to Change Rates and Tariffs*, Docket No. 43950, Order (May 1, 2015);
- *Application of Cross Texas Transmission, LLC to Establish Initial Rates and Tariffs*, Docket No. 40604, Order (Jan. 16, 2013);
- *Application of Oncor Electric Delivery Company LLC for Authority to Change Rates*, Docket No. 38929, Order (Aug. 26, 2011);
- *Application of Oncor Electric Delivery Company LLC for Authority to Change Rates*, Docket No. 35717, Order on Rehearing (Nov. 30, 2009);
- *Application of Oncor Electric Delivery Company LLC for 2010 Energy Efficiency Cost Recovery Factor*, Docket No. 36958, Order (Nov. 23, 2009); and

- *Atmos Energy Corp., Mid-Tex Division, Gas Cost Review in Compliance With 8664 and 9400*, GUD No. 9732, Final Order (Feb. 26, 2009).

Based on my experience in these and other cases, I know the rate case process and the effort and expertise that is required to pull together, file, and effectively prosecute a rate case. I have had the opportunity to coordinate the overall management of the case; develop case strategy; assemble the legal team; select witnesses (both internal and external) and consultants; review and approve schedules and testimony, discovery responses, and other case filings; negotiate settlements; and participate in the hearing and coordinate post-hearing briefing.

I have also worked with in-house counsel and regulatory personnel to coordinate the efforts of outside counsel and in-house resources for rate and other regulatory matters. Through my representation of clients in rate proceedings and other cases, I have gained knowledge and familiarity with the hourly rates charged by legal counsel and the necessary efforts that must be expended by legal counsel to effectively represent a client in rate proceedings. Finally, as a partner at HAK, I have reviewed invoices for legal work performed for the firm's clients.

Please refer to Attachment TRU-1 for additional detail regarding my professional experience.

IV. STANDARDS FOR RATE CASE EXPENSE RECOVERY

Q. IS THE CITY ENTITLED TO REIMBURSEMENT OF RATE CASE EXPENSES INCURRED IN CONNECTION WITH THIS RATE CASE?

A. Yes. The City filed this rate case under Texas Water Code (TWC) § 13.044 and under the Commission's Order on Rehearing in the City's last rate case in Docket No.

42857.[1] In the Order on Rehearing, the Commission recognized that it is a fundamental principle of ratemaking that regulated public utilities are entitled to rates that will allow them to collect total revenues equal to their cost of service.[2] The City, functioning as Austin Water, operates as a municipal water and sewer utility. Rate case expenses are part of a utility's operating expenses and, therefore, the inclusion and recovery of reasonable rate case expenses as part of the City's operating expense is appropriate here. A utility must be allowed to recover its reasonable and necessary rate case expenses in order to recover its full and reasonable cost of doing business. This is true for investor-owned utilities and for municipal utilities like Austin Water.

Furthermore, under 16 Tex. Admin. Code § 24.44(a) (TAC), a water utility may recover rate case expenses, including attorneys' fees, incurred as a result of filing a rate-change application under TWC §§ 13.187 or 13.1871, if the expenses are just, reasonable, necessary, and in the public interest. Additionally, TWC § 13.084 addresses the authority of the governing body of a municipality and provides as follows:

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[1] *Petition of North Austin Municipal Utility District No. 1, Northtown Municipal Utility District, Travis County Water Control and Improvement District No. 10, and Wells Branch Municipal Utility District from the Ratemaking Actions of the City of Austin and Request for Interim Rates in Williamson and Travis Counties*, Docket No. 42857, Order on Rehearing (Jan. 14, 2016).

[2] *Id.* at 28 (citing *Suburban Util. Corp. v. Pub. Util. Comm'n.*, 652 S.W.2d 358, 362 (Tex. 1983); Tex. Water Code Ann. § 13.044 (providing in an appeal of its rates, a municipality must show its rates are reasonable and the Commission may set its rates in a reasonable manner).

> The governing body of any municipality or the commissioners court of an affected county shall have the right to select and engage rate consultants, accountants, auditors, attorneys, engineers, or any combination of these experts to conduct investigations, present evidence, advise and represent the governing body, and assist with litigation on water and sewer utility rate-making proceedings. The water and sewer utility engaged in those proceedings shall be required to reimburse the governing body or the commissioners court for the reasonable costs of those services and shall be allowed to recover those expenses through its rates with interest during the period of recovery.

Here, the City is the governing body and also controls the affected municipal water utility. The principle stated in TWC § 13.084 should still apply—a municipality participating in litigation regarding municipal water rates must be allowed to recover its reasonable costs for its participation, including attorneys' fees, consulting fees, and other reasonable costs. And, the utility must be allowed to recover these costs through its rates.

Along with the above-described standards, several other provisions in the TWC, the Public Utility Regulatory Act, and related Commission rules support the general proposition that utilities and municipalities should be allowed to recover reasonable rate case expenses.[3] This tenet is sound, accepted ratemaking, and should be followed here.

[3] *See, e.g.*, Tex. Util. Code Ann. § 33.023 (authorizing municipalities conducting an electric ratemaking proceeding to engage outside personnel to assist in the proceeding); Tex. Util. Code Ann. § 36.061 (authorizing the recovery of rate case expenses in electric utility rate cases); 16 TAC § 25.245 (summarizing requirements for claiming recovery of rate case expenses in electric utility rate case); and TWC § 13.043(e) (authorizing recovery of reasonable rate case expenses expended by municipality in appeal proceedings concerning its rates).

Q. DOES THE COMMISSION TREAT THE RECOVERY OF RATE CASE EXPENSES THE SAME WAY AS THE RECOVERY OF OTHER OPERATING EXPENSES?

A. Not exactly. Although they are part of operating expenses, rate case expenses are treated differently, in part, based on timing issues. Most operating expenses at issue in a Texas rate case are incurred during a historical test year and are recurring, on an annual basis, but rate case expenses are not. They are not necessarily incurred during a test year, and they are not necessarily recurring on an annual basis. The Commission's practice has been to allow recovery of reasonable rate case expenses that the utility incurs both before and after the test-year ends, including the recovery of any remaining, reasonable rate case expenses incurred by the utility in connection with a previous rate case. Unlike its treatment of most other operating expenses, typically, the Commission will either amortize the recovery of rate case expenses over a fixed term of years that reflects the expected period those rates will be in effect, or permit the utility to surcharge the actual rate case expenses it incurred for recovery through a rider. The latter treatment has been more common in recent years.

Q. WHAT STANDARDS ARE USED TO DETERMINE THE REASONABLENESS OF RATE CASE EXPENSES INCURRED BY THE CITY?

A. As recognized by the Commission in the City's last rate case, Commission substantive rules and Texas statutes do not currently speak to the specific factors that the City must address to recover its rate case expenses as a municipality operating a

municipal water utility.[4] Well-established case law, however, does discuss the types of factors that the Commission can consider when determining the reasonableness of rate case costs and expenses. The seminal case in this area is *City of El Paso v. Public Utility Commission of Texas*.[5] In *City of El Paso*, the Third Court of Appeals held that a utility's requested rate case expenses are reimbursable if the Commission finds the expenses reasonable.[6] The Court discussed the types of factors the Commission can consider when determining the reasonableness of rate case costs and expenses.[7] Those factors, which are similar to the factors that may be considered in determining the reasonableness of legal fees under the Texas Disciplinary Rules of Professional Conduct (TDRPC),[8] include but are not limited to:

1. the time and labor required;
2. the nature and complexities of the case;
3. the amount of money or value of property or interest at stake;
4. the extent of responsibilities the attorney assumes;
5. the fee customarily charged in the locality for similar legal services;
6. whether the attorney loses other employment because of the undertaking; and

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[4] Docket No. 42857, Order on Rehearing at 27 ("The lack of TCEQ or Commission rules guiding the city in the proof it needed to establish a known industry standard—just and reasonable rates—does not constitute a violation of the city's due process."). The Commission recently opened a rulemaking to amend 160 TAC § 24.44. The Strawman filed on January 9, 2019, would amend the rule to provide a list of acceptable evidentiary information that a water utility may file in support of recovering its rate case expenses that largely resembles the factors used in 16 TAC § 25.245 concerning electric utility rate case expenses. *Rulemaking to Amend §24.44 Rate-Case Expenses Pursuant to Texas Water Code §13.187 and 13.1871*, Project No. 48937, Public Notice of Workshop on Strawman Amendments to 16 Texas Administrative Code (TAC) §24.44 and Request for Comments (Jan. 9, 2019) (pending).

[5] *City of El Paso v. Pub. Util. Comm'n of Texas,* 916 S.W.2d 515, 522 (Tex. App.—Austin 1995, writ dism'd by agr.).

[6] *Id.*

[7] *Id.*

[8] Tex. Disciplinary Rules Prof'l Conduct R. 1.04(b), reprinted in Tex. Gov't Code Ann., tit. 2, subtit. G app. A (Tex. State Bar R. art. X, § 9).

7. the benefits to the client from the services.[9]

More recently, in 2014, the Commission adopted 16 TAC § 25.245 that establishes (i) the specific requirements imposed on an electric utility claiming recovery of rate case expenses, and (ii) the criteria the Commission must apply to determine the reasonableness of such expenses. While not directly applicable here, this rule provides helpful guidance on the specific requirements that the Commission has looked to for the recoverability of rate case expenses. Thus, I have used 16 TAC § 25.245 to guide my evaluation of the City's requested rate case expenses in this case.

Q. PLEASE DESCRIBE THE REQUIREMENTS IMPOSED ON AN ELECTRIC UTILITY CLAIMING RECOVERY OF RATE CASE EXPENSES UNDER 16 TAC § 25.245.

A. An electric utility requesting recovery of rate case expenses must prove the reasonableness of its expenses by a preponderance of the evidence. Specifically, the utility must provide evidence showing:

1. the nature, extent, and difficulty of the work done by the attorney or other professional;
2. the time and labor required and expended by the attorney or other professional;
3. the fees or other consideration paid to the attorney or other professional for the services rendered;
4. the expenses incurred for lodging, meals and beverages, transportation, or other services or materials;
5. the nature and scope of the rate case, including:
   a. the size of the utility and number and type of customers served;

[9] *City of El Paso* at 522.

b. the amount of money or value of property or interest at stake;

c. the novelty or complexity of the issues addressed;

d. the amount and complexity of discovery;

e. the occurrence and length of a hearing; and

6. the specific issues in the rate case and the amount of rate case expenses reasonably associated with each issue.[10]

These factors, though not dispositive in this case, provide relevant guidance as to what evidence the City functioning as a municipal water utility may provide in order to establish its rate case expenses are just and reasonable.

Q. ON WHAT BASIS MAY THE COMMISSION EXCLUDE RATE CASE EXPENSES FROM RECOVERY?

A. Again, though not dispositive here, 16 TAC § 25.245 is helpful. Under section 25.245 and after considering the *City of El Paso* factors, the Commission may exclude rate case expenses to the extent it finds:

1. the fees paid to, tasks performed by, or time spent on a task by an attorney or other professional were extreme or excessive;
2. the expenses incurred for lodging, meals and beverages, transportation, or other services or materials were extreme or excessive;
3. there was duplication of services or testimony;
4. the utility's or municipality's proposal on an issue in the rate case had no reasonable basis in law, policy, or fact and was not warranted by any reasonable argument for the extension, modification, or reversal of Commission precedent;
5. rate case expenses, as a whole, were disproportionate, excessive, or unwarranted in relation to the nature and scope of the rate case addressed by the evidence pursuant to subsection (b)(5) of § 25.245; or

[10] 16 TAC § 25.245(b).

6. the utility or municipality failed to comply with the requirements for providing sufficient information pursuant to subsection (b) of § 24.245.[11]

Otherwise, the Commission is required to allow recovery of rate case expenses equal to the amount shown in the evidentiary record to be actually and reasonably incurred by the utility.

V. REVIEW METHODOLOGY

Q. PLEASE GENERALLY DESCRIBE THE METHODOLOGY YOU USED TO EVALUATE THE REASONABLENESS OF THE CITY'S CURRENT RATE CASE EXPENSES.

A. After an initial telephone conference with the City's outside counsel, Mr. Thomas L. Brocato, I reviewed the Commission's Order on Rehearing in the City's last rate case (Docket No. 42857) to provide context for this filing. Additionally, I have reviewed the rate case expenses incurred by the City for outside legal counsel from April 1, 2018 to March 31, 2019 (see Schedule II-E-4.4) in connection with the preparation of the City's RFP. I interviewed the primary outside attorneys and the in-house counsel responsible for this case about the measures and systems established to ensure the appropriateness of legal fees. I also reviewed the qualifications and hourly rates of the attorneys and paralegals involved in the rate case. Furthermore, I considered the *City of El Paso* standards and other relevant legal authority, including the TDRPC and Commission rules that bear on the recovery of rate case expenses, to determine the reasonableness of the fees, expenses, and hourly rates charged by the attorneys and their support staff in this case.

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[11] 16 TAC § 25.245(c).

Q. PLEASE DESCRIBE THE PURPOSE OF EACH PART OF YOUR REVIEW.

A. By interviewing the primary outside attorneys and the in-house counsel responsible for this case, I was able to investigate the general practices that the City used for selecting the rate case team. The interviews also provided me with information about the lawyers chosen for the rate case team, including their relevant educational and professional backgrounds. I also learned what systems are put in place by outside counsel to ensure that work is being conducted efficiently and not being duplicated. I investigated what steps have been taken to make sure the time spent by attorneys on the rate case is appropriate for the nature and complexity of the case. Finally, I reviewed the qualifications and hourly rates of the attorneys involved in the rate case to confirm consistency between the fees charged, the experience of the attorney or paralegal, and the nature of the work to be performed. Further discussion of my conclusions based on my review methodology is listed below.

Q. FOR WHAT PERIOD OF TIME WAS YOUR REVIEW CONDUCTED?

A. Thus far, my review has been limited to rate case expenses billed to and incurred by the City from April 1, 2018, through March 31, 2019. If the rate case expense issue does not settle, I will need to conduct additional review to determine the continuing reasonableness of rate case expenses throughout the rate proceeding, and I will need to file supplemental direct testimony or an affidavit regarding those expenses.

Q. IF THE RATE CASE EXPENSE ISSUE IS NOT SETTLED, WHAT REVIEW WILL YOU CONDUCT POST FILING TO DETERMINE THE CONTINUING REASONABLENESS OF THE CITY'S RATE CASE EXPENSES?

A. I will review invoices for legal fees incurred after March 31, 2019, and verify that the rate case team remained focused on their assigned tasks. I will also evaluate whether the time spent, as indicated on the invoices, is appropriate given the complexity and importance of the various issues in the rate proceeding. Additionally, I will evaluate the factors for determining the reasonableness of rate case expenses that cannot be addressed, all or in part, at the application stage of the proceeding (*e.g.*, amount and complexity of discovery, occurrence and length of the hearing, and specific issues that have arisen). After the completion of this review and research, I will file supplemental direct testimony or an affidavit detailing my findings regarding the reasonableness of the rate case expenses incurred by the City.

VI. RESULTS OF REVIEW

Q. PLEASE DESCRIBE THE BASIS FOR THIS RATE CASE.

A. Based on my interviews and research, the City's wholesale rates for water and wastewater services were historically imposed on its wholesale customers by ordinance as adopted by the Austin City Council. In 2013, four members of the City's wholesale customer class (the "Appellants") challenged the City's cost allocation and rate design methodology through an appeal to the Texas Commission on Environmental Quality (TCEQ).[12] The appeal was eventually transferred to the Commission. The Commission ultimately rejected the City's proposed increased rates and ordered the City, under TWC § 13.044, to refrain from increasing wholesale water and wastewater rates applicable to the Appellants without Commission

[12] *Appeal filed by North Austin MUD No. 1, Northtown MUD, Travis County WCID No. 10 and Wells Branch MUD ("Petitioners"), from the Ratemaking Actions of the City of Austin, and Request for Interim Rates in Williamson and Travis Counties*, TCEQ Docket No. 2013-0865-UCR, Application No. 37584-M (April 16, 2013).

approval.[13] Subsequently, the City attempted to enter into a settlement agreement with the Appellants, but the parties could not reach an agreement. In this docket, therefore, the City seeks Commission approval to increase its wholesale water and wastewater rates in compliance with the Commission's Order on Rehearing in Docket No. 42857 and TWC § 13.044.

Q. PLEASE SUMMARIZE THE RATE CASE PROCESS.

A. A rate case is highly specialized administrative litigation that requires a robust management process and reasonable decision makers to implement that process. The utility has the burden of proof, thus requiring it to prepare for and address multiple issues in its direct and, where necessary, rebuttal testimony. There are numerous possible issues in a rate case that are sometimes hard to anticipate until well into the litigation. Discovery is often complex, many times voluminous, and often with short-turnaround deadlines. Typically, the utility will anticipate the need for multiple direct and rebuttal witnesses with varied, highly specialized expertise. These witnesses need to cover a broad range of substantive topics—accounting, finance, and all aspects of utility operations and management. And still, throughout this entire process, experienced practitioners know that good public policy requires the utility to efficiently manage rate case litigation. Wasteful or unnecessary expenditures in litigating a rate case will not only place the utility's recovery of rate case expenses at risk, but it can negatively affect the utility's reputation and the credibility of its case.

[13] Docket No. 42857, Order on Rehearing at 29.

Q. WHO DID THE CITY SELECT AS ITS OUTSIDE LEGAL COUNSEL?

A. The City selected the Austin law firm of Lloyd Gosselink Rochelle & Townsend, P.C. (Lloyd Gosselink) as its outside legal counsel, and with the assistance of Lloyd Gosselink, selected several additional consulting resources to assist the City in handing this rate case.

Q. PLEASE DESCRIBE THE CITY'S RATE CASE TEAM.

A. Mr. Andy Perny, Utility and Regulatory Division Chief for the City since 2005, is the in-house counsel with overall legal responsibility for the City's rate case. As I discuss further below, Mr. Perny hired Lloyd Gosselink as the outside counsel responsible for the preparation and prosecution of this case.

Lloyd Gosselink and the City have assembled a team of lawyers and support staff to provide the necessary services to prosecute this case. In my review of the invoices provided to me, I made note of the lawyers and other support resources that have been assigned to the case. The team of lawyers primarily responsible for the rate case includes Mr. Thomas L. Brocato, who is serving as the lead lawyer for the case, Mr. Christopher L. Brewster, and Ms. Jamie L. Mauldin, and junior associates and paralegals who support the legal team. After interviewing and reviewing the credentials of Messrs. Brocato and Brewster and Ms. Mauldin and consulting with Mr. Perny at the City, I am satisfied that the members of the outside legal team are qualified for their respective roles in this case.

Q. HOW DOES THE CITY DETERMINE WHICH RATE CASE EXPENSES SHOULD BE RECOVERED?

A. Mr. Perny and I discussed the method the City uses when determining which rate case expenses should be included in the calculation of rates. According to Mr. Perny, the