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Received - 2022-06-09 06:04:08 PM

Control Number - 50788

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**PUC DOCKET NO. 50788
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RATEPAYERS APPEAL OF THE BEFORE THE STATE OFFICE DECISION BY WINDERMERE OAKS WATER SUPPLY CORPORATION TO CHANGE WATER AND SEWER RATES	§ § § § §	PUBLIC UTILITY COMMISSION OF TEXAS
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RATEPAYERS’ RESPONSE TO FILING OF TRWA LETTER

THE REPRESENTATIVES OF THE RATEPAYERS OF WINDERMERE OAKS WATER SUPPLY CORPORATION (“Ratepayers”) file this their Response and Motion to Strike as to the letter filed by Texas Rural Water Authority (“TRWA”) on June 7, 2022, and would show as follows.

A. Introduction

The TRWA’s letter portrays this proceeding as involving issues of great importance to the utility industry participants TRWA represents. TRWA purports to have information worthy of the Commission’s consideration in this matter. It is unfortunate that TRWA has had this epiphany at such a late date. Had TRWA spoken up in early 2020, Windermere’s ratepayers would not be in the predicament in which they find themselves today.

TRWA was the board’s rate consultant for purposes of the 2020 rate increase. Indeed, for years the board claimed that TRWA “circuit rider” James Smith was the one who actually determined the appealed rates.¹ That was not true and TRWA knew it was not true. To the contrary, based on a revenue requirement that included only \$166,000 in legal expenses, TRWA

¹ See, e.g., Direct Testimony of Mike Nelson, WOWSC Exhibit 07 at 006, 16-20 & Attachment MN-2; Cross-examination of George Burris, Tr. Day 1 at 43, 6-11.

calculated that Windermere needed to increase its combined base charge for water and sewer service to \$174 per month.² TRWA knew at the time, however, that Windermere's actual cash need for legal costs going forward was at least \$370,000, comprised of an additional \$120,000 in unpaid legal expenses for 2019 and a "guesstimated" \$250,000 in legal expenses for 2020.³ TRWA even opined that Windermere would become insolvent if it waited until the end of 2020 to levy an assessment for the board's legal costs.⁴ When the board then approved a rate increase that was even lower than TRWA's understated \$174 figure, no one was in a better position than TRWA to appreciate that the board's rates were not legitimate. Nevertheless, TRWA stood by in silence and allowed the board to portray that the rate increase was designed using an accepted "cash needs" methodology and appropriate cost data.

TRWA chooses not to address its integral involvement in the implementation of an ad hoc rate increase. Instead, TRWA prefers to weigh in on straw issues that are not raised by the evidence, and its "commentary" misrepresents the record and misapplies the law. It is nothing more than a thinly veiled invitation on behalf of the special interests TRWA represents – including Windermere's board – for the Commission to disregard its legislative charge to regulate retail public utilities to assure rates, operations, and services that are just and reasonable to the consumers. TRWA knows that otherwise the appealed rates will not survive.

B. Discussion.

- 1. The Commission's duty to ensure that rates are just and reasonable requires it to evaluate all expenses the board elects to include in rates; legal expenses are no exception.*

² Mike Nelson Direct Testimony (WOWSC Exhibit 07), Attachment MN-2.

³ Cross-examination of George Burris, Tr. Day 1, at 77, 10 – 78, 10; Attachment MN-5 at 037 (Line item 63000, Legal/Appraisal).

⁴ Cross-examination of George Burris, Tr. Day 1, at 76, 6 – 77, 4.

The Legislature has charged the Commission with responsibility to regulate retail public utilities to assure rates, operations and services that are just and reasonable to consumers, as well as to the utilities.⁵ The Legislature has required that the Commission exercise jurisdiction over water supply corporation (“WSC”) decisions affecting water or sewer rates in appeals under Texas Water Code Section 13.043. The Legislature has also required that the Commission exercise its full original regulatory jurisdiction over WSCs in the circumstances set forth in Section 13.004(a). In both cases, the Commission must ensure that rates paid by the WSC’s customers are just and reasonable, are not unreasonably preferential, prejudicial, or discriminatory and are sufficient, equitable, and consistent in application to each class of customers.⁶

In general, just and reasonable rates may not include expenses that are not necessarily and prudently incurred in connection with the provision of utility services. Accordingly, the Commission’s core function routinely involves “restructuring the budget line items for already incurred” expenses, “[m]aking post-hoc judgment calls” as to whether expenses were justified and “substituting its judgment” for that of whoever made the initial decision to incur the expenses in question. Legal expenses are certainly no exception.⁷

Unnecessary or imprudent expenses are no more allowable in Windermere’s rates than they are in the rates of any other form of utility. That the disallowed expenses were incurred by vote of an elected board makes no difference and TRWA cites no authority suggesting it does. By choosing to include the board’s legal expenses in the appealed rates, Windermere made them

⁵ See § 13.001(c), Tex. Water Code.

⁶ §13.043(j); §13.182(a) & (b).

⁷ The standards for “allowability” are the same for outside legal costs as for any other type of expense the utility desires to recover from its customers. See *State ex rel. Utilities Com’n v. Public Staff, North Carolina Utilities Com’n*, 317 N.C. 26, 38 – 40, 43 S.E.2d 898, 906-8 (1986), and the many decisions by courts and state utility commissions discussed therein. Ratepayers were not allowed here to provide the Commission with the level of detail that would typically be expected for this analysis, nevertheless the evidence that is in this record establishes that these legal costs were neither necessarily nor prudently incurred and are not in the public interest.

subject to Commission scrutiny. The Commission's job here is to apply recognized standards to determine whether the legal expenses are allowable in rates. To do otherwise would nullify the legislative charge in Section 13.001 to protect the public interest inherent in the rates and services of retail public utilities and to assure rates, operations, and services that are just and reasonable.

The Legislature could not have more clearly expressed its intention that annual director elections are not an adequate substitute for the Commission's performance of its critical regulatory functions. All Chapter 67 WSCs are required to have elected boards. Nevertheless, the Legislature has explicitly required the Commission to exercise rate regulation over Chapter 67 WSCs in a *de novo* rate setting in an appeal under Section 13.043(e). Moreover, the Legislature has explicitly required the Commission to exercise its full original jurisdiction over a Chapter 67 WSC when the WSC is not being operated as such.

The Legislature was quite correct: annual director elections, particularly when conducted by the very fiduciaries whose conduct has been called into question, afford no redress at all for the customers of a WSC. Windermere itself is an excellent example of this. In connection with every annual meeting and election since the rate increase, Windermere's membership has been inundated by misinformation disseminated by the board. By way of illustration, at the most recent annual meeting (and director election) Board President Gimenez falsely assured the membership that Windermere's insurance carrier is now paying the directors' legal expenses and that the base charges will soon be lowered.⁸ Ironically, it appears Windermere is no longer able to procure public officials and management liability coverage at all.⁹

⁸ This is reflected in the "Other" Ratepayers' iPetition, another untimely filing by people who declined to participate in the proceeding. In fact, the Allied lawsuit brought by the directors is on appeal to the Fifth Circuit and the insurer is not paying any of the legal fees Windermere is already obligated to pay and continues to incur for the benefit of the directors. There is no final judgment in the Allied lawsuit and the Double F lawsuit has not yet been tried. The board intends to continue charging the appealed rates until all of the litigation is finally completed and all of their legal fees have been paid in full. Gimenez cross-examination, Tr. Day 2 at 318, 7-19.

⁹ See attached email exchange between Board President Joe Gimenez and Windermere's insurance broker.

Also, Windermere's director elections have been beset by any number of irregularities.

These include:

- Refusing to count votes cast by members identified on the official voting list;
- Including deceased members as eligible voters on the official voting list;
- Counting votes allegedly cast by deceased members;
- Compiling a list of "provisional voters" as part of the official voting list;
- Allowing the independent election auditor to exercise discretion whether to count the "provisional votes";
- Refusing to allow members to vote during the annual meeting; and
- Counting votes cast by various categories of nonmembers.

At least one lawsuit is currently pending against Windermere in Burnet County District Court to challenge the results of the most recent director election.¹⁰

The irony here is that beginning in 2015, Windermere's fiduciaries have repeatedly fallen short of what the law requires of them. These transgressions have been far worse than "local political issues;" they have cost Windermere and its member/customers well over \$1 million thus far. Neither Windermere's bylaws nor its liability insurance purport to insulate its fiduciaries from liability for intentional misconduct, violations of the law, or receipt of improper benefit.¹¹ Windermere's bylaws do not require the corporation to pay the directors' legal fees at all.¹²

When Windermere's member/customers pursued recourse for their loss, Windermere's board emptied the corporation's coffers. These extravagant legal expenses have not been paid or incurred to defend Windermere or to pursue its members' interests. Indeed, the corporation has

¹⁰ Cause No. 53554, styled *Jeff Walker v. Windermere Oaks Water Supply Corporation*.

¹¹ *Id.* at 393, ll. 5-24; Ratepayers' Exhibit 27; Cross-examination of George Burris, Tr. at 57, ll. 8-21; Cross-examination of Mike Nelson, Tr. at 212, 25 – 213, 19.

¹² Ratepayers' Exhibit 27.

taken a neutral stance in the litigation.¹³ Every dollar of Windermere's resources (including rate revenue and corporate credit) spent in connection with three of the lawsuits¹⁴ has been devoted to preventing former director Dana Martin from having to return Windermere's misappropriated land and to preventing the imposition of personal liability (for the benefit of the corporation) on any of the directors involved in the misconduct.¹⁵ The directors have also used revenues from the appealed rates, as well as Windermere's credit, to file suit individually against Allied for recovery of insurance benefits for themselves.

Directors who approved the legal spending also authorized and implemented the rate increase to pay accrued balances and to fund future legal services. These same directors are also personally benefitting from both board actions. None of this is in the public interest. None of this results in just and reasonable rates.

2. *Expenses that are not allowable in rates must be funded, if at all, through other sources of revenue.*

TRWA misapprehends both Staff's position and the evidentiary record in this proceeding. As an initial matter, it is important to realize that the legal expenses at issue here were not "budgeted items." They *could not have been* "budgeted items." The board put no limits on the legal spending and had absolutely no way to anticipate how much the legal expenses might be from one month to the next or how long they might continue.¹⁶ According to Windermere's hearing representatives, that was precisely why the board made the unauthorized arrangement

¹³ Cross-examination of Joe Gimenez, Tr. Day 2 at 298, 2-11.

¹⁴ These include the Double F lawsuit by members to recover Windermere's lost property or its value and two lawsuits Windermere's board filed against the Texas Attorney General in an effort to avoid disclosure of information under the Texas Public Information Act that they perceived might reveal their defensive strategies in the other litigation. Rebuttal Testimony of Joe Gimenez, WOWSC Exhibit 03, at 9, 1. 15 – 10, 1. 3. After expending substantial corporate resources and claiming to have "won" these cases, the board unilaterally published the information on Windermere's website. Cross-examination of Joe Gimenez, Tr. Day 2 at 215, 15-21.

¹⁵ *Id.* at 297, 17-23.

¹⁶ Cross-examination of Mike Nelson, Tr. Day 1, at 192, 16-24 and 193, 14-23.

with legal counsel for Windermere to make a minimum payment each month going forward and accrue corporate debt for the unpaid balance of each invoice, without regard to how much the legal expenses might be.¹⁷ The board did not include even the minimum payments as “budgeted items,”¹⁸ probably because the arrangement with the lawyers was never properly authorized. The board has claimed from time to time since the rate increase that Windermere has operated “under budget,” but this is because the ever-increasing law firm debt has never been reported on any of Windermere’s financials.¹⁹

Staff did not recommend that Windermere pay these legal expenses with loan proceeds or other assets. Staff recommended that the legal expenses are not allowable in Windermere’s rates.²⁰ Accordingly, if the legal expenses are to be paid at all then they must be paid from other sources. Staff witness Maxine Gilford testified these sources might include insurance, loans or a sale of surplus property.²¹ The evidence showed that Windermere had (and still has) almost 7 acres of unencumbered surplus real estate.²²

Staff accepted Windermere’s representation that its lender will not allow proceeds from its loan to be used to pay the legal expenses.²³ Staff witness Gilford testified that this did not surprise her.²⁴ Apparently, Windermere’s lender agrees that the board’s legal expenses are not necessary or prudent corporate expenditures.

3. It would be improper to disregard the impact of the rate increase on other categories of Windermere ratepayers.

¹⁷ *Id.* and 198, 6 – 199, 25.

¹⁸ See Direct Testimony of Mike Nelson, WOWSC Exhibit 07, at 007, 14-20, in which Mr. Nelson testified that the Board’s 2020 budget was based on a “guesstimate” of legal costs for 2020. It was not. The board knew in early 2020 that they could not “guesstimate” the 2020 legal expenses and Mr. Nelson admitted it did not try to do so.

¹⁹ Cross-examination of Joe Gimenez, Tr. Day 2 at 333, 2-5.

²⁰ Cross-examination of Maxine Gilford, Tr. Day 3 at 528, 13-19.

²¹ *Id.* at 529, 21 – 530, 8.

²² Cross-examination of Joe Gimenez, Tr. Day 2 at 346, 22 – 347, 1.

²³ Cross-examination of Maxine Gilford, Tr. Day 3 at 524, 7-15.

²⁴ *Id.*

The evidence in this record conclusively establishes that Windermere collects revenue from at least three categories of member/customers: (i) ratepayers who presently receive and pay rates for monthly water and sewer service; (ii) ratepayers who purchase new connections and pay an equity buy-in fee to cover their share of system capital investments; and (iii) ratepayers who reserve system capacity to ensure they will receive water and wastewater service in the future and pay a standby fee. TRWA agrees that Windermere has these different categories of ratepayers.²⁵

TRWA's observation that equity buy-in fees and standby fees are not the same thing as monthly charges for water and wastewater service is simply a statement of the obvious.²⁶ It is not altogether clear why TRWA believes the Commission might overlook the distinction.

TRWA's suggestion that the Commission's authority under Section 13.043 extends only to fixing rates for water and sewer service under subsection (e) is in error.²⁷ For present purposes, however, it makes no difference. Without regard to whether it can fix a new equity buy-in fee or a new standby fee, the Commission must nonetheless evaluate whether the allocation of 100% of the burden of the legal expenses to a single category of ratepayer results in an unreasonable preference or advantage as to rates or services or subjects anyone within any of these classifications to any unreasonable prejudice or disadvantage. That is particularly true here, as the evidence establishes that the legal expenses are not costs to provide water and wastewater service, are not

²⁵ TRWA fails to mention that each type of ratepayer meets the criteria for "membership" (and for customer status) under Section 13.002(11) as one "who either currently receives or will be eligible to receive water or sewer utility service from the corporation."

²⁶ TRWA suggests that the charge for a share of system capital improvements and the charge to reserve system capacity "has nothing to do with" the charge for water and wastewater service. That clearly is not the case. Windermere reports all of its income as patronage revenue, and it is surprising that TRWA would take a contrary position. However, the evident relationship between these charges and the provision of water and sewer services need not be belabored for present purposes.

²⁷ At the very least, the Commission has jurisdiction to review costs to obtain service under Section 13.043(g) and has exercised it on numerous occasions.

costs for capital improvements and are not costs for reserved system capacity.²⁸ To the extent they are recoverable at all, there is no accepted basis upon which to allocate these expenses exclusively to any single ratepayer category. The board's decision to do so resulted in rates that are unreasonably preferential, prejudicial, or discriminatory.

C. Conclusion.

The TRWA filing should be stricken from the record. TRWA failed to speak up when they could have made a difference in this matter and should not be heard from now. TRWA fails to address the pivotal issue of rate design, with which it was integrally involved, choosing instead to focus on straw issues that it knows have nothing to do with the decisions before the Commission.

WHEREFORE, Ratepayer Representatives respectfully request that TRWA's letter be stricken from the record and given no consideration in this proceeding, and that they receive such other and further relief, at law or in equity, to which they may show themselves justly entitled.

Respectfully Submitted,

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Certificate of Service

²⁸ Cross-examination of George Burris, Tr. Day 1, at 71, 18 - 72, 6-9; Cross-examination of Mike Nelson, Tr. Day 1, at 206, 6-11; 207, 23-5; and 208, 5-11.

I hereby certify that, unless otherwise ordered by the Presiding Officer, notice of this filing was provided to all parties of record via electronic mail on June 9, 2022.

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Registered: Windermere Oaks Water Supply Corporation - Renewals Effective 3/17/2022

1 message

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Mon, Mar 7, 2022 at 3:54 PM

Reply-To: Sandy Batchelor

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To: 1129jjg@gmail.com

Cc: watermgmt@yahoo.com

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Good afternoon....

Unfortunately after submitting applications for coverage renewals effective March 17th for Windermere Oaks Water Supply we have been unable to secure any quotes for expiring coverages.

I have three declinations after submissions – two from standard carriers and another from a surplus lines market.

I did forward you applications for the Officers and Directors Management coverage on January 24,2022 but to date have not received either of these applications back with required financials from Windermere Oaks. .

If you have the applications completed for the Management Liability coverage complete with financials and still interested in our trying to secure a quote for coverage please get them back to me in the next day or two. The markets available take at least five to ten business days to get us anything back on applications submitted to them – whether it be a declination or possible quote for coverage. If you are still interested we need to have the completed applications along with financials and list of current officers/directors returned in the next day or two.

I do sincerely wish we could have secured a quote for you but all of the declinations were based on the loss history of the water supply.

We want to THANK YOU for your many years of LOYALTY and business in the past for which are grateful. We will await a response from you with regards to the coverage for the board.

If you need "valued/updated" loss runs let me know and I will secure for you.



Sandy Batchelor

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