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**SOAH DOCKET NO. 473-20-4071.WS  
PUC DOCKET NO. 50788**

<b>RATEPAYERS APPEAL OF THE</b>	<b>§</b>	<b>BEFORE THE STATE OFFICE</b>
<b>DECISION BY WINDERMERE OAKS</b>	<b>§</b>	
<b>WATER SUPPLY CORPORATION TO</b>	<b>§</b>	<b>OF</b>
<b>CHANGE WATER AND SEWER</b>	<b>§</b>	
<b>RATES</b>	<b>§</b>	<b>ADMINISTRATIVE HEARINGS</b>

**REPLY BRIEF  
OF WINDERMERE OAKS  
WATER SUPPLY CORPORATION**

**May 2, 2023**

**REPLY BRIEF  
OF WINDERMERE OAKS WATER  
SUPPLY CORPORATION**

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**WINDERMERE OAKS WATER SUPPLY CORPORATION'S  
REPLY BRIEF**

TO THE HONORABLE CHRISTIAAN SIANO AND DANIEL WISEMAN,  
ADMINISTRATIVE LAW JUDGES (ALJs), STATE OFFICE OF ADMINISTRATIVE  
HEARINGS (SOAH):

COMES NOW, Windermere Oaks Water Supply Corporation (WOWSC or the Corporation), and files this Reply Brief in the above-styled and numbered docket. Pursuant to SOAH Order Nos. 31 and 34, this brief is timely filed.<sup>1</sup> In support thereof, WOWSC shows the following:

**I. INTRODUCTION**

Ratepayers' and Staff's Initial Briefs assert various allegations related to WOWSC's revenue requirement, financial management, and fiduciary duties to mischaracterize the Corporation's affairs and its involvement in this rate appeal. However, this rate appeal still boils down to a single issue: WOWSC's 2019 outside legal expenses and, specifically, whether WOWSC can recover these expenses through rates. As discussed in WOWSC's Initial Brief, WOWSC incurred the 2019 legal expenses defending itself in several lawsuits filed by the appellant ratepayers (Ratepayers) and responding to an excessive number of Ratepayers' Public Information Act (PIA) requests.<sup>2</sup> WOWSC accurately budgeted 2020 legal expenses based on the 2019 legal expenses and the likelihood of continued litigation.<sup>3</sup> It now defends itself in this rate appeal that, again, Ratepayers initiated. As such, the Corporation continues to incur outside legal

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<sup>1</sup> SOAH Order No. 31 – Post-Hearing Briefing Schedule; Guidelines (Apr. 4, 2023); SOAH Order No. 34 – Extending Deadline (Apr. 27, 2023).

<sup>2</sup> WOWSC Ex. 3, Rebuttal Testimony of Joe Gimenez, III at Bates 9:6-10:7; WOWSC Ex. 26, Supplemental Rebuttal Testimony of Joe Gimenez, III at Bates 7:10-8:2; Bates 3-19; Bates 10:12-15.

<sup>3</sup> See also Windermere Oaks Water Supply Corporation's (WOWSC) Initial Brief at 6 (Dec. 30, 2021) (WOWSC's Initial Brief).

costs solely on account of the same group of members that now, without basis, asserts WOWSC's legal expenses were unreasonable and unnecessary.

As a preliminary matter, State Office of Administrative Hearings (SOAH) Order No. 31 provided that “all factual assertions in briefs shall be supported by evidence admitted at the hearing....”<sup>4</sup> Ratepayers wholly failed to meet this low bar. Its Initial Brief is littered with broad, sweeping statements that are unsupported by any evidence in the record. In fact, Ratepayers often fail to provide citations altogether.<sup>5</sup> When it does provide citations, the footnotes are often incomplete or clearly cite to the wrong page and, moreover, contain no support for the matter asserted in the brief.<sup>6</sup> Because Ratepayers' factual and legal misstatements are too widespread to fully address in the body of this brief, WOWSC prepared a spreadsheet detailing each unsupported statement of fact, misstatement of fact and law, and mischaracterization of evidence in the record.<sup>7</sup> Moreover, more than two weeks after the hearing on the merits, Ratepayers had still failed to provide SOAH with a copy of Ratepayers' properly numbered exhibits.<sup>8</sup> And to further prejudice the parties in this proceeding, Ratepayers—also two weeks after the hearing on the merits—replaced mislabeled exhibits and uploaded additional exhibits to the share file service the parties used to share exhibits before the hearing. In sum, the majority of Ratepayers' Initial Brief is unsupported by any evidence in the record and continues to unfairly malign WOWSC without evidence. Ratepayers' exhibits are mislabeled, unorganized, and constantly changing. Its Initial Brief and supporting evidence are therefore unreliable and should be dismissed.

Nevertheless, Staff apparently relies on Ratepayers' characterization of the underlying legal lawsuits at issue. Although its Initial Brief is mostly silent regarding the lawsuits, it provides that WOWSC's “legal expenses are not costs of service” and, even more concerning, questions

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<sup>4</sup> SOAH Order No. 31 Post-Hearing Briefing Scheduled; Guidelines at 2 (Apr. 6, 2023).

<sup>5</sup> See, e.g., Ratepayers Representatives' Initial Brief at 4 (Apr. 11, 2023) (Ratepayers' Initial Brief) (stating that “Windermere has suggested the Commission must create an exception for the rates of a retail public utility organized as a nonprofit corporation with members” but providing no citation to the record); *id.* at 8 (providing that “[n]either Windermere's legal expenditures nor the rate increase implemented to fund them was approved by Windermere's board as the contract requires” but providing no citation to the record); *id.* at 17 (alleging that “these proceedings sought to recover land and damages from individual fiduciaries and to hand them over the company, free of charge” but providing no citation to the record).

<sup>6</sup> See, e.g., Ratepayers' Initial Brief at 16, FN56 (citing to “bates 2425” when cited exhibit begins at Bates 2433); *Id.* at 16, FN62 (failing to provide a citation to a specific page number).

<sup>7</sup> Excel Spreadsheet (provided as Exhibit 1).

<sup>8</sup> SOAH Order No. 32 Requiring Submission Exhibits (Apr. 6, 2023).

whether the Corporation should have “contract[ed] for legal services related to external litigation...*at all*.”<sup>9</sup> This is dangerous rhetoric that chills responsible corporate judgment and directly conflicts with sound public policy. It further states that “[t]he Board’s decision to spend such an extreme amount stems from the Board’s failure to understand its fiduciary duties.”<sup>10</sup> Staff blatantly disregards Texas law. As discussed below, the Texas Business Organizations Code *required* that WOWSC incur the outside legal fees at issue.<sup>11</sup> Thus, in contrast to Staff’s apparent assumption, WOWSC’s decision to retain outside counsel was not discretionary: it was required by statute. Staff, however, attempts to punish WOWSC for protecting its volunteer directors, impose post-hoc judgment on WOWSC’s legal decisions, and opine on local issues best left to an elected Board of Directors. Its position is reckless and misguided and, therefore, must be dismissed.

The record is clear: WOWSC’s legal expenses paid in 2019 and budgeted in 2020 were just and reasonable. As discussed below, recent developments in the underlying lawsuits further validate the legal expenses.<sup>12</sup> Most importantly, Staff’s proposed revenue requirement arbitrarily excludes WOWSC’s legal expenses and would financially destroy the Corporation within a single year.<sup>13</sup> Staff’s and Ratepayers’ assertions regarding WOWSC’s financial records and management that suggest otherwise are unfounded and false.

The Commission shall conduct a de novo review of an appeal brought under the Texas Water Code (TWC).<sup>14</sup> Further, the Commission may consider only the information available to the governing body at the time it established rates and evidence of reasonable expenses incurred in the appeal proceedings.<sup>15</sup> More specifically, the Remand Order instructed the ALJs to determine whether the appealed rates meet “all of the standards prescribed under TWC § 13.043(j).”<sup>16</sup> As such, the ALJs must determine whether the appealed rates are “just and reasonable” and “not []

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<sup>9</sup> Commission Staff’s Initial Brief on Issues Addressed in the Second Hearing on the Merits at 2, 5 (emphasis added) (Apr. 11, 2023) (Staff’s Initial Brief).

<sup>10</sup> *Id.* at 12.

<sup>11</sup> Tex. Bus. Orgs. Code Ann. (TBOC) § 8.051.

<sup>12</sup> WOWSC Ex. 26 at Bates 8:3-13:19.

<sup>13</sup> WOWSC Ex. 27, Supplemental Rebuttal Testimony of Mike Nelson at Bates 8:5-9:8.

<sup>14</sup> Tex. Water Code Ann. §§ 13.043(a) and (c) (TWC); *see also* 16 Tex. Admin. Code § 24.101(c) (TAC).

<sup>15</sup> *Id.*

<sup>16</sup> Order Remanding Proceeding at 7 (Jun. 30, 2022) (Remand Order).

unreasonably preferential, prejudicial, or discriminatory but... sufficient, equitable, and consistent in application to each class of consumers.”<sup>17</sup> If WOWSC’s rates fail to meet these standards, the Commission must set new rates.<sup>18</sup> Importantly, however, the Commission must “use a methodology that preserves the financial integrity of the retail public utility.”<sup>19</sup>

As discussed in WOWSC’s Initial Brief, WOWSC’s customers demonstrate similar characteristics and, as such, the appealed rates of general applicability are nondiscriminatory and equitable. Further, because the record clearly shows that the legal expenses at issue were both reasonable and necessary, WOWSC’s inclusion of the expenses in its annual base rates resulted in just and reasonable rates. Thus, the Commission should deny Staff’s recommendation to open an unnecessary and administratively burdensome Compliance Docket. Furthermore, if the Commission adopts Staff’s proposed rates and refund, the utility will be unable to provide safe and adequate water and wastewater services to its members within one year. Finally, WOWSC’s rate case expenses are reasonable and should be recovered in full. The Commission should therefore deny Ratepayers’ appeal and allow WOWSC to continue charging the appealed rates. In the alternative, the Commission should allow WOWSC to recover its legal expenses through a surcharge<sup>20</sup> or assessment in accordance with Staff’s recommendation.<sup>21</sup>

## **II. CUSTOMER CHARACTERISTICS AND DISCRIMINATORY RATES**

A uniform rate charged equally to all customers is not, on its own, equitable and consistent in application.<sup>22</sup> Rather, to demonstrate that a uniform rate is nondiscriminatory, the utility must also show that its customers’ characteristics do not differ in a meaningful manner.<sup>23</sup> Because WOWSC’s customers reside in the same location and receive the same services from the same

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<sup>17</sup> TWC § 13.043(j).

<sup>18</sup> Remand Order at 8.

<sup>19</sup> TWC § 13.043(j).

<sup>20</sup> In WOWSC’s Initial Brief, the Corporation requested that the Commission, if it adopts Staff’s proposed rates, authorize WOWSC to recover the \$171,337 of outside legal fees through a surcharge. WOWSC’s Initial Brief at 3, 14. To further clarify, if the Commission adopts Staff’s proposed rates, WOWSC requests an *annual* surcharge of \$171,337 until it pays its legal debt in full.

<sup>21</sup> Tr. at 857:12-19 (Givens Cross) (Mar. 22, 2023); WOWSC Ex. 27, Attachment MN-8, (Commission Staff witness Anna Givens adopting Commission Staff witness Maxine Gilford’s testimony that WOWSC could recover rate case expenses through a surcharge); *see also* Staff’s Initial Brief at 8.

<sup>22</sup> Remand Order at 6.

<sup>23</sup> *See Id.*

facilities, the Corporation appropriately grouped all its customers in one class.<sup>24</sup> Thus, the appealed rates charged equally to all WOWSC customers are non-discriminatory.

As discussed in WOWSC's Initial Brief, The American Water Works Association provides that, when a utility establishes customer classes, the utility should consider the location of its customers, service characteristics, and demand patterns.<sup>25</sup> Service characteristics refer to both the actual services provided, such as raw versus treated water, and the facilities that provide the service, such as transmission versus distribution systems.<sup>26</sup> Demand patterns capture the cost to serve a particular customer by considering the customer's total demand and the difference between the customer's peak and average service uses.<sup>27</sup> Noticeably absent from these considerations is whether a customer identifies as commercial, residential, or irrigation.<sup>28</sup> This consideration is insignificant because, for purposes of customer classes, utilities should only consider factors that impact costs to provide water and wastewater services.<sup>29</sup>

Nevertheless, Ratepayers alleges that because WOWSC does not distinguish residential and non-residential customers, the Corporation's ratepayers necessarily have "a variety of characteristics."<sup>30</sup> Ratepayers cites to WOWSC's RFI response where former WOWSC President Joe Gimenez provided that "WOWSC's tariff does not request members to clarify whether its members are residential or non-residential."<sup>31</sup> It subsequently cites to Mr. Gimenez's testimony that, to determine whether more than one property has multiple connections to one grinder pump, Mr. Gimenez stated he "would have to check with our manager to see if he has those records."<sup>32</sup>

Ratepayers misconstrues and greatly expands these statements to provide "Windermere supports the opinion that the tariff does not require applicants to disclose...their classification such

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<sup>24</sup> WOWSC Ex. 24, Supplemental Direct Testimony of Grant Rabon at Bates 7, Bates 10.

<sup>25</sup> *Id.* at Bates 5; Attachment GR-2.

<sup>26</sup> *Id.*

<sup>27</sup> WOWSC Ex. 24 at Bates 4.

<sup>28</sup> *Id.* at Bates 6.

<sup>29</sup> *Id.* at Bates 7.

<sup>30</sup> Ratepayers' Initial Brief at 10-11.

<sup>31</sup> Ratepayers' Initial Brief at 10; *see also* Staff HoM2 Ex 19, Windermere's Response to Staff RFI 6-12.

<sup>32</sup> Ratepayers' Initial Brief at 12.



as single-family residence, commercial, industrial or irrigation.”<sup>33</sup> It provides no citation to this statement.<sup>34</sup> It then alleges that, because of WOWSC’s alleged reporting deficiencies, “clearly a variety of characteristics among ratepayers do exist.”<sup>35</sup> Again, it provides no citation to this statement that supports any “variety” between WOWSC member characteristics.<sup>36</sup> Rather, it relies on a single commercial hangar that has multiple connections to one meter. The hangar Ratepayers refers to is a grandfathered property constructed before WOWSC was formed.<sup>37</sup> This is the only property known by WOWSC with different entities that share a single meter.<sup>38</sup> It would be improper and unnecessary for WOWSC to establish a separate customer class for a single, grandfathered property as Ratepayers suggests.

Moreover, as discussed in WOWSC’s Initial Brief, the airport hangar accounts and single-family residential (SFR) accounts both impose similar costs on WOWSC’s provision of service.<sup>39</sup> It is therefore irrelevant, for purposes of customer classes, that one property with different entities share a single meter: this property has a similar cost to serve compared to all other WOWSC connections.<sup>40</sup> Thus, despite this single grandfathered property, all WOWSC members reside in the WOWSC subdivision, receive the same potable water and wastewater service from the same facilities and water source, and have a similar demand pattern.<sup>41</sup> WOWSC’s alleged reporting deficiencies—which Ratepayers provides no evidence to support—are irrelevant. Rather, to show that WOWSC’s customers do indeed have different characteristics, Ratepayers must provide evidence that WOWSC serves customers with meaningfully different costs to serve.<sup>42</sup> Ratepayers provided no such evidence, and Staff’s silence on this issue further supports WOWSC’s position.<sup>43</sup> Therefore, Ratepayers’ unfounded allegations must be dismissed.

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<sup>33</sup> Ratepayers’ Initial Brief at 11.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> Staff HoM2 Ex. 17, Windermere’s Confidential Response to Staff RFI 6-10.

<sup>38</sup> *Id.*

<sup>39</sup> WOWSC’s Initial Brief at 4; *see also* WOWSC Ex. 24 at Bates 9.

<sup>40</sup> WOWSC Ex. 24 at Bates 9.

<sup>41</sup> WOWSC’s Initial Brief at 5; *see also* WOWSC Ex. 24 at Bates 10.

<sup>42</sup> WOWSC Ex. 24 at Bates 7.

<sup>43</sup> Staff’s Initial Brief at 5.

In sum, because WOWSC's customers reside in the same location, receive the same service, and impose similar costs on WOWSC, the customers have similar characteristics.<sup>44</sup> It is therefore appropriate to group all WOWSC customers in a single class and charge the customers a single rate. Thus, in accordance with TWC § 13.043(j), the appealed rates are not unreasonably preferential, prejudicial, or discriminatory.<sup>45</sup>

### **III. STAFF'S REVENUE REQUIREMENT AND RECOMMENDED RATES**

Staff alleges that WOWSC has failed to show that its 2019 outside legal expenses were reasonable and beneficial to its ratepayers and, therefore, recommends removing \$171,337 from the Corporation's annual base rate cost recovery.<sup>46</sup> As such, Staff recommends that the Commission order WOWSC to charge a new monthly base water rate of \$40.43 and a new monthly base wastewater rate of \$29.81 in place of the appealed rates of \$90.39 and \$66.41, respectively.<sup>47</sup> Staff further suggests that the Commission order WOWSC to refund the difference between the appealed rates and Staff's proposed rates for the period starting on the effective date of March 23, 2020, and first billing on or about September 1, 2023.<sup>48</sup>

Staff continues to rely on Ratepayers' mischaracterization of the underlying litigation and disregards WOWSC's statutory duty to protect itself and its directors from legal threats.<sup>49</sup> It disregards recent developments in the underlying litigation that show, in contrast to Staff's assertion,<sup>50</sup> WOWSC has acted reasonably and limited legal fees to the benefit of its ratepayers.<sup>51</sup> And perhaps most importantly, it misconstrues WOWSC's financial records and chooses to ignore the detrimental impact Staff's rates and proposed refund would have on the Corporation's financial

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<sup>44</sup> WOWSC Ex. 24 at Bates 10.

<sup>45</sup> TWC § 13.043(j).

<sup>46</sup> Staff Ex. 4, Direct Testimony of Maxine Gilford at 12; Tr. at 844:21-24 (Givens Cross) (Mar. 22, 2023); *see also* Prehearing Conference Tr. at 21:16-17 (ALJ Siano) (Mar. 21, 2023) (granting Commission Staff's motion to adopt Maxine Gilford's testimony).

<sup>47</sup> Staff HoM2 Ex. 1, Supplemental Direct Testimony of Stephen Mendoza at 4:12-26, 5:5-13.

<sup>48</sup> Staff HoM2 Ex. 2, Supplemental Direct Testimony of Anna Givens at 8 (Bates 10).

<sup>49</sup> WOWSC's Reply Brief at 9-10 (Jan. 25, 2022).

<sup>50</sup> Staff's Initial Brief at 4 (alleging that WOWSC's rate-making policy allows "Windermere's board of directors *carte balance*...for legal expenses").

<sup>51</sup> WOWSC Ex. 26 at Bates 8:3-13:19.

integrity.<sup>52</sup> Staff's proposed rates and refund should therefore be rejected, and the Commission should allow WOWSC to continue charging the appealed rates instead.

In the alternative, Staff recommends that WOWSC, if it exhausts all available revenue streams, recover its legal expenses through an assessment or surcharge.<sup>53</sup> WOWSC will soon adopt a resolution to amend its tariff to allow for a surcharge to recover its legal expenses.<sup>54</sup> Importantly, including these legal fees in a surcharge would enable WOWSC to continue operations.<sup>55</sup> As such, if the Commission does ultimately adopt Staff's proposed rates, it should allow WOWSC to recover the underlying legal fees through a surcharge.

#### **A. WOWSC's Revenue Requirement**

Staff emphasizes that WOWSC has "misrepresented" its revenue requirement "time and time again."<sup>56</sup> It claims—without any legal citations—that because the appealed rates "are premised on a false revenue requirement," the rates are necessarily "neither just nor reasonable."<sup>57</sup> In other words, Commission Staff alleges that the appealed rates violate TWC § 13.043 merely because, when WOWSC set the appealed rates, the Corporation allegedly misapplied the Texas Rural Water Association's (TRWA) \$576,192 revenue requirement.

But Staff fails to mention that WOWSC, as a non-profit water supply corporation under Chapter 67 of the TWC,<sup>58</sup> has far greater ratemaking discretion compared to other utilities.<sup>59</sup> Specifically, because the Corporation operates in accordance with TWC §§67.007, 13.002(11), 13.002(24), WOWSC is not subject to the Commission's original jurisdiction.<sup>60</sup> WOWSC's rates

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<sup>52</sup> WOWSC Ex. 27 at Bates 8:5-11:2.

<sup>53</sup> Tr. at 857:12-19 (Givens Cross) (Mar. 22, 2023); *see also* WOWSC Ex. 27, Attachment MN-8, (Commission Staff witness Anna Givens adopting Commission Staff witness Maxine Gilford's testimony that WOWSC could recover legal expenses through a surcharge); Commission Staff's Initial Brief at 8.

<sup>54</sup> WOWSC Ex. 26 at Bates 14:4-15; Staff's Initial Brief at 9-10.

<sup>55</sup> WOWSC Ex. 27 at Bates 5:8-16.

<sup>56</sup> Staff's Initial Brief at 1.

<sup>57</sup> *Id.* at 2.

<sup>58</sup> WOWSC Ex. 2 at Bates 27.

<sup>59</sup> *See* TWC § 13.004.

<sup>60</sup> *Compare* TWC § 13.004 (providing that the Commission has "the same jurisdiction over a water supply or sewer service corporation that the [Commission] has...over a water and sewer utility" only under particular circumstances), *with* TWC § 13.041 (providing the Commission with original jurisdiction over water and sewer utilities); *see also* 16 TAC § 24.47.

are, therefore, only subject to the Commission's appellate jurisdiction.<sup>61</sup> Put differently, the manner in which WOWSC originally established the appealed rates is not binding on the Commission's decision, so long as the rates are ultimately just and reasonable, and not unreasonably preferential, prejudicial, or discriminatory, in accordance with TWC § 13.043(j).<sup>62</sup> As discussed further below, WOWSC's rates meet this threshold.

Moreover, WOWSC has consistently maintained that to establish the appealed rates it relied on the TRWA Model, which computed a \$576,192 revenue requirement using 2019 financials, and subsequently adjusted the TRWA-recommended rates to account for an increase in legal fees identified in the 2020 budget.<sup>63</sup> The adjusted rates were ultimately lower than the TRWA computed rates and, therefore, WOWSC adopted them to minimize burden on its members.<sup>64</sup> This has been WOWSC's position throughout testimony, hearing, and discovery.<sup>65</sup> Moreover, it amended previous RFI responses to further clarify this ratemaking process.<sup>66</sup> But Ratepayers again mischaracterizes the record and asserts that WOWSC now represents that its revenue requirement

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<sup>61</sup> TWC §§ 13.004; 13.002(23) (defining "water and sewer utilities"); 13.043(b)(1) (authorizing nonprofit water supply or sewer service corporation to appeal rates to the Commission).

<sup>62</sup> TWC § 13.043(j).

<sup>63</sup> Staff HoM2 Ex. 25, Windermere's Supplemental Response to Staff RFI 1-1.

<sup>64</sup> *Id.*

<sup>65</sup> See WOWSC Ex. 36 OC, WOWSC's Response to Staff RFI 6-7 at Bates 2 (stating that "[t]he TRWA spreadsheet generated the calculated base rates at roughly \$175. The Board used the financial data and determined that, to add to the previous year's legal fee budget of roughly \$3,150 per month and to satisfy its obligations to law firms that totaled \$20,000 per month (\$250,000 in the year 2020), it required an extra \$16,000 per month. Thus, because the Board could collect \$16,000 per month with a rate lower than \$175, it reduced the base rate to reflect the amount needed for ongoing legal fees."); Tr. at 199:1-11 (Nelson Cross) (Dec. 1, 2021) (providing that "the concept was to look at 2019, right, use it in a rate study to understand how high we could increase rates and then see if we could meet the \$10,000 a month per law firm [in the 2020 budget]"); Tr. at 199:8-11 (Nelson Cross) (Dec. 1, 2021) (WOWSC answering "[y]ep" after questioned whether WOWSC "designed these rates to enable you to meet a budget of 10,000 a month per law firm going forward"); WOWSC Ex. 7, Direct Testimony of Mike Nelson at Bates 9:4-7 (Nelson Direct) (providing that "WOWSC's 2020 budget estimated a net loss of \$174,515 primarily by estimated legal costs of \$250,000.... In order to defend itself in these various lawsuits, WOWSC needed to increase rates in order to be able to continue providing safe and adequate water and sewer service while also paying the necessary legal fees associated with ongoing litigation"); Ratepayers Ex. 12, WOWSC's Supplemental Response to Staff's First RFI at Bates 36 (WOWSC stating that "[t]he 2020 Budget shows that without the rate increase, WOWSC projected a \$174,515.00 loss").

<sup>66</sup> See Staff HoM2 Ex. 3, WOWSC's Supplemental Response to Staff's RFI 1-2; Staff HoM2 Ex. 4, WOWSC's Supplemental Response to Staff's RFI 1-4; Staff HoM2 Ex. 5, Supplemental Response to Staff's RFI 1-11; Staff HoM2 6, WOWSC's Supplemental Response to Staff's RFI 1-17; Staff HoM2 7, Supplemental Response to Staff's RFI 1-25.

is \$674,905.75.<sup>67</sup> To support its claim, Ratepayers cites to an RFI response where it had ask WOWSC to perform extraneous calculations and which WOWSC expressly stated this amount is “*not a revenue requirement* and would not be appropriate for setting rates.”<sup>68</sup> Staff witness Anna Givens stated that she had “no reason to disagree” with this statement.<sup>69</sup> As such, Ratepayers’ mischaracterization is unsupported and, therefore, must be rejected.

Importantly, WOWSC’s board is composed of volunteer directors who have offered, and were elected to, spend their time running a water and wastewater utility in their community.<sup>70</sup> They are not employees of the utility and have responsibilities outside of their capacity as WOWSC directors.<sup>71</sup> As such, WOWSC’s directors are not ratemaking experts. Although WOWSC may have utilized its revenue requirement in a manner in which Staff is unfamiliar to establish the appealed rates, this alone does not establish that the rates are unjust and unreasonable.<sup>72</sup> Staff implies this but provides no legal citation to support its claim.<sup>73</sup> In contrast to Staff’s assumption, the just and reasonable standard does not require that WOWSC set rates “to recover [its] cost of service down to the cent.”<sup>74</sup> Rather, WOWSC’s rates “must be set within a range of reasonable values.”<sup>75</sup> As discussed further below, WOWSC’s ratemaking process resulted in rates “set within a range of reasonable values” and recovers only reasonable and necessary expenses. Staff’s allegations regarding “mischaracterization[s]” of WOWSC’s revenue requirement and related legal assertions must therefore be rejected.

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<sup>67</sup> Ratepayers’ Initial Brief at 20-21.

<sup>68</sup> *Id.*; Staff HoM2 Ex. 58, WOWSC’s Response to Ratepayer RFI 8-2 at Bates 4 (emphasis added).

<sup>69</sup> Tr. at 891:7-15 (Givens Recross) (Mar. 22, 2023).

<sup>70</sup> WOWSC Ex. 2, Direct Testimony of Joe Gimenez, III at 5:21-6:3 (Bates 6:21-7:3).

<sup>71</sup> *See* WOWSC Ex. 2 at 4:1-7 (Bates 5:1-7).

<sup>72</sup> *See* Staff Ex. 4 at 8:1-20 (providing that just and reasonable rates provide a utility with “adequate debt service, reasonable interest rates, ability to maintain facilities, and ability to obtain funding for future infrastructure”); *Petition of Paloma Lake Municipal Utility District No. 1, et al. Appealing the Ratemaking Actions of the City of Round Rock in Travis and Williamson Counties*, PUC Docket No. 48836, Order on Appeal of SOAH Order No. 17 at 3 (Apr. 29, 2022).

<sup>73</sup> Staff’s Initial Brief at 2 (stating that “Windermere’s rates are neither just nor reasonable as they are premised on a false revenue requirement” but providing no citation).

<sup>74</sup> *Petition of Paloma Lake Municipal Utility District No. 1, et al. Appealing the Ratemaking Actions of the City of Round Rock in Travis and Williamson Counties*, PUC Docket No. 48836, Order on Appeal of SOAH Order No. 17 at 3 (Apr. 29, 2022).

<sup>75</sup> *Id.*

**1. WOWSC's rates collect budgeted legal expenses anticipated with reasonable certainty.**

Under the just and reasonable standard, a water supply corporation's rates may "collect only expenses actually realized or which can be anticipated with reasonable certainty."<sup>76</sup> Ratepayers asserts that because WOWSC, at the time it set the appealed rates, did not have projections for total future legal costs, it was improper for WOWSC to incorporate into the appealed rates the \$250,000 budgeted legal fees that included the \$171,337 of 2019 legal fees.<sup>77</sup> However, WOWSC knew that pursuant to its payment agreements with outside law firms, it would owe \$20,000 a month for its legal representation for the foreseeable future.<sup>78</sup> And it knew that once its legal fees were fully paid in accordance with the payment agreements, it would lower its base rates.<sup>79</sup> Therefore, the total future legal expenses are irrelevant: WOWSC knew at the time it set the appealed rates, with absolute certainty, that it would owe \$20,000 in legal fees a month until it pays off its legal debt. Its 2020 budget and monthly profit and loss statements reflect this certainty.<sup>80</sup> Importantly, its general ledger shows that after the appealed rates went into effect, WOWSC consistently paid Lloyd Gosselink and Enoch Kever in accordance with the Corporation's 2020 budget.<sup>81</sup>

Ratepayers implies that WOWSC improperly approved its payment plan and, without any citation, asserts that "Windermere never told CoBank about any alleged 'minimum payment' arrangement."<sup>82</sup> But in the sentence directly after this assertion, Ratepayers quotes a WOWSC email that disclosed to CoBank WOWSC's minimum payment plan at issue.<sup>83</sup> As such, Ratepayers' assertions are unsupported by the record. More importantly, the assertions are

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<sup>76</sup> *Id.*; see also *Suburban Util. Corp. v. Pub. Util. Comm'n of Tex.*, 652 S.W.2d 358, 362 (Tex. 1983).

<sup>77</sup> Ratepayers' Initial Brief at 18-19.

<sup>78</sup> Tr. 198:9-14, 199:1-11 (Nelson Cross) (Dec. 1, 2021); see also Staff HoM2 Ex. 41, WOWSC's Response to Staff RF1 8-5 at Bates 1-2.

<sup>79</sup> WOWSC Ex. 26 at 13:20-14:3.

<sup>80</sup> Staff HoM2 Ex. 41 at Bates 2 (note that WOWSC's 2020 budget grouped "appraisal" and "legal" expenses together, which total \$250,000); see, e.g., WOWSC Ex. 27 at Attachment MN-12, Bates 13 (Providing that February 2022 budget related to underlying lawsuits was \$20,000).

<sup>81</sup> See, e.g., Ratepayers HOM2 Ex. 119, Windermere 2021 GL from Attachment Ratepayers 8-24 at Bates 1-6.

<sup>82</sup> Ratepayers' Initial Brief at 19.

<sup>83</sup> *Id.*

completely irrelevant for purposes of this rate appeal and should therefore be rejected. In sum, because WOWSC knew with “reasonable certainty” that it would owe \$20,000 a month for its legal representation, it validly incorporated this amount into its base rates.

**2. WOWSC does not object to Staff’s recommendation related to the Corporation’s depreciation expense.**

WOWSC does not contest Commission Staff’s recommendation that the Corporation record the revenues it recovers through its annual depreciation expense as customer-contributed capital in WOWSC’s Capital Expenditure Reserve, and to use such revenues to fund future plant investment.<sup>84</sup>

**B. Just and Reasonable Outside Legal Expenses**

Just and reasonable rates provide a utility with the amount necessary to maintain an adequate debt service, obtain funding for future infrastructure, and pay operating and maintenance expenses associated with the provision of adequate water and wastewater services.<sup>85</sup> The National Association of Regulatory Utility Commissioners’ (NARUC) definition of “operation and maintenance” *includes legal fees* and books these fees under “Account 631.”<sup>86</sup> The Commission operates under the NARUC chart of accounts and, therefore, classifies legal fees as expenses associated with the operation and maintenance of a utility.<sup>87</sup> Thus, a utility may recover through its base rates reasonable and necessary legal fees as a cost of service.<sup>88</sup>

The TWC specifically authorizes a non-profit water supply corporation to “employ and compensate counsel to represent the corporation as the board determines is necessary.”<sup>89</sup> And importantly, the Texas Business and Organizations Code provides that a non-profit corporation “*shall indemnify a governing person, former governing person...against reasonable expenses actually incurred by the person in connection with a proceeding in which the person is a respondent because the person is or was a governing person...if the person is wholly successful...in the*

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<sup>84</sup> Staff’s Initial Brief at 8-9.

<sup>85</sup> See Staff Ex. 4 at 8:1-20; 16 TAC § 24.41(b)(1)(A).

<sup>86</sup> Tr. 845:6-17 (Givens Cross) (Mar. 22, 2023). WOWSC similarly categorizes its legal expenses under Account 631. Tr. at 847:10-20 (Givens Cross) (Mar. 22, 2023); see also WOWSC Ex. 17, WOWSC’s Response to Ratepayers RFI 1-12 at Bates 7.

<sup>87</sup> See Tr. at 846:8-15 (Givens Cross) (Mar. 22, 2023).

<sup>88</sup> See 16 TAC § 24.41(b)(1)(A).

<sup>89</sup> TWC § 67.013.

defense of the proceeding.”<sup>90</sup> Texas courts broadly construe TBOC § 8.051 and, if a governing person is successful in her defense, have found that “indemnification is *mandatory*” even if “disinterested governing persons” failed to approve the indemnification by vote under TBOC § 8.031.<sup>91</sup>

The record is clear: the legal fees at issue were necessary. As discussed in WOWSC’s Initial Brief, the Corporation incurred the fees defending itself and its directors against a handful of WOWSC members who, after exhausting all other remedies through litigation, the election process, and even social media harassment,<sup>92</sup> attempt to use this rate appeal as a forum to resolve local disputes.<sup>93</sup> In fact, Ratepayers initiated all the underlying lawsuits other than the *Paxton* Lawsuit, which WOWSC filed in response to Ratepayers’ PIA requests to preserve confidential information.<sup>94</sup> In their Initial Brief, Ratepayers again disregards WOWSC’s duties under the TBOC and allege that—without any citations to the record or law—WOWSC had “no obligation” to defend its directors and that “[a] majority of the board... were [sic] motivated by self-interest.”<sup>95</sup> In fact, the majority of Ratepayers’ allegations regarding WOWSC’s involvement in the underlying lawsuits lack citations to the record altogether.<sup>96</sup> They should therefore be rejected.

Staff justifies its exclusion of outside legal expenses by characterizing WOWSC’s Board of Directors as recklessly approving legal expenses without limit and without check.<sup>97</sup> But again, Staff fails to review the underlying litigation and, therefore, apparently relies on Ratepayers’ erratic and unsupported mischaracterizations.<sup>98</sup> One of the few exhibits Commission Staff does rely on to characterize WOWSC’s legal expenses as imprudent was not admitted at hearing and, therefore, is not in the record.<sup>99</sup> Put differently, Staff blindly follows Ratepayers—the same

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<sup>90</sup> TBOC § 8.051 (emphasis added); *see also* TBOC § 8.002 (providing that § 8.051 applies to non-profit corporations).

<sup>91</sup> *Hotze v. IN Mgmt., LLC*, 651 S.W.3d 19, 33 (Tex. App.—Houston [14<sup>th</sup> Dist.] 2021, pet. Filed) (emphasis added).

<sup>92</sup> WOWSC Ex. 2 at 19:16-20:10 (Bates 20:16-21:10).

<sup>93</sup> *Id.* at 16:13-20 (Bates 17:13-20), 21:10-22:11 (Bates 22:10-23:11); WOWSC Ex. 26 at Bates 7:10-11:15.

<sup>94</sup> WOWSC Ex. 3 at Bates 9:6-14; WOWSC Ex. 26 at Bates 7:10-8:2, Bates 8:3-19, Bates 10:12-15.

<sup>95</sup> Ratepayers’ Initial Brief at 17.

<sup>96</sup> *Id.* at 14, 17.

<sup>97</sup> Staff’s Initial Brief at 4.

<sup>98</sup> *Id.*

<sup>99</sup> Compare Staff’s Initial Brief at 4, FN16 (citing to Ratepayers HoM 2 Ex. 48), with Tr. Table of Contents



members who brought the underlying lawsuits against the Corporation—and without any explanation proclaims that WOWSC’s legal fees were unreasonable.

**1. Texas statute required WOWSC to incur the legal fees at issue.**

The record<sup>100</sup> shows that the \$171,337 of legal fees at issue in this proceeding relate to (1) general counsel for contracts, Public Information Act (PIA) requests, Open Meeting Act compliance, and general member inquiries regarding Texas law and WOWSC’s corporate bylaws; (2) *WOWSC v. The Honorable Ken Paxton* (“Paxton Lawsuit”);<sup>101</sup> (3) *TOMA Integrity v. WOWSC* (“TOMA Lawsuit”);<sup>102</sup> and (4) *Rene Ffrench, et al. v. Friendship Homes & Hangers, LLC, et al.* (“Double F Hanger Lawsuit”).<sup>103</sup> As Staff provides, due to these lawsuits, “evaluating the justness and reasonableness of [WOWSC’s] rates...requires a slightly more nuanced approach” compared to normal rate appeals.<sup>104</sup> Nevertheless, Staff failed to review the underlying litigation altogether. As discussed below, however, these matters required that WOWSC incur the legal fees now at issue.

In 2018, several WOWSC members including Patti Flunker, one of the Ratepayer Representatives, initiated the *TOMA* Lawsuit seeking mandamus against WOWSC related to a land transaction.<sup>105</sup> As a named defendant in the *TOMA* Lawsuit, WOWSC was required to incur legal expenses to defend itself.<sup>106</sup> The trial court and court of appeals both denied the plaintiffs’ requested remedy and, after the plaintiffs appealed to the Texas Supreme Court, the Court refused

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at xi (providing that Ratepayers HoM 2 Ex. 48 was offered but not admitted).

<sup>100</sup> WOWSC Ex. 26 at Bates 7:16-8:2; WOWSC Ex. 3 at Bates 7:1-8:8, 9:6-10:7.

<sup>101</sup> *Windermere Oaks Water Supply Corporation v. The Honorable Ken Paxton, Attorney General of Texas*, Cause No. D-1-GN-19-006219 (201<sup>st</sup> Dist. Ct., Travis County, Tex. Sept. 16, 2019) (*Paxton Lawsuit*).

<sup>102</sup> *TOMA Integrity v. Windermere Oaks Water Supply Corporation*, Cause No. 47531 (33<sup>rd</sup> Dist. Ct., Burnet County, Tex., Dec. 12, 2017) (*TOMA Lawsuit*).

<sup>103</sup> *Rene Ffrench, John Richard Dial, Stuart Bruce Sorgen, and as Representatives for Windermere Oaks Water Supply Corporation v. Friendship Homes & Hangers, LLC; WOWSC; and its Directors William Earnest, Thomas Michael Madden, Dana Martin, Robert Mebane, and Patrick Mulligan (originally styled Double F Hanger Operations, LLC, Lawrence R. Ffrench, Jr., Patricia Flunker, and Mark A. McDonald v. Friendship Homes & Hangers, LLC, and Burnet County Commissioners Court)*, No. 48292 (33<sup>rd</sup> Dist. Ct., Burnet County, Tex. Jul. 9, 2018) (*Double F Hanger Lawsuit*).

<sup>104</sup> Staff’s Initial Brief at 4.

<sup>105</sup> WOWSC Ex. 2 at 18:3-10 (Bates 19:3-10); WOWSC Ex. 3 at 9:11-14.

<sup>106</sup> *Id.* at 18:22-19:15 (Bates 19:22-20:15).

to reconsider the case.<sup>107</sup> Around this time, the Corporation started to receive an inordinate amount of PIA requests from individuals involved in the *TOMA* lawsuit, including an individual that cohabitates with Ratepayer Representative Patti Flunker.<sup>108</sup> Due to the litigious nature of the PIA requestors, WOWSC retained legal counsel to ensure compliance with the PIA and avoid future lawsuits.<sup>109</sup>

These PIA requests eventually forced WOWSC to bring the *Paxton* Lawsuit against the Attorney General's office (AG) to prevent disclosure of privileged information.<sup>110</sup> Although the AG changed its position and ultimately agreed with the Corporation that the PIA excepted the requested information from disclosure, the PIA requester engaged attorney Kathryn Allen—who now represents Ratepayers in this proceeding—to intervene.<sup>111</sup> As such, despite its superior legal standing, WOWSC released the information to reduce the legal fees now at issue.<sup>112</sup>

Finally, in 2019 the same plaintiffs in the *TOMA* Lawsuit, including Ratepayer Representative Patti Flunker, again retained Kathryn Allen and initiated the *Double F Hanger* Lawsuit suing the Corporation and five former directors in their capacity as WOWSC directors for their involvement in the land transaction at issue in the *TOMA* Lawsuit.<sup>113</sup> Subsequently, the plaintiffs modified their suit to also name three active directors in their capacity as WOWSC directors.<sup>114</sup> As such, the plaintiffs structured their lawsuit in a manner that required WOWSC to retain multiple law firms to provide proper defenses for both the Corporation and its directors, resulting in increased legal fees.<sup>115</sup>

Importantly, however, WOWSC has done everything in its power to limit legal expenses to the benefit of its ratepayers. It prudently required each named director defendant to sign an

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<sup>107</sup> WOWSC Ex. 26 at 9:1-6.

<sup>108</sup> WOWSC Ex. 2 at 14:15-15:12 (Bates 15:15-16:12), 21:10-17 (Bates 22:10-17); *see also* Voluminous Attachment to WOWSC Ex. 3 (PIA requests).

<sup>109</sup> WOWSC Ex. 2 at 15:12-17 (Bates 16:12-17).

<sup>110</sup> WOWSC Ex. 26 at 8:3-7.

<sup>111</sup> *Id.* at 8:8-10.

<sup>112</sup> *Id.* at 8:10-19.

<sup>113</sup> WOWSC Ex. 2 at 18:11-12 (Bates 19:11-12), 19:9-11 (Bates 20:9-11); WOWSC Ex. 3 at 9:6-14, Attachment JG-21 at Bates 57; *see also* WOWSC Ex. 3 at Attachment JG-25 (*Double F Hanger* Lawsuit First Amended Petition).

<sup>114</sup> WOWSC Ex. 2 at 19:12-15 (Bates 20:12-15).

<sup>115</sup> WOWSC Ex. 3 at 7:12-14, Attachment JG 22 at Bates 19-20.

indemnification agreement that guaranteed legal fee reimbursement to WOWSC if “any final determination is made by a Court” that the director breached her fiduciary duty.<sup>116</sup> And despite Ratepayers demands, WOWSC refrained from bringing the *Double F Hanger* Lawsuit against former WOWSC director Dana Martin and incurring additional legal fees.<sup>117</sup> Recently, after plaintiffs spent over \$400,000 in legal fees in the *Double F Hanger* Lawsuit, the jury returned a verdict against Dana Martin for a mere \$70,000, further vindicating WOWSC’s legal decision making.<sup>118</sup> Finally, WOWSC attempted to mitigate outside legal expenses associated with the *Double F Hanger* Lawsuit through demand letters, mediations, and community meetings.<sup>119</sup> Unfortunately, after extensive effort, resolution was unsuccessful due to the plaintiffs’ litigious nature.<sup>120</sup>

In sum, Ratepayers required that WOWSC incur the \$171,337 of legal fees at issue, and the extensive amount WOWSC has continued to incur since 2019. First, WOWSC initiated the *Paxton* Lawsuit, an administrative proceeding limited in scope and cost, to protect privileged information from Ratepayers and ultimately nonsuited the suit to avoid incurring additional legal expenses.<sup>121</sup> Second, as Staff witness Maxine Gilford previously conceded, WOWSC was a named defendant in the *TOMA* and *Double F Hanger* Lawsuits and was therefore required to defend itself.<sup>122</sup> Third, because Ratepayers sued the WOWSC directors “in their official capacities as current or former Directors and/or Officers of the WSC,” the TBOC § 8.051 *required* WOWSC to indemnify its current and former directors in the *Double F Hanger* Lawsuit.<sup>123</sup> It is therefore irrelevant, even if true, that the “member lawsuits and PIA requests posed no risk to the company.”<sup>124</sup> Sound corporate judgment required that WOWSC defend itself and protect its interests. Texas law required that WOWSC indemnify its directors and adequately respond to

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<sup>116</sup> WOWSC Ex. 26 at Bates 136.

<sup>117</sup> WOWSC Ex. 3 at Bates 12:1-17.

<sup>118</sup> *Id.* at Bates 10:8-17, 19:6-14; WOWSC Ex. 26, Attachment JG-44 at p. 3 of 98 (Bates 40).

<sup>119</sup> *Id.* at Bates 18:5-19:6.

<sup>120</sup> WOWSC’s Initial Brief at 12.

<sup>121</sup> WOWSC Ex. 26 at 8:14-19.

<sup>122</sup> Staff Ex. 4 at 12:14-15 (Commission Staff witness Maxine Gilford providing “I understand that Windermere could not just ignore the *TOMA* and *Ultra Vires* suits”).

<sup>123</sup> WOWSC Ex. 3 at Attachment JG-25 at Bates 1-2; TBOC § 8.051; *Hotze*, 651 S.W.3d at 33.

<sup>124</sup> Ratepayers’ Initial Brief at 15-16.

Ratepayers' PIA requests. The related legal fees were, therefore, necessary and reasonable costs of service.<sup>125</sup> As such, the Commission should allow WOWSC to continue charging the appealed rates or, in the alternative, allow WOWSC to recover its legal expenses through a surcharge.

### **C. Staff's Revenue Requirement**

The Commission must set rates that preserve the utility's financial integrity.<sup>126</sup> Although there is no definition or standard of "financial integrity," the Supreme Court of Texas has found that an investor owned utility (IOU) must be allowed to recover its operating expenses together with a reasonable return on invested capital.<sup>127</sup> Importantly, that requirement is "only met if the return is sufficient to ensure confidence in the financial integrity of the enterprise, *so as to maintain its credit and to attract capital.*"<sup>128</sup>

In contrast to an IOU, however, WOWSC is a nonprofit water supply corporation that does not have any shareholders and, therefore, may only realistically pay its legal expenses and maintain its credit through rates.<sup>129</sup> As discussed in WOWSC's Initial Brief, WOWSC may eventually recover Dana Martin's defense costs, Allied World Insurance's (Allied) settlement, and damages from the *Double F Hanger* lawsuit, and would use this recovery to pay its legal debt.<sup>130</sup> But the recovery is still uncertain and subject to the judicial process.<sup>131</sup> WOWSC's financial integrity, therefore, depends on recovery of the 2019 legal fees through its base rates or a surcharge.

Ratepayers implies that because WOWSC's Board has mismanaged the Corporation's financial affairs, the Commission is not required to establish rates that preserve WOWSC's financial integrity.<sup>132</sup> As discussed below, however, it supports these allegations with fabricated loan and financial reporting requirements and a mischaracterization of financial records.<sup>133</sup> It even attempts to show that WOWSC, merely because it retained outside counsel, violated federal tax

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<sup>125</sup> See 16 TAC § 24.41 (emphasis added) (providing that a utility's cost of service includes "expenses that are reasonable and *necessary* to provide service to the ratepayers").

<sup>126</sup> TWC § 13.043(j).

<sup>127</sup> *Suburban Util. Corp.*, 652 S.W.2d at 362.

<sup>128</sup> *Id.*

<sup>129</sup> WOWSC Ex. 27 at Bates 11:5-13.

<sup>130</sup> WOWSC Ex. 26 at Bates 11:16-12:9, Bates 13:1-19.

<sup>131</sup> *Id.*

<sup>132</sup> Ratepayers' Initial Brief at 22-26; Staff's Initial Brief at 4.

<sup>133</sup> Ratepayers' Initial Brief at 16-19, 22-26.

law.<sup>134</sup> Again, these allegations are unfounded and blatantly false, but more importantly, well outside the scope of this proceeding.<sup>135</sup>

Staff similarly misconstrues WOWSC's financial records and proclaims that Staff's rates "would allow Windermere to maintain its financial integrity while also allowing it to pay what it owes."<sup>136</sup> It further states that WOWSC "has cried financial ruin" and "brought on the financial vapors."<sup>137</sup> Staff chooses to patronize WOWSC's volunteer board of directors rather than adequately review the Corporation's financial records. Specifically, it relies on WOWSC's "profit of \$41,158.66" that the Corporation realized "even at its pre-increase rates."<sup>138</sup> Due to this alleged profit, the Corporation "never needed to raise its rates to pay external legal expenses."<sup>139</sup> Importantly, however, WOWSC received a \$59,855.84 insurance settlement in 2019.<sup>140</sup> As such, the "profit" Staff relies on derived almost entirely from a one-time insurance payment and is therefore irrelevant for purposes of WOWSC's rates and required revenue. Excluding this one-time payment, with the pre-increase rates WOWSC's loss in 2019 was \$18,697.18. Importantly, this loss occurred before the Corporation recognized significant increases in legal expenses.<sup>141</sup> Thus, the appealed rates were, and still are, necessary for WOWSC to provide water and wastewater services to its members.

Nevertheless, despite WOWSC's additional loan requirements, customer growth, and required infrastructure improvements, Staff recommends rates lower than the rates effective *before* WOWSC's March 2020 rate change.<sup>142</sup> As discussed in WOWSC's Initial Brief, to fund necessary capital expenditures, the Corporation entered into a credit agreement with CoBank in September 2020 that requires WOWSC to maintain a Debt Service Coverage Ratio (DSCR) of 1.25 to 1.00.<sup>143</sup>

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<sup>134</sup> *Id.* at 5-10.

<sup>135</sup> TWC § 13.043(j); Remand Order; Prehearing Conference Tr. at 12:21-13:7 (ALJ Siano) (Mar. 21, 2023).

<sup>136</sup> Staff's Initial Brief at 2.

<sup>137</sup> *Id.* at 2, 9.

<sup>138</sup> *Id.* at 9.

<sup>139</sup> *Id.*

<sup>140</sup> Ratepayers HoM2 Exhibit 133, WOWSC's Response to Ratepayers 8-27D, 2019 Year End Financials - Balance Sheet & Profit and Lost Performance at Bates 3 (see "Line Item 4200 – Insurance Claim Settlements").

<sup>141</sup> *Id.*

<sup>142</sup> Staff HoM2 Ex. 1, Supplemental Direct Testimony of Stephen J. Mendoza at 4:14-26, 5:10-13.

<sup>143</sup> WOWSC Ex. 26 at Bates 5:3-9; WOWSC Ex. 27, Attachment MN-13 at p. 11 of 19 (Bates 118), p. 18

Moreover, the WOWSC subdivision currently adds roughly six houses each year, and has 130 vacant lots and forty additional hangars that could soon be developed.<sup>144</sup> Finally, WOWSC must expand its Sewer Plant, soon replace its raw water pumps, and soon replace its clarifier system.<sup>145</sup> As such, legal expenses aside, it is unclear how Staff expects WOWSC to maintain its credit, fund necessary expansion, and issue refunds with rates *lower* than the rates effective prior to the appealed rates.

Staff's proposed rates applied to WOWSC billing data that incorporates the Corporation's necessary legal payments<sup>146</sup> have the following financial impact: (1) after 11 months, WOWSC would have no funds to meet its loan covenant reserves; (2) after 12 months, WOWSC would exhaust its checking and money market account balances and, therefore, be incapable of paying its bills; and (3) after 12 months, WOWSC would not meet its loan covenant's DSCR.<sup>147</sup> Staff's proposed rates *and* recommended refund would have the following impacts: (1) after six months, WOWSC would have no funds to meet its loan covenant reserves; (2) after seven months, WOWSC would exhaust its checking and money market account balances; and (3) after 12 months, WOWSC would not meet its loan covenants' DSCR.<sup>148</sup> Moreover, these analyses assume that WOWSC receives all standby and late fees in the first month of the year, WOWSC has no capital expenditures throughout the year, and WOWSC has complete access to its account balance and standby and late fees.<sup>149</sup> As such, the analyses represent ideal outcomes and, under realistic conditions, WOWSC's default timeline would accelerate.<sup>150</sup>

In short, Staff's proposed rates would financially destroy WOWSC. Within a year, WOWSC's loans would become immediately payable, likely leading to a quick sale of WOWSC property vital to the Corporation's operations.<sup>151</sup> WOWSC would violate its CoBank loan

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of 19 (Bates 125).

<sup>144</sup> WOWSC Ex. 26 at Bates 6:11-14.

<sup>145</sup> *Id.* at Bates 6:15-7:3.

<sup>146</sup> WOWSC Ex. 27, Attachment MN-12 at p. 5 of 91 (Bates 21).

<sup>147</sup> *Id.* at Bates 8:5-14; Attachment MN-11.

<sup>148</sup> *Id.* at Bates 9:9-18, Attachment MN-14.

<sup>149</sup> *Id.* at Bates 8:15-9:3, Bates 9:18-10:2.

<sup>150</sup> *Id.*

<sup>151</sup> *Id.* at Bates 10:16-20.

covenant's DSCR and, therefore, fail to secure new loans for capital improvements.<sup>152</sup> And it would default on its legal bills, subjecting itself to increased legal liability.<sup>153</sup> Thus, Staff's proposals would inevitably lead WOWSC to bankruptcy or receivership and, ultimately, impact WOWSC customers' ability to receive water and wastewater services. Therefore, Staff's proposed rates and refund must be denied.

**1. *Town of Woodloch* does not apply.**

Both Ratepayers and Staff rely on *Town of Woodloch* and, specifically, the conclusion that "[c]onsiderations of financial integrity cannot...be treated as a trump card that overrides the utility's obligation to comply with the standard requirements for proving its water and sewer rates."<sup>154</sup> Accordingly, Ratepayers and Staff assert that TWC § 13.043 does not require the Commission to set rates that preserve the financial integrity of the utility.<sup>155</sup> But importantly, the Commission reached this conclusion due to the Town of Woodloch's (Town) inclusion of discretionary operation and maintenance expenses that the administrative law judge (ALJ) ultimately found improper.<sup>156</sup> Specifically, the Town included in its revenue requirement expenses that it likely already collected through a surcharge.<sup>157</sup> As such, according to the ALJ, the Town included unreasonable and unproven expenses in its revenue requirement and, therefore, the proposed rates' impact on the Town's financial integrity was not dispositive.<sup>158</sup>

In contrast to the Town, Windermere did not include any discretionary and extraneous expenses in its revenue requirement. Rather, the primary revenue requirement expenses at issue are the 2019 legal fees.<sup>159</sup> As explained above, these expenses were not discretionary but were

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<sup>152</sup> *Id.* at Bates 10:20-21.

<sup>153</sup> *Id.* at Bates 10:3-10.

<sup>154</sup> Staff's Initial Brief at 4; Ratepayers' Initial Brief at 23; *see also Appeal of Water and Sewer Rates Charged by the Town of Woodloch CCN Nos. 12312 and 20141*, Docket No. 42862, Order at Conclusion of Law 13 (Mar. 7, 2016).

<sup>155</sup> Ratepayers' Initial Brief at 22-23; Staff's Initial Brief at 4.

<sup>156</sup> *Appeal of Water and Sewer Rates Charged by the Town of Woodloch CCN Nos. 12312 and 20141*, Docket No. 42862, Proposal for Decision at 9- 10, 22-23 (Oct. 29, 2015).

<sup>157</sup> *Id.* at 9-10.

<sup>158</sup> *Id.* at 22-23.

<sup>159</sup> Staff Ex. 4 at 12; Tr. at 844:21-24 (Givens Cross) (Mar. 22, 2023); *see also* Prehearing Conference Tr. at 21:16-17 (ALJ Siano) (Mar. 21, 2023) (granting Commission Staff's motion to adopt Maxine Gilford's testimony).

necessary costs of service. It is therefore imperative that the Commission recognize the proposed rates' detrimental impact on WOWSC's financial integrity.

**2. Ratepayers' scattered allegations regarding the WOWSC Board's mismanagement are unfounded, irrelevant, and should be dismissed.**

First, Ratepayers claims that WOWSC's rates allow the Corporation to recover revenue "beyond the reasonable needs of its business" and, therefore, the rates are inconsistent with Internal Revenue Code (IRC) § 501(c)(2) and the Corporation's bylaws.<sup>160</sup> Ratepayers fail to mention that outside legal fees are a recognized cost of providing water and sewer service and are categorized as such under the NARUC system of accounts.<sup>161</sup> Therefore, as a 501(c)(2) corporation, WOWSC was well within its rights to allocate revenue to legal representation for the benefit of the Corporation and its ratepayers. Moreover, Ratepayers fails to cite to anything in the record that demonstrates WOWSC's alleged over-recovery of revenue.<sup>162</sup> Most importantly, however, Ratepayers federal tax related claims are far outside the scope of this rate appeal.<sup>163</sup> They should therefore be dismissed.

Ratepayers subsequently cobbles together various financial documents and emails to mischaracterize the WOWSC Board's financial management. Specifically, it fabricates CoBank reporting requirements and misconstrues the Corporation's general ledger. It implies that because WOWSC failed to disclose its \$121,000 legal liability "anywhere on its financials or tax filings," the records failed to accurately reflect the Corporation's operations.<sup>164</sup> Importantly, however, Ratepayers fails to cite to any law or CoBank credit agreement provision that requires WOWSC to report its legal liability.<sup>165</sup> Nevertheless, the Corporation disclosed its legal liability, in accordance with CoBank's credit agreement,<sup>166</sup> in writing to CoBank representative John Deluca.<sup>167</sup> Further, without any citation to the record, Ratepayers alleges that WOWSC was

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<sup>160</sup> Ratepayers' Initial Brief at 6, 8.

<sup>161</sup> Tr. 845:6-17, 847:10-20 (Givens Cross) (Mar. 22, 2023).

<sup>162</sup> Ratepayers' Initial Brief at 8.

<sup>163</sup> TWC § 13.043(j); Remand Order; Prehearing Conference Tr. at 12:21-13:7 (ALJ Siano) (Mar. 21, 2023).

<sup>164</sup> Ratepayers Initial Brief at 23-24.

<sup>165</sup> *Id.*

<sup>166</sup> WOWSC Ex. 27 at 5 (Section 4.7 requires that "the Borrower is not aware of any Material Adverse Change that has not been *disclosed in writing* to Lender") (emphasis added).

<sup>167</sup> WOWSC Ex. 44 OC, Confidential – WOWSC's Response to Ratepayers' RF1 8-7 at 385 (Bates 387)



insolvent at the end of 2019.<sup>168</sup> However, it fails to define “insolvent” and, importantly, WOWSC’s financial records show that in 2019 the Corporation’s assets exceeded liabilities.<sup>169</sup> Moreover, Ratepayers claims that WOWSC failed to inform CoBank of the Corporation’s payment agreements with outside legal counsel and “misled” CoBank about WOWSC’s legal debt.<sup>170</sup> But WOWSC informed CoBank of its minimum payment plans and legal liabilities in writing.<sup>171</sup> The Corporation continued to provide updates to CoBank regarding the underlying lawsuits as they proceeded.<sup>172</sup>

Finally, Ratepayers asserts that WOWSC “comingled” CoBank funds and, therefore, improperly devoted loan proceeds to legal fees.<sup>173</sup> It subsequently states that “[i]t is undisputed that CoBank prohibited [WOWSC] from using loan proceeds to pay legal costs” but, again, fails to support this assertion with any citation to the record. Nevertheless, because the Corporation “transferred only \$259,000 of the \$300,000 [CoBank loan] to the ‘MM’ account” in January 2022 and, “[s]ince that time, there have been... numerous legal payments,” Ratepayers accuses WOWSC of allocating CoBank loan proceeds to pay the Corporation’s legal expenses.<sup>174</sup> Importantly, however, WOWSC wrote a check to “Superior Tank Company, Inc.,” a corporation that supplies clarifier tanks, on January 24, 2022, for \$40,583.75.<sup>175</sup> As such, in contrast to Ratepayers’ accusation, WOWSC allocated the remaining loan proceeds to pay for a clarifier tank in accordance with its CoBank loan promissory note.<sup>176</sup> Ratepayers’ theory must therefore be rejected.

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(informing CoBank in May 2020 that the Corporation “is currently...in arrears to our legal firms for \$110,000); *see also* WOWSC Ex. 44 OC at 343 (Bates 345).

<sup>168</sup> *Id.* at 24.

<sup>169</sup> Ratepayers HoM 2 Ex. 133 (Bate stamped as Ratepayers HoM2 Exhibit 132) at Bates 1.

<sup>170</sup> *Id.* at 19.

<sup>171</sup> WOWSC Ex. 44 OC at 385 (Bates 387).

<sup>172</sup> WOWSC Ex. 44 OC at 3034 (Bates 3036), 3410 (Bates 3412).

<sup>173</sup> Ratepayers’ Initial Brief at 24.

<sup>174</sup> *Id.*

<sup>175</sup> WOWSC Ex. 38 OC, Confidential – WOWSC’s Response to Ratepayers RF1 8-24 at 213 (Bates 215).

<sup>176</sup> WOWSC Ex. 3 at Attachment JG-19 at 12 (providing that “[t]he purpose of the Commitment is to provide financing for a new clarifier/pre-treatment tank and UV treatment equipment”)

In sum, Ratepayers' various allegations related to WOWSC's financial management are unsupported by the record. And again, they are entirely irrelevant and beyond the scope of this rate appeal. They should therefore be dismissed.

### **3. Staff's alternate revenue streams are inadequate.**

Staff offers several alternate revenue streams available to WOWSC for purposes of its legal liability. The revenue sources are wholly inadequate to recover WOWSC's legal costs. Several sources, as discussed below, are still subject to judicial review and may never materialize.<sup>177</sup> Thus, in contrast to Staff's position, for the foreseeable future there is not "more than one way to skin a cat."<sup>178</sup> Rather, WOWSC's financial integrity depends solely on recovery of the underlying legal fees through the appealed rates or a surcharge.

Staff first suggests that the Corporation devotes its equity buy-in fees towards its legal liability.<sup>179</sup> However, the Corporation only receives revenue through equity-buy in fees when a customer requires a new service tap.<sup>180</sup> As such, equity-buy in revenue is inconsistent and unreliable. For example, in 2015 the Corporation received \$8,000 in equity-buy in fees and, in 2019, received \$50,600.<sup>181</sup> To recover its legal fees, the Corporation requires a more reliable, steady source of revenue such as rates or a surcharge.

Staff then recommends that the Corporation satisfy its legal liability with the Allied settlement, Dana Martin's indemnification costs, and *Double F Hanger* Lawsuit damages.<sup>182</sup> Importantly, however, this revenue is still subject to judicial review. Although the United States District Court of the Western District of Texas ruled in favor of WOWSC and held that Allied owes the Corporation for defense costs related to the *Double F Hanger* Lawsuit, Allied appealed the court's ruling.<sup>183</sup> It is therefore unclear exactly when WOWSC will recover the 2019 insurance settlement proceeds.<sup>184</sup> Moreover, pursuant to Dana Martin's indemnification agreement,

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<sup>177</sup> See also WOWSC Ex. 26 at Bates 11:16-12:9, Bates 13:1-19.

<sup>178</sup> Staff's Initial Brief at 2.

<sup>179</sup> *Id.* at 10.

<sup>180</sup> WOWSC Ex. 2, Voluminous Attachment to WOWSC Ex. 2 at 42.

<sup>181</sup> Staff HoM2 Ex. 48, WOWSC's Response to Staff's RF1 8-4 at Bates 1.

<sup>182</sup> Staff's Initial Brief at 10.

<sup>183</sup> WOWSC Ex. 2 at Bates 12:10-20, 12:1-4; Attachment JG-48.

<sup>184</sup> *Id.* at Bates 13:1-4.

WOWSC may only seek repayment of her defense costs in the *Double F Hangar* Lawsuit after a court makes a “final determination.”<sup>185</sup> Because the plaintiffs indicated they will seek an appeal, it is unclear when the Corporation will ultimately recover Ms. Martin’s legal fees.<sup>186</sup> WOWSC’s recovery of the *Double F Hangar* damages is, similarly, subject to plaintiffs’ appeal. Therefore, this revenue is unreliable and may never materialize.

Staff then goes so far to suggest that WOWSC should sell “assets that are not being used in the provision of service,” “its land,” or “sell itself to another functioning utility.”<sup>187</sup> It is hard to fathom how Staff could consider WOWSC’s financial integrity and simultaneously suggest that WOWSC sell valuable land or even itself to another entity. In fact, Staff witness failed to identify another instance where, in a rate appeal, the Commission suggested that a utility sell land—or even itself—to pay its cost of service.<sup>188</sup> Moreover, as a non-profit water supply corporation, the only assets WOWSC owns it uses “in furtherance of the legitimate business of a water supply cooperative.”<sup>189</sup> It therefore has no excess assets to sell.

Commission Staff’s alternate revenue streams are insufficient and, most importantly, not guaranteed. WOWSC’s financial integrity therefore depends on recovery of the appealed rates or a surcharge. As such, Commission Staff’s alternate revenue stream suggestions should be dismissed. Importantly, WOWSC has provided that after it pays its legal debt in full, it will immediately reduce its base rates.<sup>190</sup>

#### **D. Surcharge or Assessment**

Staff suggests that if its suggested alternate revenue streams are insufficient, the Corporation could recover the underlying legal fees through an assessment or a surcharge.<sup>191</sup> Moreover, WOWSC will soon adopt a resolution to amend its tariff to allow for a surcharge to

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<sup>185</sup> WOWSC Ex. 26 at Bates 136.

<sup>186</sup> *Id.* at Bates 12:7-9.

<sup>187</sup> Staff’s Initial Brief at 8; WOWSC Ex. 27, Attachment MN-10.

<sup>188</sup> Tr. at 866:7-24 (Givens Cross) (Mar. 22, 2023).

<sup>189</sup> WOWSC Ex. 2, Attachment JG-2 at p. 2 of 22 (Bates 28).

<sup>190</sup> *Id.* at Bates 13:20-14:3; *see also* WOWSC Ex. 3, Attachment JG-39 at p. 4 of 6 (Bates 396).

<sup>191</sup> Tr. at 857:12-19 (Givens Cross) (Mar. 22, 2023); WOWSC Ex. 27, Attachment MN-8, (Commission Staff witness Anna Givens adopting Commission Staff witness Maxine Gilford’s testimony that WOWSC could recover rate case expenses through a surcharge); *see also* Staff’s Initial Brief at 8.

recover its legal expenses.<sup>192</sup> Ratepayers, without any legal citation, asserts that “[t]he only authority for the Commission to impose a surcharge is found in 13.043(e).”<sup>193</sup> However, the Commission substantive rule § 24.25 provides that “[i]f authorized by the commission...a surcharge to recover the actual increase in costs to the utility may be collected...for any purpose noted in the [Commission] order approving the surcharge.”<sup>194</sup> Ratepayers’ statement, therefore, is a blatant misstatement of law and should be dismissed.

If the Commission adopts Staff’s recommended rates and moves the underlying legal fees into a surcharge or assessment, the Corporation could maintain its financial integrity and continue to provide continuous and adequate service.<sup>195</sup> Thus, this recommendation appropriately considers WOWSC’s financial integrity in accordance with TWC § 13.043(j).<sup>196</sup> As such, WOWSC requests that, if the Commission ultimately adopts Staff’s rates, the Commission also authorize a surcharge or assessment for the Corporation to recover its underlying legal fees.

#### **E. Staff’s Recommended Rate Design**

Staff also recommends a different rate design that lowers WOWSC’s base rates and raises WOWSC’s volumetric rates.<sup>197</sup> To support this recommendation, it merely provides that “[t]he entirety of non-recurring expenses should not be recovered through base rates.”<sup>198</sup> Importantly, it does not provide any legal support for this opinion.<sup>199</sup> As discussed in WOWSC’s Initial Brief, however, this rate design is unsuitable for WOWSC’s service area due to the nature of the Corporation’s members. Specifically, many WOWSC connections are with second home and hangar owners and, as such, a significant number of customers use minimal water and pay minimal

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<sup>192</sup> WOWSC Ex. 26 at Bates 14:4-15.

<sup>193</sup> Ratepayers’ Initial Brief at 26.

<sup>194</sup> 16 TAC § 24.25(a)(2)(G).

<sup>195</sup> WOWSC Ex. 27 at Bates 5:8-16.

<sup>196</sup> TWC § 13.043(j).

<sup>197</sup> Staff HoM2 Ex. 1 at 4:13-26; WOWSC Ex. 26 at Bates 15:5-15.

<sup>198</sup> Staff’s Initial Brief at 8.

<sup>199</sup> *Id.*

volumetric rates.<sup>200</sup> Accordingly, under Staff's proposed rate design, permanent residences effectively subsidize temporary residents with higher volumetric rates.<sup>201</sup>

The volumetric and base rate ratio is a policy decision best left to the locally elected WOWSC Board of Directors. The Board decided that, based on WOWSC's customer base, higher base rates establish a more equitable rate design that ensures all residents, whether permanent or temporary, fund the system that stands ready to serve them. It is inappropriate for the Commission to substitute its judgment for the policy preferences of the elected board. The Commission should therefore reject Staff's proposed rate design and allow the Corporation to continue collecting rates in accordance with the rate design effective March 2020.

#### **IV. STAFF'S RECOMMENDED COMPLIANCE FILINGS**

Staff recommends that the Commission order the Corporation to submit "compliance filings...that would allow the Commission to track [WOWSC's] financial progress."<sup>202</sup> It bases this recommendation on the premise that WOWSC's legal liability was "not prudently incurred" and, moreover, that the Corporation has failed "to maintain and provide clear and accurate records."<sup>203</sup> However, as discussed above, WOWSC's legal fees were not discretionary; rather, they were required. Moreover, because Staff fails to cite to any WOWSC records, it is unclear what records Staff refers to.<sup>204</sup> In fact, WOWSC has gone so far to provide Ratepayers and Staff with its general ledger and the general ledger's supporting documentation.<sup>205</sup> There is nothing in the record to suggest that these records are inaccurate. Staff's recommendation, therefore, is arbitrary and without basis.

Moreover, it would impose an unnecessary administrative burden on a volunteer board of directors and waste Commission resources. As discussed above, the underlying lawsuits will soon conclude and, therefore, the Corporation will soon stop incurring legal fees. Moreover, the Corporation has already entered a minimum payment plan with its outside counsel and has paid its

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<sup>200</sup> WOWSC Ex. 26 at Bates 15:16-20.

<sup>201</sup> *Id.* at Bates 15:21-22.

<sup>202</sup> Staff's Initial Brief at 2-3.

<sup>203</sup> *Id.*

<sup>204</sup> *Id.*

<sup>205</sup> WOWSC Ex. 38 OC.

legal fees in accordance with this agreement.<sup>206</sup> There is therefore nothing more for the Commission “to track.” As such, Staff’s recommendation should be denied.

## **V. RATE CASE EXPENSE RECOVERY**

Ratepayers argues that Staff witness Anna Givens’ testimony regarding WOWSC’s rate case expense recovery should be stricken because it was “surprise testimony” and it “establishes that [Ms. Givens] does not have experience to testify regarding expenses in a rate appeal under Section 13.043.”<sup>207</sup> But Ratepayers fails to cite to any legal support that entitles them to such broad relief.<sup>208</sup> Similarly, Ratepayers asserts that Jamie Mauldin’s testimony regarding rate case expenses should be stricken because “Ratepayers were not allowed to cross-examine Ms. Mauldin” regarding 16 TAC § 24.44.<sup>209</sup> Again, however, Ratepayers fails to provide any legal support for such broad, retroactive relief.<sup>210</sup> Finally, Ratepayers claims that WOWSC mischaracterized its revenue requirement and, as such, its request for any rate case expenses should be rejected.<sup>211</sup> It provides no legal support for this relief, but merely states that “Anna Givens admitted that it is not good public policy” to award rate case expenses under these circumstances.<sup>212</sup> It provided no citation to the record demonstrating that Ms. Givens stated this.<sup>213</sup>

Nevertheless, as discussed above, WOWSC has consistently maintained that to establish the appealed rates it relied on the TRWA Model, which computed a \$576,192 revenue requirement using 2019 financials, and subsequently adjusted the TRWA-recommended rates to account for an increase in legal fees identified in the 2020 budget.<sup>214</sup> In fact, at the first hearing on the merits,

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<sup>206</sup> See, e.g., Ratepayers HOM2 Ex. 119 at Bates 1-6.

<sup>207</sup> Ratepayers’ Initial Brief at 26-27.

<sup>208</sup> *Id.*

<sup>209</sup> *Id.* at 27.

<sup>210</sup> *Id.*

<sup>211</sup> *Id.* at 28-29.

<sup>212</sup> *Id.* at 29.

<sup>213</sup> *Id.*

<sup>214</sup> See WOWSC Ex. 36 OC at Bates 2 (stating that “[t]he TRWA spreadsheet generated the calculated base rates at roughly \$175. The Board used the financial data and determined that, to add to the previous year’s legal fee budget of roughly \$3,150 per month and to satisfy its obligations to law firms that totaled \$20,000 per month (\$250,000 in the year 2020), it required an extra \$16,000 per month. Thus, because the Board could collect \$16,000 per month with a rate lower than \$175, it reduced the base rate to reflect the amount needed for ongoing legal fees.”); Tr. at 199:1-11 (Nelson Cross) (Dec. 1, 2021) (providing that “the concept was to look at 2019, right, use it in a rate study to understand how high we could increase rates and then see if we could meet the \$10,000 a month per law firm [in

WOWSC witness Mike Nelson expressly stated to Ratepayers' attorney Kathryn Allen that "the concept was to look at 2019, right, use it in a rate study to understand how high we could increase rates and then see if we could meet the \$10,000 a month per law firm. And so that's where we're able to do that...at a lower amount than the TRWA analysis."<sup>215</sup> Ms. Allen subsequently asked "[s]o, you designed these rates to enable you to meet a budget of 10,000 a month per law firm going forward?"<sup>216</sup> Mr. Nelson responded "[y]ep."<sup>217</sup> Therefore, in contrast to Ratepayers' assertions, WOWSC expressly stated to Ratepayers' counsel on December 1, 2021, that it used the TRWA revenue requirement and incorporated its 2020 legal budget. Ratepayers' "public policy" allegations should therefore be dismissed.

Staff recommends that the Corporation recover \$379,000 in rate case expenses.<sup>218</sup> It further recommends that the Commission evaluate "any expenses incurred after January 31, 2022."<sup>219</sup> Finally, Staff suggests that Windermere recover its rate-case expenses through a surcharge over five years.<sup>220</sup>

As discussed in WOWSC's Initial Brief, however, the Corporation has incurred significant additional rate case expenses due to the Remand Order. As such, WOWSC requests that the Commission allow the Corporation to recover \$478,184.04 in reasonable and necessary legal and consultant rate case expenses.<sup>221</sup> This total includes \$85,662 of legal expenses incurred from May 23, 2022, through January 31, 2023.<sup>222</sup> Moreover, WOWSC requests that the Commission allow

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the 2020 budget[]"); Tr. at 199:8-11 (WOWSC answering "[y]ep" after questioned whether WOWSC "designed these rates to enable you to meet a budget of 10,000 a month per law firm going forward"); WOWSC Ex. 7 at Bates 9:4-7 (Nelson Direct) (providing that "WOWSC's 2020 budget estimated a net loss of \$174,515 primarily by estimated legal costs of \$250,000.... In order to defend itself in these various lawsuits, WOWSC needed to increase rates in order to be able to continue providing safe and adequate water and sewer service while also paying the necessary legal fees associated with ongoing litigation"); Ratepayers Ex. 12 at Bates 36 (WOWSC stating that "[t]he 2020 Budget shows that without the rate increase, WOWSC projected a \$174,515.00 loss").

<sup>215</sup> Tr. at 199:1-5 (Nelson Cross) (Dec. 1, 2021).

<sup>216</sup> Tr. at 199:8-10 (Nelson Cross) (Dec. 1, 2021).

<sup>217</sup> Tr. at 199:11 (Nelson Cross) (Dec. 1, 2021).

<sup>218</sup> Staff's Initial Brief at 10.

<sup>219</sup> *Id.* at 12.

<sup>220</sup> *Id.*

<sup>221</sup> WOWSC Ex. 28, Fifth Supplemental Direct Testimony of Jamie L. Mauldin at Bates 4:21-5:1. At hearing, Staff Witness Anna Givens stated that Commission Staff recommends that the Commission allow WOWSC \$379,000 in rate case expenses. Tr. at 864:10-18 (Givens Cross) (Mar. 22, 2023).

<sup>222</sup> WOWSC Ex. 28 at Bates 6:18-19.

the Corporation to update its rate case expenses after the close of the record and request a recovery of trailing expenses in a compliance proceeding where its residual rate case expenses can be reviewed.<sup>223</sup> Finally, the Corporation requests a surcharge over a 42 month period to recover the \$478,184.04, plus trailing rate case expenses.<sup>224</sup> The amount requested is reasonable given the complexity of this case and comparable to the rate case expenses awarded in other rate appeals.<sup>225</sup>

## VI. CONCLUSION

For the foregoing reasons, WOWSC respectfully requests that the Commission deny Ratepayers' appeal, maintain the rates approved effective March 23, 2020, and grant WOWSC such other relief to which it may be entitled. In the alternative, WOWSC respectfully requests that the Commission allow WOWSC to recover the underlying legal fees through a surcharge<sup>226</sup> or assessment.

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<sup>223</sup> Staff Ex. 4 at 7:21-24, 8:1-24, 9:1-20; *see also* Prehearing Conference Tr. at 21:16-17 (ALJ Siano) (Mar. 21, 2023).

<sup>224</sup> *Ratepayers Appeal of the Decision by Windermere Oaks Water Supply Corporation to Change Water and Sewer Rates*, Docket No. 50788, Proposal for Decision at 13 (Mar. 31, 2022) (recommending that WOWSC recover rate case expenses through a surcharge over a 42-month period); *see also* Tr. at 857:12-19 (Givens Cross) (Mar. 22, 2023); WOWSC Ex. 27, Attachment MN-8, (Commission Staff witness Anna Givens adopting Commission Staff witness Maxine Gilford's testimony that WOWSC could recover rate case expenses through a surcharge); WOWSC Ex. 26 at Bates 14:4-15 (providing that WOWSC will soon amend its tariff to allow for a surcharge).

<sup>225</sup> *Ratepayers Appeal of the Decision by Bear Creek Special Utility District to Change Rates*, Docket No. 49351, Order on Rehearing at 3, Findings of Fact No. 56 (Nov. 19, 2021) awarding \$409k in rate case expenses.

<sup>226</sup> In WOWSC's Initial Brief, the Corporation requested that the Commission, if it adopts Staff's proposed rates, authorize WOWSC to recover the \$171,337 of outside legal fees through a surcharge. WOWSC's Initial Brief at 3, 14. To further clarify, if the Commission adopts Staff's proposed rates, WOWSC requests an *annual* surcharge of \$171,337 until it pays its legal debt in full.



Respectfully submitted,

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**ATTORNEYS FOR WINDERMERE OAKS  
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**CERTIFICATE OF SERVICE**

I certify that, unless otherwise ordered by the presiding officer, notice of the filing of this document was provided to all parties of record via electronic mail on May 2, 2023, in accordance with the Order Suspending Rules, issued in Project No. 50664.



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JAMIE L. MAULDIN

Statement	Citation	Footnote	Authority	Issue
Windermere has suggested the Commission must create an exception for the rates of a retail public utility organized as a nonprofit corporation with members. For example, Windermere claims that all expenditures its board chooses to authorize are necessarily "just and reasonable", even those that have nothing to do with providing service. Windermere urges the Commission to arbitrarily single out the ratepayers of a nonprofit corporation retail public utility for different, and (according to Windermere) less favorable, treatment regarding rates than the similarly situated customers of other types of retail public utilities.	Pages 4-5	N/A	N/A	No citation to the record.
This contract determines the amount of revenue Windermere has authorized to collect from its ratepayers and the purposes for which such revenue may be disbursed.	Page 5	N/A	N/A	No citation to the record.
An L.R.C. 501(c)(12) organization exists for the sole purpose of providing services to its members at the lowest possible costs.	Page 6	FN 13	<i>Puget Sound Plywood v. Commissioner</i> , 44 T.C. 305, 307-08 (1965); see also TWC 67.002	Neither the case or the statute cited broadly provides that the "sole" purpose of a cooperative organization is to provide services to its members "at the lowest possible costs."
Windermere's appealed rates were intended to and do collect revenues to pay outside legal costs that are not costs to provide water or sewer services or a reasonable reserve for systems maintenance or replacements.	Page 8	FN 33	N/A. Ratepayers provides further unsupported assertions in FN 33.	No citation to the record.
The additional revenue generated by the appealed rates has not paid costs of service but has been used to make payments towards the corporation's undisclosed but ever-increasing legal debt. Neither Windermere's legal expenditures nor the rate increase implemented to fund them was approved by Windermere's board as the contract requires	Page 8	N/A	N/A	No citation to the record.

Statement	Citation	Footnote	Authority	Issue
To make matters worse, Windermere now claims it intends to levy some sort of additional charge on its ratepayers to recover outside legal costs, including the costs related to this appeal proceeding.	Page 8	N/A	N/A	No citation to the record.
The appealed rates are a graphic example. They were approved by vote of a board with a clear and substantial pecuniary interest and have conferred on those directors and a few other members the exclusive benefit of more than a million dollars in legal services at corporate expense.	Page 9	N/A	N/A	No citation to the record.
Windermere supports the opinion that the tariff does not require applicants to disclose on any application for service identification as to what type of customer defines their classification such as single-family residence, commercial, industrial or irrigation even though their tariff states otherwise.	Page 11	N/A	N/A	No citation to the record.
Whether Windermere gathers this data clearly a variety of characteristics [sic] among ratepayers do exist.	Page 11	N/A	N/A	No citation to the record demonstrating a variety of customer characteristics.
However, he overlooks characteristics of the purported one class of customers such as the commercial customers, residential customers, irrigation customers and customers who share service.	Page 12	N/A	N/A	No citation to the record demonstrating multiple customer classes.
Mr. Rabon clearly is unaware that Windermere encompasses several subdivision which all have unique characteristics identified as commercial ratepayers, residential ratepayers, irrigation properties, and multiple users to one tap.	Page 12	N/A	N/A	No citation to the record.
Not even Windermere's representatives have suggested that Windermere's outside legal costs have anything to do with providing water or wastewater service.	Page 13	N/A	N/A	No citation to the record. Rather, this entire proceeding has focused on WOWSC's request to recover outside legal costs as a cost of service.

Statement	Citation	Footnote	Authority	Issue
The common thread from one version to the next, however, is the intention to recover Windermere's costs for outside legal service in lawsuits and other matters arising from the 2016 land sale to then director Dana Martin. For years, Windermere's nonlawyer hearing representatives suggested that the corporation had substantial exposure with these matters. They hinted that the corporation's very existence might be at stake. They claimed the board was justified in spending hundreds of thousands of dollars in corporate funds and credit in connection with these matters.	Page 14	N/A	N/A	No citation to the record.
Even the meager evidence the ALJs allowed into the record at the December 2020 hearing belied that claim. The evidence showed that no one had ever sought any recovery against the corporation in any of the lawsuits. To the contrary, both the TOMA Integrity plaintiff and the Double F plaintiffs sought to require Martin, an unfaithful corporate fiduciary, to return to the corporation the property she had misappropriated. In addition, the Double F plaintiffs sued a small group of current and former directors to recover damages for the benefit of the corporation. Neither Martin nor her entity Friendship Homes ever asserted a claim against the corporation. Well before the rate increase, both of them gave Windermere a full and final release extinguishing any potential exposure the company might have had.	Page 14	N/A	N/A	No citation to the record.
Windermere's consultant Grant Rabon demonstrated through a financial analysis in late 2020--many months after the rate increase-- that the board's management of legal costs for the TOMA Integrity litigation, the Double F litigation and the rate appeal had placed "significant financial strain" on the utility's financial condition.	Page 16	1/N 56	Ratepayers' Exhibit HOM2 135 at bates 2425	This page does not exist. Ratepayers' Amended Exhibit HOM2 135 begins at bates 2433.

Statement	Citation	Footnote	Authority	Issue
Mr. Rabon opined before the board approved the CoBank loans that as a result of these decisions, Windermere did not have the wherewithal to comply with comply with [sic] CoBank's DSCR loan covenant.	Page 16	FN 57	Ratepayers' Exhibit HOM2 135 at bates 2437	The record cited to does not discuss CoBank's DSCR requirements.
He did not know that Windermere carried forward from 2019 more than \$121,000 in legal debt it did not have the resources to pay. Windermere's board president told him it was a 'timing difference,' i.e., that the debt was paid in 2020.	Page 16	FN 60	Tr. at 630:13-631:13. Ratepayers' Exhibit HoM2 at 135 at bates	The transcript cited to does not speak to Mr. Rabon's knowledge. Rather, Mr. Rabon expressly stated "I don't know." Moreover, the footnote excluded page numbers. Finally, Ratepayers cites to nothing that shows WOWSC had \$121,000 in legal debt in 2019.
None of Windermere's financial reports disclosed that liability.	Page 16	FN 61	Tr. at 637:17-640:1.	Mr. Rabon merely stated that he was not a CPA and that he did not remember observing \$121,000 in unpaid legal fees in WOWSC's financials. This testimony is not a basis for the assertion that the \$121,000 of legal fees are in "none of Windermere's financial reports."
Mr. Rabon's proposed 2020 budget for 'Legal' of \$245,000 did not include the company's existing legal debt.	Page 16	FN 62	Ratepayers' Exhibit HoM2 135 at bates_	Incomplete citation.

Statement	Citation	Footnote	Authority	Issue
Further, these proceedings sought to recover land and damages from individual fiduciaries and to hand them over to the company, free of charge. A reasonable, prudent and properly motivated board might well have directed its lawyers that the company would take a neutral stance. Such a board would not have emptied the company's coffers and plunged it into undisclosed legal debt greater than its institutional debt. Such a board would not have obligated the company to expend unlimited funds and credit to furnish legal services to for the only parties who needed them: the individual directors who were accused of misconduct and had personal exposure for a potentially large amount of money. The company had no obligation to furnish these individuals with legal services. A majority of the board that decided it were motivated by self-interest; they were prohibited by Windermere's bylaws from even casting a vote. As Mr. Rabon's analysis made clear, the company did not have the resources to fund such a commitment. There was no source from which the company would be able to obtain reimbursement.	Page 17	N/A	N/A	No citation to the record.
Every dollar the company has spent has been devoted to preventing the company's recovery of its land from those who misappropriated it and to preventing the corporation's recovery of compensation from the individuals who precipitated the loss.	Page 18	FN 66	Testimony of Joe Gimenez, Transcript (Dec. 2, 2021), p. 297:17-23	Mr. Gimenez stated that the money spent in the Double L Hangar lawsuit was for this purpose. This is a portion of the underlying legal fees at issue rather than "every dollar." The underlying legal fees also relate to the <i>Paxton</i> Lawsuit, the <i>TOMA</i> Lawsuit, and this rate appeal.
The beneficiaries were the eight individual who were being sued personally and the individual who was at risk of losing the land if the plaintiffs prevailed.	Page 18	FN 67	Testimony of Joe Gimenez, T. at 758:2-759:3	The Corporation was also a named party in the lawsuit, as stated in Mr. Gimenez's cited testimony. See also WOWSC-44 OC at 355.
Windermere never told ColBank about any alleged "minimum payment" arrangement.	Page 19	N/A	N/A	This is a blatant misstatement of fact. See WOWSC-44 OC at 379.

Statement	Citation	Footnote	Authority	Issue
Windermere's board president misled the CoBank representative in May 2020 about the amount of Windermere's legal debt.	Page 19	FN 77	N/A	This is a blatant misstatement of fact. See WOWSC-44 OC at 379 (Mr. Gimenez stating to CoBank representative that "we currently are in arrears to our legal firms for \$110,000").
He allowed CoBank's representative to assume that "the rate increase is covering much of what's been invoiced," which was completely false.	Page 19	N/A	N/A	No citation to the record. WOWSC disclosed its legal fees, the fact that its legal fees were increasing, and its 2020 budgeted legal fees to CoBank. See WOWSC-44 OC at 388.
Staff adjusted Windermere's proposed revenue requirement to remove the disallowed legal costs and to account for actual "other revenue." Otherwise, however, Staff relied on the costs reflected in the TRWA rate sheet Windermere furnished as Attachment Staff 1-1.	Page 20	N/A	N/A	No citation to the record.
No one knows the components for that "absolute minimum" amount because Windermere never furnished any information regarding them. Windermere certainly has not proven that its revenue requirement should be \$674,905.	Page 21	FN 87	Tr. at 884:21-886:25.	WOWSC never asserted that its revenue requirement is \$674,905. Rather, WOWSC expressly stated that the \$674,905 "is not a revenue requirement and would not be appropriate for setting rates." See Ratepayers IIOM2 Ex. 138 at 1.
Windermere now sometimes claims its board did not use any revenue requirement to calculate the appealed rates, but just bumped up the base rates enough to generate approximately \$18,000 in additional monthly cash flow indefinitely.	Page 21	FN 88	Tr. at 881:7-23	The testimony cited is silent regarding WOWSC base rates and recovery of 18,000 in additional monthly cash flow. Moreover, it contains no admission by WOWSC that it did not use a revenue requirement.
After disallowance of the cost component for "Legal," the TRWA revenue requirement comprised of cost components pulled from Windermere's 2019-year end financials is the only cost data for which there is any evidence as to the "just and reasonable" standards.	Page 22	N/A	N/A	No citation to the record.
As Windermere has often reminded, it is not a public utility and the requirements of Section 13.183 do not apply.	Page 22	N/A	N/A	No citation to the record.

Statement	Citation	Footnote	Authority	Issue
In the exercise of its appellate jurisdiction, the Commission is not required to fix a utility's overall revenues at a level that will preserve the financial integrity of a utility.	Page 23	FN 99	Compare Section 13.043(j) with Section 13.183(a)(2)	Section 13.183(a)(2) provides that "in fixing the rates for water and sewer services, the regulatory authority <i>shall</i> fix its overall revenues at a level that will...preserve the financial integrity of the utility."  Section 13.043(j) provides that "[t]he utility commission <i>shall</i> use a methodology that preserve the financial integrity of the retail public utility."  Ratepayers statement is therefore a blatant misstatement of law.
Mr. Rabon's financial analysis shows that Windermere's financial woes are the direct result of its board's authorization for unlimited corporate legal spending.	Page 23	FN 102	Tr. 683:24-684:13	Here, Mr. Rabon did not provide that the Corporation's financial problems resulted from the litigation. Rather, Mr. Rabon merely stated that his report was a hypothetical regarding the Corporation's financial state if it had not been involved in the lawsuits. Later, he expressly stated that the report <i>did not</i> show that the "board's decisions about legal spending and handling the lawsuits were having a significant and detrimental effect on the financial health of the Company." Tr. 689:11-18.
As a result of the board's mismanagement, Windermere had more than \$121,000 in legal debt for 2019 that was not reported anywhere on its financials or tax filings and was not included in its 2020 budget.	Page 23	FN 104	Tr. 626:5-627:25; 638:7-639:3; 680:7-681:5.	Mr. Rabon stated that he did not know whether Windermere's unpaid balance of \$121,000 would be reflected somewhere in the Company's financial reporting. Mr. Rabon never stated, in any of the cited transcript, that WOWSC failed to report the \$121,000 legal liability.
The legal debt increased over the course of 2020 by \$264,592, for a total legal debt at year-end of \$386,211. Windermere paid less than half the costs it incurred for legal services rendered in 2020.	Pages 23-24	N/A	N/A	No citation to the record.
Windermere was insolvent at the end of 2019 but no one other than the board knew it.	Page 24	N/A	N/A	No citation to the record.



Statement	Citation	Footnote	Authority	Issue
It is undisputed that CoBank has prohibited Windermere from using loan proceeds to pay legal costs.	Page 24	N/A	N/A	No citation to the record.
This violated the loan covenants of the CoBank Credit Agreement.	Page 24	FN 106	Tr. at 658:12-664:4.	The transcript cited to shows that Mr. Rabon never stated that WOWSC's financial reporting violated CoBank's agreement, but rather provided that he was unsure and would need to consult with the Corporation's CPA.
It is undisputed that CoBank has prohibited Windermere from using loan proceeds to pay legal costs.	Page 24	N/A	N/A	No citation to the record.
To the contrary, the evidence shows that Windermere has used these funds to pay legal costs and operating expenses.	Page 25	N/A	N/A	No citation to the record.
TRWA advised in October 2020 that the TRWA rate sheet focuses on the cash needs of the system by looking "at the systems audit and gallons of water sold to the members for the year."	Page 25	N/A	N/A	No citation to the record.
Windermere's board knew it did not have a systems audit at the time of the rate increase and did not look at gallons of water sold. The board knew it did not add any "known adjustments" to the revenue requirement.	Page 25	FN 112	N/A	No citation to the record.
Based on its recent discovery updates, Windermere's board claims it also knew there was no way to keep the company afloat with the appealed rates.	Pages 25-26	FN 114	Ratepayers' Exhibit HoM2 138	The cited RFI response contains no assertion from WOWSC regarding the appealed rates. Rather, it expressly provides that the figures provided are "not appropriate for setting rates."

Statement	Citation	Footnote	Authority	Issue
The only authority for the Commission to impose a surcharge is found in 13.043(c).	Page 26	N/A	N/A	16 Tex. Admin. Code s 24.25(G) authorizes the Commission to authorize a utility to impose "a surcharge to recover revenues over and above the usual cost of service...for any purpose noted in the order approving the surcharge." Ratepayers' assertion is a blatant misstatement of law.
She was completely unaware of Windermere's recent supplements and amendments proposing an entirely new revenue requirement, a budgeted cost revenue requirement or no revenue requirement at all, depending on who is asked. She was completely unaware that Windermere's ratepayers could have had a professional cost of service study and fully-vetted rates in December 2020 for a "not to exceed" price of \$22,500.	Page 27	N/A	N/A	No citation to the record.
Even Staff Witness Anna Givens admitted that it is not good public policy or in the public interest to award case expenses in these circumstances.	Page 29	N/A	N/A	No citation to the record.