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

**RATEPAYERS' CONSOLIDATED REPLY TO THE EXCEPTIONS OF WOWSC
AND PUC STAFF TO THE PROPOSAL FOR DECISION**

August 10, 2023

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**RATEPAYERS’ CONSOLIDATED REPLY TO THE EXCEPTIONS OF WOWSC AND PUC
STAFF TO PROPOSAL FOR DECISION**

The Ratepayer Representatives (“Ratepayers”) of Windermere Oaks Water Supply Corporation (“Windermere”) file this CONSOLIDATED REPLY to address the more egregious inaccuracies and omissions reflected in the exceptions to the Proposal for Decision (“PFD”) filed by WOWSC and PUC Staff. In support thereof, Ratepayers show as follows:

I. INTRODUCTION (Responsive to Section I of Windermere’s Exceptions)

A. No Relationship Between the Appealed Rates and \$171,337 Paid for Outside Legal Services in 2019

Ratepayers are hard pressed to determine which is more astonishing: that Windermere “commends” the ALJs for their “extensive[] review [of] the \$171,337 in legal expenses”¹ that Windermere itself formally admits have nothing at all to do with the appealed rates, or that even now the ALJs seem not to have figured that out.

Ratepayers can understand how a casual observer not paying close attention might think the legal services for which Windermere reported having paid just over \$166,000 in 2019 could

¹ The PFD provides no indication that the ALJs actually reviewed the invoices reflecting the \$171,337 reported as being paid for legal services furnished in 2019. They most certainly did not engage in any “extensive review” of any of the matters for which the \$171,337 in legal services were provided; to the contrary, they excluded or unilaterally chose not to consider the pleadings, orders, judgments, and other objective and reliable evidence concerning these matters.

be relevant data points in this appeal. For virtually the duration of this appeal, Windermere sponsored the fictitious proposition that the appealed rates were determined by TRWA using a cash needs approach and a revenue requirement of \$576,192 (including \$171,337 for outside legal services) based on a cost-of-service study reflected by the TRWA rate sheet, Attachment Staff 1-1. For years, Windermere insisted the only data relevant to this appeal were its 2019-year end financials and the invoices reflecting the legal services for which Windermere paid in 2019. For years, Windermere successfully precluded even discovery of other data concerning the massive legal expenditures it made with revenue from the appealed rates. For years, Windermere actively concealed the even more massive legal debt with which its board had burdened its ratepayers to ensure that the individual defendants would have the benefit of unlimited outside legal services.

For years, Windermere's strategy in this appeal relied on deception, obfuscation and massive legal spending. When Windermere's fiction first began to collapse, Windermere stood its ground even more loudly and emphatically and firmly berated anyone who dared to take the utility to task for its lack of candor. That strategy had the other parties so busy chasing their tails and (as PUC Staff describes it) scratching their heads that it almost prevailed.

Ratepayers persevered against Windermere's well-funded and sophisticated legal machine to get to the truth behind Windermere's inconsistencies and just plain nonsense. As a result of their efforts, just before the March 2023 hearing Windermere finally admitted that the story it had sponsored for years was just not true, and that the appealed rates do not include \$171,337 in fees for outside legal services in 2019, whether paid or incurred, whether for services to defend the civil litigation or for any other purpose.²

² Ratepayers Ex. 148, Ratepayers Ex. 145 and

Windermere has yet to come to ground on a new story as to how its board set the appealed rates,³ but the utility has not suggested any version that involves the \$171,337 Windermere reported on its financials as having been paid for outside legal services in 2019.

These significant developments have been highlighted repeatedly in briefing,⁴ discovery motions⁵ and during the March 2023 hearing.⁶ It is hard to imagine the ALJs haven't noticed them. It is dishonest for Windermere now to pretend they never happened.

Even before Windermere admitted the truth, only one witness in this appeal claimed to have made an "extensive review" of the invoices reflecting \$171,337 in legal services paid for in 2019: PUC Staff witness Maxine Gilford. Based upon her review, confirmed by Windermere's acknowledgement that none of the time entries could be allocated to any given matter,⁷ Ms. Gilford concluded that Windermere had failed to prove either (i) what legal services (if any) were rendered for defense of the civil lawsuits or (ii) what portion (if any) of the \$171,337 was attributable to those services.

Although Windermere proffered "estimates" in this proceeding, there was no evidence that the "estimates" were (i) prepared by someone qualified to review and understand the invoice and time entries, (ii) prepared using a reliable methodology, or (iii) based on reliable data. Ms. Gilford,

³ During cross-examination during the March 2023 hearing, Windermere's representative was unable to reproduce the calculation or to identify the data Windermere now claims the board relied on to set the appealed rates. See, e.g., Nelson Cross-examination, Transcript (March 23, 2023) at p. 731.

⁴ See, e.g., Ratepayers Representatives Objections to Supplemental Testimony of Mike Nelson and Motion to Strike

⁵ *Id*

⁶ See, e.g., Staff Exhibit 4, MG-8 p. 1

⁷ Windermere identified a number of matters it claimed required the employment of counsel during this time. These included the TOMA lawsuit, the Double F lawsuit, the Paxton lawsuit, the settlement with Martin, the dispute with Allied Insurance, the PIA requests, director election issues, director recall efforts, and online postings by members-customers; only 2 involved defense of civil lawsuits. Lloyd Gosselink maintained only 4 files for Windermere matters; these were labeled "General Counsel," "TOMA Integrity Litigation," "WWTP Detention Decommissioning," and "PUC Rate Appeal," respectively. According to Windermere, time for all matters was recorded in one or another of these four files, without regard to the matter for which the work was actually done.

the only witness arguably qualified to opine as to such matters, determined that the “estimates” were not adequate to prove either the legal services or the costs paid (and certainly not the costs incurred) for defense of the civil lawsuits or any other given matter. Her testimony is unrebutted.

It became crystal clear during the March 2023 hearing that Windermere’s “estimates” were contrived for purposes of this appeal and conflict fatally with the utility’s financial reporting. Consultant Grant Rabon testified that he was engaged to generate a report intended to blame “the lawsuits” for Windermere’s financial deterioration. Rabon admitted on cross-examination, however, that it was not “the lawsuits,” but rather the board’s mismanagement of the legal spending, that had adversely impacted the utility.⁸ As one would expect, Rabon used the cost allocation reported in Windermere’s financials to prepare his report.⁹ Before the report was finalized, board president Joe Gimenez realized that Rabon’s numbers would alert the Ratepayers to the fact that the “estimates” provided under oath in this proceeding were material misrepresentations.¹⁰ With guidance from Windermere’s appeal counsel Jamie Mauldin, Gimenez insisted that Rabon change his report to obscure the deception.¹¹

No one conducted an “extensive review” of the data (if any) Windermere claims was the basis for its 2020 budgeted legal cost of \$250,000. This is because Windermere never claimed to have relied on budgeted costs and never produced any such data.¹² Indeed, Windermere’s representatives repeatedly admitted that they had no projection for 2020 legal costs and no basis

⁸ See Transcript at pp. 678-9; Ratepayers Exh. HOM2-135.

⁹ According to Rabon, Windermere’s 2019-year end financials reported \$159,172 in lawsuit related legal costs and \$7,410.65 in other legal costs.

¹⁰ Gimenez explained to Rabon that although he was taking the position in the community that the Double F plaintiffs were to blame for all of the outside legal fees, he knew that wasn’t true. See Ratepayers Exh. HOM2-135 at pp. 2450-2.

¹¹ See Ratepayers Exh. HOM2-135 at bates 2450-9.

¹² Cross-examination of Anna Givens, Transcript (March 23, 2023) at pp. 847-9.

upon which to formulate one.¹³ In prefiled testimony, Windermere called the 2020 budget a “guesstimate.”¹⁴

During the December 2021 hearing, Windermere’s representative claimed there was some alleged “minimum payment” arrangement with the law firms; however, there is no objective evidence any such arrangement was ever made.¹⁵ Windermere certainly never disclosed any such arrangement to its ratepayers, its lender or its financial consultant. There is no mention of any “payment plan” in the minutes of the board’s budget discussions. Nor did Windermere mention any alleged “minimum payment plan” in its testimony prefiled before the December 2021 hearing.

Perhaps more important for present purposes, it is clear Windermere’s board neither expected nor intended that a budget of \$250,000 would enable Windermere to pay its legal costs in full as they came due. Instead, it was a vehicle by which the director defendants could enjoy the benefit of unlimited legal services (and perhaps even accumulate a “war chest”¹⁶) while the corporation accrued unlimited legal debt, and that is exactly what happened. Windermere failed to disclose in its financial reports or otherwise the enormous legal debt the corporation incurred by failing to pay its legal costs in full as they came due. Both the accumulation of legal debt and the failure to disclose it in the financial reports breached the warranties and covenants in the CoBank loan agreement.¹⁷

¹³ See, e.g., Ratepayers HOM2-132 at bates 2229-30.

¹⁴ Nelson Direct Testimony at p. 7, lines 14-20, and p. 14, lines 3-7.

¹⁵ Director and secretary-treasurer Mike Nelson apparently completely forgot about the story of an alleged “minimum payment” arrangement. See Transcript (March 23, 2023) at pp. 728-9. There is no documentation reflecting any such arrangement or that such an arrangement was approved by Windermere’s board, and it conflicts directly with the terms of the written engagement agreements with the law firms.

¹⁶ See Ratepayers Exh. HOM2-150.

¹⁷ Grant Rabon discussed these warranties and covenants in cross examination. See Transcript (March 23, 2023) at pp. 638-40 & 659-74. Windermere now claims that a reduction in its rates or an order requiring refunds to customers would put the corporation in breach of the CoBank loan covenants. In fact, however, the board put Windermere in breach of the CoBank loan covenants almost immediately after the loan was made.

B. The Evidence Concerning Windermere's Financial Integrity and the Credibility of the Board's Promise to Lower Rates.

Ratepayers are similarly astonished by Windermere's assertion that "no party offered evidence" to rebut the "conclusion" that Staff's rates would financially destroy Windermere. That is not even Windermere's claim. Windermere's contention is that without the additional revenue generated by the appealed rates it will be unable to operate the utility, perform its obligations to its institutional lender *and* pay for unlimited legal services by outside counsel. The law does not afford Windermere such a guarantee.

Moreover, the evidence shows that Windermere's financial circumstances are largely the product of its board's mismanagement. The evidence shows that Windermere's board failed to take (or to engage a qualified expert to take) the steps required to ensure that its rate revenue, together with its other revenue, would be adequate to pay its actual costs of service (i.e., not its litigation-related expenses), to service its institutional debt and to fund a host of capital improvements its board has suddenly determined are "required by law."¹⁸ Windermere's board has acted in wholesale disregard for its tariff mandatory requirements that costs other than normal utility costs be paid by the person who receives the services for which the costs were incurred and that operating shortfalls be recovered through an assessment at the end of the year. Finally, despite Grant Rabon's report warning about the potential consequences of the board's unbridled legal spending, Windermere's board continued to approve the expenditure of hundreds of thousands of dollars' worth of corporate resources for the benefit of themselves and a handful of former directors in matters that could not materially impact the corporation even if it did not "prevail."

¹⁸ Ironically, in late 2020 consultant Grant Rabon proposed to perform a full cost of service study and to design proper rates for Windermere for a "not-to-exceed price of \$22,500." See Ratepayers Exh. HOM2-129.

To make matters worse, every financial report Windermere's board has furnished to CoBank is materially inaccurate, in that it fails to reflect the corporation's legal debt and it mischaracterizes the corporation's legal costs. This is a breach of the corporation's representations and warranties, as well as its loan covenants, under the CoBank credit agreement.

The financial consequences of board mismanagement, however, are not costs any retail public utility's ratepayers should be required to bear. The Commission cannot burden Windermere's ratepayers with these costs just because it has required them to become members and customers of a nonprofit water supply corporation with members, rather than some other form of retail public utility.

If all that were not enough, in June Windermere received a cash payment in the amount of \$687,812.05 from Allied Insurance to settle the controversy over coverage and the payment of defense costs for the civil suits the PFD asserts was known to the board at the time of the rate increase. This payment had not been received as of the time of the March 2023 hearing.

Promptly upon learning of the Allied settlement, Ratepayers moved to complete the record with the information concerning this cash payment. Such information is clearly relevant to Windermere's assertion that its financial integrity will somehow be jeopardized. As and to the extent the outcomes of Windermere's litigation matters bear on this appeal, the Allied result is relevant there as well.¹⁹

While asserting that Windermere will be plunged into financial disaster and that no party offered evidence to rebut this claim, Windermere inexplicably opposes the admission of this post-hearing cash payment. Windermere apparently claims that while its current and prospective future

¹⁹ These matters are fully discussed in Ratepayers' Motion to Reopen the Record and To Admit evidence filed on August 1, 2023. That Motion and its attachments are incorporated fully by this reference.

financial circumstances are relevant and within the scope of this appeal, evidence that Windermere has just received a substantial cash payment cannot be considered.

The Allied payment includes reimbursement of “defense fees and expenses” for the directors in the amount of \$411,616.43,²⁰ reimbursement of “defense fees and expenses” for Windermere in the amount of \$5,000, attorneys’ fees and costs for the Shidlofsky Law Firm in the amount of \$110,838.50 and penalties and prejudgment interest in excess of \$100,000.00.²¹ As Ratepayers’ proffered evidence clearly establishes, the amount of defense fees and expenses for the directors and for Windermere, respectively, as well as the fees and expenses of Shidlofsky to pursue the claim, was determined exclusively by Windermere itself.²² Unless Windermere’s board mismanaged its calculations, by definition the Allied settlement reimbursed in full all of Windermere’s costs for defense of the civil suits.²³

Even more important, setting aside the costs Windermere’s board has incurred for this rate appeal,²⁴ the Allied settlement is likely more than adequate to pay in full Windermere’s current unreported legal debt for all matters – civil suits (whether plaintiff or defendant) and the many other matters for which Windermere’s board involved outside counsel. The evidence at the March 2023 hearing²⁵ showed that as of the beginning of 2023, Windermere’s approximate legal debt was as follows:

Enoch Kever: \$75,000
Lloyd Gosselink (excluding Rate Appeal file): \$235,274
Shidlofsky: \$1,449

²⁰ This is around \$100,000 more than the Enoch Kever firm billed, however Windermere declined to provide the attachments to the Shidlofsky letter so the discrepancy cannot be reconciled with available information.

²¹ See Ratepayers Post-Hearing Exhibit 1 attached to the Motion to Reopen.

²² See Ratepayers Post-Hearing Exhibit 1.

²³ The TOMA Integrity litigation is not expressly mentioned, however the \$100,000 for penalties would easily cover the \$38,000 Windermere claims to have paid its attorneys in that case.

²⁴ The corporation’s appeal case expenses must be considered independently and are recoverable from ratepayers only if, as and through the mechanism determined by the Commission.

²⁵ See Ratepayers’ HOM2-144A and 144B.

Windermere asserted at the March 2023 hearing that it was continuing to pay \$10,000 per month per law firm against its unpaid balances, therefore the balances shown above should have been reduced by those amounts. The evidence showed that the Double F lawsuit was tried to a jury verdict in late 2022 and there was no evidence of any significant activity (or expense) in that case since then. To the extent the Shidlofsky Firm had additional billings, those should have been included within and covered by the settlement payment.

As a result, unless Windermere's board mismanaged the Allied settlement, it should now be in a position to fully extinguish the corporation's legal debt and to make good on its promise to put the rates back to pre-lawsuit levels. With a needed adjustment for other revenue, this is essentially what PUC Staff's recommended rates should accomplish. Assuming the board acts prudently going forward, there is simply no reason to think that Windermere's financial integrity will be jeopardized.

III. DISCUSSION

D. Revenue Requirement (PO Issue 7)

4. Analysis

a. Legal Expenses (Responsive to Section III.D.4.a of Staff's Exceptions)

Ratepayers cannot emphasize enough the simple truth that the appealed rates were borne of a blatant conflict of interest that resulted in the expenditure of unlimited corporate funds and credit for the benefit of interests other than those of the utility's ratepayers. Windermere's representatives have advanced a plethora of arguments over the course of this appeal in an effort to deflect from this truth, but none hold water. It is a fact that the corporation had no exposure in either of the "civil lawsuits." Its board confirmed as much when they warranted and represented

to CoBank that even if decided adversely to the corporation neither of the “civil lawsuits” could have a material impact on its finances or operations.²⁶ It is a fact that the corporation had nothing but potential upside from the “civil lawsuits.” In both cases, members using their own personal resources were attempting to restore to the corporation title to 4.3 acres of land taken by an unfaithful fiduciary and later in the Double F lawsuit, to also recover compensation for the corporation as necessary to make it whole. It is a fact that when the interests for which Windermere paid the enormous legal fees “prevailed,” the corporation did not receive its land back and was not compensated for its loss.

As PUC Staff illustrates, a rational, prudent and properly motivated board would not have authorized unlimited corporate expenditures to achieve such a result. The majority of Windermere’s 2020 board, however, was driven by their own personal interest in avoiding a personal judgment for damages without paying any legal costs. When Allied refused to pay defense costs, these directors took advantage of their positions to authorize unlimited legal services for the director defendants at corporate expense. These same directors approved a rate increase to require Windermere’s ratepayers to fund their ever-burgeoning legal needs. They disregarded mandatory provisions of the corporation’s governing documents and its tariff in the process.

The massive size of the legal spending relative to the means of the corporation just makes the situation that much worse.

Identifying conflicts of interest such as this, and protecting the ratepayers from abusive behavior by management, is an integral part of the Commission’s discharge of its regulatory

²⁶ Ratepayers note that the board also represented and warranted that this rate appeal, even if adversely decided, could not materially impact Windermere’s financial condition or operations.

duty. The Commission engages in this type of analysis all the time. The Commission does not hesitate to disallow expenses in these circumstances. It should take an equally hard line here.

Here, there are not just “discrepancies” in Windermere’s records. To the contrary, despite its extensive industry experience, Windermere’s sophisticated general counsel inexplicably failed even to prepare its records in a manner that would enable Windermere to segregate and to quantify its legal costs for defense of the civil lawsuits. Lloyd Gosselink failed to open separate files even for significant matters such as the Double F lawsuit. Lloyd Gosselink failed to record its work on a given matter under the file number for that matter. Lloyd Gosselink failed to record any of its work in such a way that time entries or costs could be associated with any particular matter.

In light of Lloyd Gosselink’s sophistication and experience, as well as

b. Other Revenues (Responsive to Section III.D.4.b of Windermere’s Exceptions)

G. Rate Case Expenses (Responsive to Section III.G of Staff’s Exceptions)

Staff’s exceptions acknowledge, as they must, that here a regulated utility represented by a firm with extensive industry experience incurred substantial legal expenses to participate in an appeal proceeding it knew was a sham. Staff’s exceptions chronicle Windermere’s pattern of deception, obfuscation and omission throughout this proceeding – and the substantial expense associated with such misconduct -- and conclude that Windermere should not be allowed to recover any of its appeal case expenses. Indeed, when pressed about Windermere’s misconduct, PUC Staff witness Anna Givens admitted that allowing recovery of case expenses in these circumstances would not be good public policy.²⁷

²⁷ Transcript, pp. 885-7.

And how could it be good public policy?

Over the course of a 3-year rate appeal and with excellent legal representation, Windermere has not furnished a coherent rate methodology, a rate calculation, or accurate and reliable data concerning its claimed costs of service or its revenues.

For almost the entire proceeding, Windermere unequivocally sponsored a version of its rate setting that its board knew was completely fictitious. The other parties spent countless hours reviewing legal invoices that had nothing at all to do with the appealed rates, and Windermere successfully prevented discovery of information that might have revealed the deception.

Windermere knew from PUC Staff's prefiled and hearing testimony that Staff had accepted the fictitious version as true and was working under the utterly false impression that Windermere's rates were set using a cash needs methodology with a revenue requirement of \$576,123 derived from Windermere's 2019-year end financials (including \$177,000 of legal costs) and a cost-of-service study reflected in the TRWA rate sheet which was furnished as Attachment Staff 1-1. Windermere did not lift a finger to correct Staff's misimpression until Ratepayers called its hand by filing an evidentiary motion that outlined a multitude of inaccuracies in Windermere's discovery responses that were never corrected by supplementation.

Even then, Windermere waited until the eve of the remand hearing to supplement some, but not all, of its false discovery information, but the supplementation raised more questions than it answered.

Although the board's stated reason for the rate increase was to pay legal costs, Windermere's sophisticated counsel Lloyd Gosselink kept its records in a manner that prevented anyone from allocating its legal services to defense of a civil suits or any other given matter or determining the costs for services rendered for any given matter. Instead, Windermere's

representatives proffered cost “estimates” under oath that its sponsors knew varied materially from the company’s reported information and took affirmative steps to conceal the deception. Most of that misinformation has never been corrected.

By all outward appearances, the Commission expects and requires better behavior on the part of the utilities it regulates. An award of case expenses in this appeal is purely discretionary, and this case will establish a precedent. In a far less egregious circumstance, the TCEQ refused to allow San Saba to recover any case expenses. The Commission should follow that lead here.

Whether Lloyd Gosselink does or does not get paid for this appeal is not the inquiry here. That said, the Commission need not feel sorry for Lloyd Gosselink. Ratepayers were prepared to put on evidence to show that Lloyd Gosselink, by far the largest beneficiary of the rate increase, was aware of and in some instances participated in the misconduct described above. Apparently under the mistaken impression that evidence must be directed either to case expenses or to the underlying rates, but never both, and that no witness proffered on one of these topics may be questioned about the other, the ALJs would not allow Ratepayers to develop their evidence.²⁸ Nevertheless, it is clear that Lloyd Gosselink itself has a conflict of interest. There is evidence to show Lloyd Gosselink knew at the time of the rate increase that the TRWA rate study had nothing to do with the appealed rates. There is evidence to show Lloyd Gosselink knew Windermere’s sworn “cost estimates” were materially inaccurate and assisted in the effort to cover it up. Such behavior should not be rewarded.

²⁸ See, e.g., Transcript (March 23, 2023) at p. 648.

IV. CONCLUSION

WHEREFORE, premises considered, Ratepayers respectfully request that Commission does not adopt the ALJ's proposal for decision and awarded such other and further relief, at law or in equity, to which Ratepayers has shown themselves justly entitled.

Respectfully Submitted,

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Certificate of Service

I hereby certify that, unless otherwise ordered by the Presiding Officer, notice of this filing was provided to all parties of record via electronic mail on August 10, 2023.

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