Bryan W. Shaw, Ph.D., *Chairman*
Buddy Garcia, *Commissioner*
Carlos Rubinstein, *Commissioner*
Mark R. Vickery, P.G., *Executive Director*

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

Protecting Texas by Reducing and Preventing Pollution

September 26, 2011

Ms. Bridget Bohac
Chief Clerk
Office of the Chief Clerk
Texas Commission on Environmental Quality
P.O. Box 13087, MC-105
Austin, Texas 78711-3087

Re: Appeal of Each Member of Navarro County Wholesale Ratepayers to review the wholesale water rate increase imposed by the City of Corsicana, CCN No. 10776 in Navarro County. SOAH Docket No. 582-10-1944; TCEQ Docket No. 2009-1925-UCR.

Dear Ms. Bohac:

Enclosed for filing with the Texas Commission on Environmental Quality is the original plus seven copies of "The Executive Director's Response to Exceptions to the Proposal for Decision" for the above referenced matter.

If you have any questions, please call me at (512) 239-0608.

Sincerely,

Ron M. Olson
Staff Attorney
Environmental Law Division

Enclosure

cc: Mailing List

SOAH DOCKET NO. 582-10-1944
TCEQ DOCKET NO. 2009-1925-UCR

APPEAL OF EACH MEMBER OF	**§**	**BEFORE THE STATE OFFICE**
THE NAVARRO COUNTY	**§**	
WHOLESALE RATEPAYERS TO	**§**	
REVIEW THE WHOLESALE RATE	**§**	
INCREASE IMPOSED BY THE	**§**	**OF**
CITY OF CORSICANA,	**§**	
CERTIFICATE OF CONVENIENCE	**§**	
AND NECESSITY NO. 10776, IN	**§**	
NAVARRO COUNTY	**§**	**ADMINISTRATIVE HEARINGS**

THE EXECUTIVE DIRECTOR'S RESPONSE TO EXCEPTIONS TO THE PROPOSAL FOR DECISION

TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

SEPTEMBER 26, 2011

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SOAH DOCKET NO. 582-10-1944
TCEQ DOCKET NO. 2009-1925-UCR

APPEAL OF EACH MEMBER OF THE NAVARRO COUNTY WHOLESALE RATEPAYERS TO REVIEW THE WHOLESALE RATE INCREASE IMPOSED BY THE CITY OF CORSICANA, CERTIFICATE OF CONVENIENCE AND NECESSITY NO. 10776, IN NAVARRO COUNTY	§ § § § § § § § §	**BEFORE THE TEXAS COMMISSION** **ON** **ENVIRONMENTAL QUALITY**

THE EXECUTIVE DIRECTOR'S RESPONSE TO EXCEPTIONS TO THE PROPOSAL FOR DECISION

TO THE HONORABLE COMMISSIONERS OF THE TEXAS COMMISSION ON ENIVROMENTAL QUALITY:

COMES NOW, the Executive Director ("ED") of the Texas Commission on Environmental Quality ("TCEQ" or "Commission"), and files the Executive Director's Response to Exceptions to the Proposal for Decision in the above-referenced matter.

I. THE ALJ HAS APPROPRIATELY RECOMMENDED DENIAL OF THE PETITIONERS' PETITIONS.

The Executive Director reviewed the members of the Navarro County Wholesale Ratepayers'[1] ("NCWR" or "Petitioners") petitions and all information provided by the parties, including discovery responses and pre-field testimony. Based on that information, the Executive Director recommended in his pre-filed testimony that the petitions be denied. The Administrative Law Judge ("ALJ") agreed and concluded that the Petitioners' wholesale water rate appeal should be denied because the Petitioners have "failed to show that Corsicana's rates evidence its abuse of monopolistic power in its provision of water service to them or that Corsicana's rates adversely affects the public interest."[2]

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[1] The members named as parties are: M.E.N. WSC, Rice WSC, Angus WSC, Chatfield WSC, Corbet WSC, Navarro Mills WSC, City of Blooming Grove, City of Frost, City of Kerens, and Community Water Company. The ED will refer to the Petitioners collectively as NCWR.
[2] Proposal for Decision ("PFD") at 70.

A. The ALJ correctly applied the appropriate legal standard in this case.

In 1977, the Texas Legislature enacted Texas Water Code Sections 11.036, 11.041, and 12.013 as the statutory framework used to appeal rate decisions made by the provider of state-owned water.[3] In 1994, the 3rd Court of Appeals held that before the Commission can modify a contractual rate in a wholesale rate appeal it must first make a finding that the rate adversely affects the public interest.[4] Therefore in August of 1994, the TCEQ adopted rules which were designed to determine if a seller's protested rate adversely affects the public interest.[5] In drafting the public interest rules, the Commission specifically considered and harmonized the statutory authority for reviewing wholesale rate appeals with the judicial precedence requiring a public interest test.[6] As the ALJ noted in the PFD, the public interest rules were upheld by the 13th Court of Appeals when it found that the TCEQ's public interest rules are a proper exercise of the Commission's statutory authority and found no reason to disturb the rate-reviewing scheme instituted by the Commission.[7] The Commission's public interest rules apply to petitions for the review of wholesale water rates filed pursuant to Texas Water Code Chapters 11, 12, and 13.[8] The ALJ correctly found that the Petitioners have failed to prove that Corsicana's protested rate adversely affects the public interest based on the Commission's rules.[9]

The Petitioners claim that the ALJ did not apply the appropriate legal standard in this case because they allege that rate discrimination between retail and wholesale customers should be reviewed under the public interest rules.[10] However, the ALJ correctly concluded that the public interest inquiry is limited to the criteria set out in 30 TEX. ADMIN. CODE § 291.133(a)(1)-(4), which does not include a comparison of the protested rate's impacts on wholesale and retail customers.[11] In fact, as the ALJ notes, "the Commission specifically chose to narrow the public interest inquiry and not look into alleged discrimination favoring

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[3] The Texas Legislature later enacted Texas Water Code Section 13.043(f) in 1989. The ED's Response to Exception to the PFD will not address Section 13.043(f) in this matter due to the ALJ's denial of the Petitioners' appeal under that section.
[4] *Texas Water Commission v. City of Fort Worth*, 875 S.W.2d 332, 336 (Tex. App. – Austin 1994).
[5] 19 Tex. Reg. 6227
[6] *See generally*, 19 Tex. Reg. 6227
[7] *Canyon Regional Water Authority v. Guadalupe-Blanco River Authority*, 286 S.W.2d 397, 406 (Tex. App. – Corpus Christi-Edinburg 2008). This case was transferred from the Third Court of Appeals to the Thirteenth Court of Appeals under a docket equalization order issued by the Supreme Court of Texas.
[8] 30 TEX. ADMIN. CODE § 291.128
[9] PFD at 70.
[10] NCWR's Exceptions to the PFD at 3-8.
[11] PFD at 13.

retail over wholesale customers."[12] The ALJ bases his finding on specific revisions to the public interest criteria before the public interest rules were adopted.[13] The original proposed language for Commission rule 291.133(a)(4) stated that one criteria to consider is that "the protested rate appears to discriminate between the purchaser and others who purchase water... service from the seller, and the seller does not provide reasonable support for such discrimination."[14] However, after considering comments relating to the proposed rule language, the Commission agreed that 291.133(a)(4) should be changed to its current form[15], which focuses only on discrimination between wholesale customers.[16] The Commission reasoned that it is the rate charged to other wholesale customers that is relevant to the public interest inquiry.[17] The preamble to the public interest rules expressly states that the public interest criteria as adopted are sufficiently broad; and a party should not be allowed to urge that some other criteria have been violated.[18] Accordingly, the ALJ correctly found that the Petitioners' argument regarding rate discrimination between Corsicana's wholesale and retail customers cannot be added as an additional criterion under 291.133(a).

Petitioners also argue that abuse of monopoly power is a way of characterizing rate discrimination between wholesale and retail customers; and that issue should be an additional factor considered under 291.133(a)(3).[19] However, as the Commission stated in the preamble, the public interest inquiry under Section 291.133(a)(3) sufficiently covers whether any disparity in treatment between retail and wholesale customers adversely affects the public interest.[20] Therefore, the analysis of the disparity in treatment between a seller's wholesale and retail customers is considered through analyzing factors A through H listed in Section 291.133(a)(3).[21] In other words, there is no need to create and analyze an additional factor as suggested by the Petitioners. The ALJ correctly found that the language in the preamble limited the inquiry and did not expand the rule to cover the Petitioners' additional factor.[22] The PFD provides a thorough analysis of the evidence presented based on factors A-

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[12] PFD at 15.
[13] *Id*.
[14] 19 Tex. Reg. 3900
[15] "(4) the protested rate is unreasonably preferential, prejudicial, or discriminatory, compared to the wholesale rates the seller charges other wholesale customers." 30 TEX. ADMIN. CODE § 291.133(a)(4).
[16] PFD at 15.
[17] 19 Tex. Reg. 6229
[18] 19 Tex. Reg. 6228
[19] NCWR's Exceptions to the PFD at 7-8.
[20] 19 Tex. Reg. 6229
[21] Tr. 946:24-947:4 & Tr. 956:6-14 (Brian Dickey).
[22] PFD at 15.

H. The ALJ appropriately held that the Petitioners failed to provide sufficient evidence to prove that Corsicana's protested rate was an abuse of monopoly power.[23]

The Petitioners further argue that the PFD misapplies the law to the facts in this case and fails to consider important evidence.[24] The Petitioners claim that the ALJ should have given some evidentiary weight to the McLain rate study because they allege that the study demonstrates Corsicana's rate discrimination based on the three alternative rate structures Corsicana considered.[25] The crux of the Petitioners' argument regarding rate discrimination is that Corsicana's tiered volumetric rate discriminatorily shifts the allocation of Corsicana's revenue requirement to the wholesale customers.[26] However, the allocation of Corsicana's revenue requirement is a cost of service issue which cannot be considered in this proceeding.[27] The TCEQ rules expressly state that the "Commission shall not determine whether the protested rate adversely affects the public interest based on an analysis of the seller's cost of service."[28] In order to determine if there is discrimination between the wholesale and retail customers based on the allocation of Corsicana's revenue requirement, a cost of service analysis would have to be performed in order to determine what costs were allocated to each customer group. The mere fact that Corsicana's customers purchase water at different tiers does not prove that the rate design is discriminatory. For example, each Petitioner testified that they are not being surcharged for Corsicana's capital improvements used to provide water service to them.[29] Therefore, as Mr. Mullins testified, all of Corsicana's customers are sharing the costs incurred for Corsicana to increase its capacity to meet the needs of its wholesale customers.[30] The Petitioners do not pay extra for the high demand that they place on Corsicana's water system.[31] To cure that inequity, Corsicana could reasonably choose to recover those costs attributed to the wholesale customers through implementation of its tiered rate design, rather than having the average residential customer subsidize the additional expenses incurred to provide service to the high demand customers.

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[23] PFD at 70.
[24] NCWR's Exceptions to the PFD at 8.
[25] *Id*. at 10.
[26] *Id*. at 19.
[27] 30 TEX. ADMIN. CODE § 291.133(b)
[28] *Id*.
[29] Tr. 94:24-95:2 (James Metcalfe); Tr. 239:17-21 (David Weinkauf); Tr. 287:21-25 (Melinda Gatewood); Tr. 346:12-16 (Joey Smith); Tr. 385:11-16 (Scott Hampel); Tr. 405:23-406:2 (Cindy Scott); Tr. 449:17-22 (Dennis Donoho); Tr. 499:11-16 (Chris Ivey).
[30] Tr. 1145:3-12 (Allen Mullins).
[31] Tr. 1144:19-25 (Allen Mullins).

If that is the case, clearly the effects of Corsicana's rate design would not be discriminatory; the Petitioners would be paying for their increased demand on Corsicana's water system. Therefore, the fact that the Petitioners purchase most of their water at the highest tier, as opposed to Corsicana's residential customers purchasing most of their water at the lowest tier, does not prove that Corsicana's rate design is discriminatory. Nevertheless, a cost of service analysis cannot be considered in this phase of the proceeding.[32] As the ALJ correctly found, the "evidence concerning Corsicana's cost of service is irrelevant to determining whether Corsicana's rates adversely affect the public interest."[33] Accordingly, the ALJ applied the correct legal standard to the evidence presented in this case and appropriately determined that Corsicana's protested rate does not adversely affect the public interest.[34]

B. The ALJ properly found that cost of service is not relevant in determining whether the protested rates affect the public interest.

As mentioned *supra*, the Commission's rules clearly state that the Commission shall not determine whether the protested rate adversely affects the public interest based on an analysis of the seller's cost of service.[35] Throughout the hearing process, cost of service has been a significant issue. Therefore, the ALJ spends a portion of his proposal for decision discussing what cost of service is and whether evidence should be excluded on the basis that it is cost of service. The ALJ concludes that "evidence concerning Corsicana's cost of service is irrelevant to determining whether a protested rate adversely affects the public interest."[36] In their exceptions, the Petitioners argue that the ALJ correctly draws the line in determining cost of service in some instances but not in others.[37] Specifically, Petitioners erroneously argue that: 1) Corsicana's need for additional operating reserves is a cost of service issue and not a changed condition; 2) a wastewater subsidy is not a cost of service issue for any water customer; and 3) the PFD mischaracterizes many of the Protestants' arguments as cost of service.[38]

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[32] 30 TEX. ADMIN. CODE § 291.133(b)
[33] PFD at 18.
[34] PFD at 70.
[35] 30 TEX. ADMIN. CODE § 291.133(b).
[36] PFD at 18.
[37] NCWR's Exceptions to the PFD at 12.
[38] NCWR's Exceptions to the PFD at 11-19.

1. The Petitioners incorrectly argue that Corsicana's need for additional operating reserves is a cost of service issue and is not a changed condition under 291.133(a)(3)(B).

Before reaching Petitioners substantive argument regarding whether Corsicana's need for additional operating reserves is cost of service, it is important to consider the burden of proof in this matter. TCEQ rules make it clear that the petitioner bears the burden of proof in the public interest phase of the hearing.[39] Section 291.136 of the Commission's rules states that the "petitioner shall have the burden of proof in the evidentiary proceedings to determine if the protested rate is adverse to the public interest."[40] That rule is clear and unambiguous in its placement of the burden on the petitioner. Therefore, it is the Petitioners who must satisfy their burden of proof and show that Corsicana did not reasonably demonstrate the changed conditions that are the basis for the change in rates. Contrary to the rules, Petitioners argue that the burden is on Corsicana to provide evidence of the changed conditions that are the basis for the change in its rates.

If the Commission were to determine that it is Corsicana's burden to demonstrate the changed conditions that are the basis for the change in rates, Corsicana has met that burden. The ALJ concluded in his proposal for decision that the Utility Fund deficit, regardless of its cause or causes was a changed condition that gave Corsicana a reasonable basis for increasing its water rates."[41] There was no evidence presented to contradict that the Utility Fund had a one million dollar deficit when Corsicana changed its rates.[42] The Petitioners' argument that the deficit in the Utility Fund is a cost of service issue is unfounded. Regardless of what caused the Utility Fund deficit, the Utility Fund deficit in and of itself is not a cost of service issue. The cause or causes of the Utility Fund deficit may be cost of service issues, but the actual deficit is not.[43] The ALJ appropriately limits his analysis of the Utility Fund deficit to exclude cost of service issues.

The Petitioners also argue that consideration of the Utility Fund deficit cannot be considered a changed condition. Petitioners argue that Corsicana's Utility Fund required additional reserves only because water revenues were subsidizing wastewater expenses. However, in order to analyze the cause behind the Utility Fund's deficit, a cost of service

[39] 30 TEX. ADMIN. CODE § 291.136.
[40] *Id*.
[41] PFD at 50.
[42] PFD at 49.
[43] PFD at 50.

analysis would have to be conducted. The TCEQ rules clearly prohibit such an analysis in this phase of the proceeding.[44] The ALJ properly found that Corsicana's Utility Fund deficit was a changed condition that was the basis for its change of rates and properly avoided a cost of service analysis in making his finding.

2. The Petitioners incorrectly argue that a wastewater subsidy is not a cost of service issue for any water customer.

Petitioners' claim that wholesale water rates are subsidizing wastewater services is a cost of service issue which is outside the scope of the public interest portion of this hearing.[45] In order to determine whether the rates Petitioners pay are subsidizing wastewater service, Corsicana's cost of service would need to be analyzed. The Commission would have to look at whether Corsicana's water and wastewater operation and maintenance expenses are reasonable and necessary to provide water service.[46] TCEQ rules expressly prohibit this type of analysis during the public interest portion of the hearing.[47] Therefore, the ALJ properly excluded from consideration whether the Petitioners water rates were subsidizing wastewater expenses.[48]

Petitioners also argue that only wholesale water cost of service issues are barred from consideration.[49] However, the Commission rule makes no distinction between whether water and wastewater cost of service issues may be analyzed. The rule simply states that the Commission shall not consider the "seller's cost of service."[50]

3. The Petitioners incorrectly argue that the PFD mischaracterizes many of the Petitioners' arguments as cost of service.

The Petitioners argue that it is not claiming that Corsicana's abuse of monopoly power is demonstrated through Corsicana's cost of service.[51] Instead Petitioners claim that their reliance on Corsicana's cost of service in Table 1.7 of the McLain study, and discussions of the alternative rate structure that McLain titled "Cost-Based Rates", is to highlight the extent of

[44] 30 TEX. ADMIN. CODE § 291.133(b)
[45] *See* PFD at 22.
[46] *See* PFD at 22.
[47] 30 TEX. ADMIN. CODE § 291.133(b).
[48] *See* PFD at 22.
[49] NCWR's Exceptions to the PFD at 16.
[50] 30 TEX. ADMIN CODE § 291.133(b).
[51] NCWR's Exceptions to the PFD at 18.

Corsicana's rate discrimination.[52] Petitioners' argument fails to take into consideration that cost of service cannot be considered to show Corsicana's rate discrimination or for any portion of the public interest hearing. The rule does not make an exception for cost of service issues to be considered in matters of discrimination. Instead the rule clearly states, "[t]he Commission shall not determine whether the protested rate adversely affects the public interest based on an analysis of the seller's cost of service."[53] Nowhere does the rule state that cost of service may be used in order to determine whether the seller has discriminated against the buyer.

Although Table 1.7 of the McLain study is an analysis of Corsicana's rate allocation, the Petitioners argue that its reliance on Table 1.7 is unrelated to Corsicana's cost of service. Petitioners argue that their reliance on Table 1.7 is to show Corsicana's discriminatory intent is to shift the burden of raising revenue to wholesale customers while shielding residential customers.[54] As mentioned *supra*, this argument relies on determining how Corsicana decided to allocate its revenues, which is a cost of service argument. Petitioners speculate that the reason Corsicana chose the rate structure it did was to discriminate against the wholesale ratepayers. However, in order to come to this conclusion Corsicana's cost of service would need to be analyzed, which is prohibited by TCEQ rules. The ALJ properly assigned no evidentiary weight to the McLain study, and its previous drafts, based on a lack of testimony by Mr. McLain to evaluate his credibility, his expertise to offer the opinions stated in his study, the bases for his opinions, or the sources of information for the facts stated in the studies.[55] Accordingly, the ALJ properly found that cost of service is not relevant even if it is supported by evidence.[56]

C. The ALJ appropriately found that whether the protested rates conform to the wholesale contracts is outside the scope of this case.

The TCEQ does not have jurisdiction to interpret the meaning of contractual clauses regarding whether the protested rate is set pursuant to a contract. Petitioners argue in their exceptions to the PFD that all terms of the contract should be considered. Petitioners claim

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[52] *Id.*
[53] 30 TEX. ADMIN. CODE § 291.133(b).
[54] NCWR's Exceptions to the PFD at 19.
[55] PFD at 24.
[56] PFD at 22.

that the ALJ did not consider the clause in their contracts which they allege requires "Corsicana [to] charge the minimum retail rate to its wholesale customers."[57] However, TCEQ rules specifically state that if the seller and the buyer to a wholesale contract do not agree that the protested rate is set pursuant to a written contract, then the administrative law judge shall abate the proceedings until the contract dispute over whether the protested rate is part of the contract has been resolved by a court of proper jurisdiction.[58] The ALJ appropriately found that the rule assumes the seller's protested rate correctly interprets any existing agreement between the seller and the purchaser.[59] Petitioners' allegations that the contracts are being misread must be presented in district court; and therefore, are improperly made before the State Office of Administrative Hearings ("SOAH"). The ALJ properly concludes that whether the protested rate conforms to the contracts between the Petitioners and Corsicana is outside the scope of this case.[60]

D. The ALJ correctly determined that Corsicana's change in rate design does not evidence an abuse of monopoly power.

The Petitioners argue that Corsicana's change in rate design evidences an abuse of monopoly power.[61] The Petitioners erroneously claim that the "2009 Rate Increase raised rates for wholesale customers by more than three times as much as for Corsicana's... average residential customers."[62] However, as the PFD illustrates, that allegation is without evidentiary support.

Corsicana's City Manager, Ms. Standridge, testified that the "wholesale customers negotiated their contracts to ensure that they would pay the same rates as the retail customers residing inside Corsicana..."[63] As discussed in the PFD, Corsicana's ordinance establishing the 2009 rate increase included a base rate and a volumetric rate that are the same for its wholesale customers and its inside-city retail customers.[64] Therefore, both

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[57] NCWR's Exceptions to the PFD at 25.
[58] 30 TEX. ADMIN. CODE § 290.131(d).
[59] PFD at 24.
[60] PFD at 23
[61] NCWR's Exceptions to the PFD at 26-30.
[62] NCWR's Exceptions to PFD at 27. The Petitioners citations to the record refer to exhibits that do not address Corsicana's protested rates. Instead, the citations refer to the revenues collected by Corsicana. The TCEQ's public interest rules are only focused on the seller's protested rate, not the revenues. Any review beyond the rate itself leads to a cost of service analysis which is specifically prohibited by Commission rule 291.133(b).
[63] *Direct Testimony of Connie Standridge* at 6:16-19.
[64] PFD at 57. *See also,* Ex. NCWR 25.

customer groups pay the same rates based on the varied amounts of water they purchase.[65] Although the Petitioners may purchase most of their water at the highest tier, that circumstance is not limited solely to wholesale customers. As the ALJ points out in the PFD, there are at least 689 retail customers that pay Corsicana's top tier gallonage rate.[66] The evidence presented at the hearing conclusively established that all of Corsicana's high-volume customers, whether they are wholesale or retail customers, pay the third tier rate for water consumption over 25,000 gallons. Therefore, Corsicana's rate design affects each customer group the same. The ALJ correctly determined that the "evidence shows that the inside-city retail rates have not been set as a sham so that only wholesale customers are affected by the change."[67]

Additionally, as discussed further below, the ALJ correctly found that Corsicana's change in rate design is not an abuse of monopoly power because it encourages water conservation in keeping with Commission policy.[68] The Petitioners are simply unhappy with the rate structure Corsicana adopted, and have not presented any evidence which proves that the protested rate itself is an abuse of monopoly power. Accordingly, the ALJ correctly found that Corsicana's rate design was not abusive.[69]

E. The ALJ properly found that inclining block rates encourage water conservation.

The protested rate creates an incentive to encourage water conservation measures. As Ms. Standridge testified, the tiered rates encourage wholesale customers to efficiently use water resources by looking for leaks, lowering unaccounted for water losses, and requiring wholesale customers to implement the same measures that the TCEQ requires Corsicana to comply with in order to ensure efficient water use.[70] For example, Ms. Gatewood testified that without Angus WSC's line leakage, its water volume used in 2010 would have been lower.[71] Likewise, as Ms. Scott testified, the City of Kerens can reduce the amount of water it purchases from Corsicana by fixing its line loss.[72] Therefore, as Ms. Standridge's testimony

[65] Tr. 645:22-646:10 (Connie Standridge).
[66] PFD at 57.
[67] *Id.* at 58.
[68] PFD at 58.
[69] *Id.* at 50 & 56.
[70] Tr. 644: 22-645:4 (Connie Standridge).
[71] *Direct Testimony of Melinda Gatewood* at 10:9-10.
[72] Tr. 411:18-21 (Cindy Scott).

demonstrates, the tiered volumetric rates are also used to incentivize Corsicana's wholesale customers to conserve water. That is not an abuse of Corsicana's monopoly power.

The Petitioners argue that conservation is not needed because Petitioners already use less water and it would be impossible for Petitioners to conserve enough water to drop below the third tier.[73] It is difficult to rationalize this argument in light of the current drought conditions. Even under non-drought conditions, the Region C Water Plan recommends conservation as a valid water management strategy for the City of Blooming Grove, Chatfield WSC, Community Water Company, City of Frost, City of Kerens, M.E.N. WSC, Navarro Mills WSC, and Rice WSC.[74] Petitioners' argument that it would be impossible for Petitioners to conserve enough water to drop them below the third tier fails to take into consideration that a reduction in the amount of water each Petitioner purchases would simultaneously save money and conserve water. Regardless of whether the Petitioners fall below the third tier rate, a reduction in the volume of water purchased will prolong the existing source of water through conservation and reduce the monthly amount of water the Petitioners need to purchase. Therefore, the ALJ properly concluded that "inclining block rates encourage water conservation . . . that includes encouraging wholesale customers like the [Petitioners] to search for and repair leaks."[75]

F. The ALJ appropriately found that the rates charged by other sellers of water for resale in Texas do not suggest that Corsicana's rates indicate an abuse of monopoly power.

The Petitioners failed to provide evidence showing that there was an abuse of monopoly power based on the wholesale rates charged by other wholesale providers. The language in 30 Texas Administrative Code Section 291.133(a)(3)(G) clearly states that one relevant factor that shows that the protested rate evidences an abuse of monopoly power is by comparing the seller's rates to "the rates charged in Texas by other sellers of water or sewer service for resale."[76] The Petitioners, however, misinterpret this subsection. They argue that Corsicana has abused its monopoly power based on the comparison "between wholesale and retail rates charged by other sellers."[77] This interpretation is flawed because the rule

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[73] *Id.* at 30.
[74] Corsicana Ex. 31 at 4F.339-4F.340.
[75] PFD at 60.
[76] 30 TEX. ADMIN. CODE § 291.133(a)(3)(G)
[77] *See* NCWR's Exceptions to the PFD at 32.

expressly requires a comparison of the rates charged in Texas by other sellers of water or sewer service for resale. The rule does not compare the wholesale rates and the retail rates of other retail providers in Texas.

The evidence showed that Waxahachie's volumetric rate for wholesale customers is $3.45 per 1,000 gallons and that the Brazos River Authority charges an average rate of $3.97 per 1,000 gallons.[78] Both of these wholesale providers' rates are higher than Corsicana's top tier rate of $3.25. Therefore, the ALJ correctly found that the "rates charged by other sellers of water for resale in Texas do not suggest that Corsicana's rates indicate an abuse of monopoly power."[79]

G. The ALJ correctly determined that Corsicana's protested rate does not evidence an abuse of monopoly power based on the retail rates charged by the Petitioners and Corsicana.

The Petitioners erroneously argue that the PFD incorrectly analyzes Section 291.133(a)(3)(H) of the TCEQ rules.[80] The Petitioners allege that Corsicana's wholesale rate evidences an abuse of monopoly power because each Petitioner's retail rates are higher than Corsicana's retail rates.[81] However, as the ALJ concluded, this comparison is meaningless.[82] There are numerous reasons which explain why a wholesale purchaser's retail rates are higher than the wholesale seller's retail rates.[83] For example, all of the Petitioners in this case have their own operation and maintenance costs which contribute to their retail rates being higher than Corsicana's retail rates.[84] "The higher rates to the wholesale customer's end users are the result of the wholesale customers' cost over and above the cost to purchase water from Corsicana, and are not attributed to Corsicana's wholesale rate."[85] The proper analysis under Section 291.133(a)(3)(H) is to examine "the seller's rates for water...service charged to its retail customers, compared to the retail rates the purchaser charges its retail customers as a result of the wholesale rate the seller demands from the purchaser."[86] This factor focuses on the comparison between Corsicana's retail rate and each Petitioner's retail

[78] PFD at 62.
[79] PFD at 63.
[80] *Id*. at 32.
[81] NCWR's Exceptions to the PFD at 32.
[82] PFD at 69.
[83] *Direct Testimony of Brian Dickey* at 28:5-9.
[84] *Id. See also, Direct Testimony of Jack Stowe* at 30:1-4.
[85] *Direct Testimony of Allen Mullins* at 9:9-12.
[86] 30 TEX. ADMIN. CODE § 291.133(a)(3)(H).

rate that it charges its customers *as a result of Corsicana's wholesale rate*.[87] Therefore, the analysis under this factor should not compare Corsicana's retail rates to the Petitioners' marked-up retail rates.[88] The comparison is made by reviewing Corsicana's retail rates and the Petitioners' retail rates without including the portion of the Petitioners' rates that are not attributable to Corsicana's wholesale rate. As the ALJ stated, the Petitioners' suggested rate comparisons "are not required by or relevant under the Commission's public interest rules."[89]

The Petitioners also argue that the ALJ inappropriately analyzed Section 291.133(a)(3)(H) by "comparing the effective rate of an average Corsicana customer to the effective rate paid by the [Petitioners]."[90] However, the Petitioners' allegations are false. In accordance with Commission rules, the ALJ specifically compared Corsicana's retail rates with the retail rates that the Petitioners charge its customers as a result of Corsicana's wholesale rate.[91] Despite the Petitioners' claim, the PFD does not compare Corsicana's retail rates to the rate that the Petitioners themselves pay to Corsicana. As discussed in the PFD, Corsicana's average in-city retail customers are billed $32.60 for water.[92] That translates into Corsicana's retail customers paying $5.43 per 1,000 gallons of water.[93] Conversely, the portion of the Petitioners' customers' retail water bills that result from Corsicana's wholesale rate range from $19.73 to $20.68.[94] That translates into the Petitioners' retail customers paying from $3.29 to $3.45 per 1,000 gallons of water.[95] Therefore, once the Petitioners' operating costs that are not attributable to Corsicana's wholesale rate are removed, Petitioners' retail customers pay approximately 36% less than Corsicana's retail customers for the same amount of water. As the ALJ found, "this is a straightforward apples-to-apples comparison"[96], which does not indicate Corsicana's abuse of monopoly power.[97] Accordingly, the ALJ correctly analyzed the evidence in accordance with Section 291.133(a)(3)(H) and determined that Corsicana's protested rate does not evidence an abuse of monopoly power based on the retail rates charged by the Petitioners and Corsicana.

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[87] *Id*. at 8:19-9:12; *See also*, 30 TEX. ADMIN. CODE § 291.133(a)(3)(H).
[88] *Direct Testimony of Allen Mullins* at 8:25-27.
[89] PFD at 68.
[90] NCWR's Exceptions to the PFD at 33.
[91] PFD at 64-67.
[92] PFD at 65. $17.60 + ($3.00 x 5) = $32.60. Corsicana's base rate includes 1,000 gallons. *See also* Corsicana Ex. 28
[93] $32.60/6 = $5.43. *See also*, Tr. 1139:8-14 (Allen Mullins).
[94] PFD at 66-67. *See also*, Page 23 of the ED's Closing Arguments for the same table which details each Petitioner's retail rate that result from Corsicana's wholesale rate.
[95] *Id*.
[96] PFD at 64.
[97] PFD at 69.

II. CONCLUSION

The TCEQ rules provide specific factors to consider when determining whether a seller's protested rate evidences an abuse of its monopoly power. The ALJ's PFD accurately analyzes the evidence presented in this case based on the Commission's public interest rules. As discussed in the PFD, Corsicana's deficit in its operating reserves is a legitimate changed condition for instituting the 2009 rate increase. Even with the increased rates, the Petitioners' retail customers still pay less than Corsicana's retail customers based on the rate that Corsicana demands from the Petitioners. Corsicana's rate design applies to both its wholesale and retail customers equally based on the volume of water they purchase, and encourages water conservation. Accordingly, the PFD correctly concludes that the change in rate design is not an abuse of Corsicana's monopoly power. Additionally, other wholesale water providers charge more per 1,000 gallons of water than what the Petitioners pay to Corsicana at the top tier. Therefore, the PFD correctly finds that the Petitioners have failed to show that Corsicana's protested rate adversely affects the public interest. Accordingly, the ED recommends that the Commissioners adopt the Proposal for Decision and proposed order as revised by the ED's previously filed exceptions.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that on September 26, 2011, a copy of the foregoing document was sent by first class, agency mail, electronic mail, and/or facsimile to the persons on the attached Mailing List.

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