

RAILROAD COMMISSION OF TEXAS

RATE CASE EXPENSES ISSUES §
SEVERED FROM GAS UTILITIES § GAS UTILITIES DOCKET NO. 8941
DOCKET NOS. 8749-8754 §

PROPOSAL FOR DECISION**I. Introduction**

Texas Southeastern Gas company (TSE) is a gas utility that owns and operates three physically discrete pipeline systems (North, Central, and South) in Texas. The North System serves Complainant Cities of Hempstead, Navasota, Tomball, and Waller, as well as the City of Prairie View and various industrial customers; the Central System serves the Complainant Cities of Brenham and Sealy, as well as the City of Bellville and various industrial customers; and the South System serves the Cities of Columbus and Eagle Lake as well as various industrial customers. TSE also sells gas to certain marketing affiliates and provides gas service to Bay City Gas Company using a third party's pipeline system.

On September 30, 1996, the Cities of Brenham, Hempstead, Navasota, Sealy, Tomball, and Waller (Cities) filed a complaint with the Railroad Commission of Texas (Commission) asserting that TSE had engaged in "a pattern of discrimination and misrepresentation and has consciously disregarded the Commission's rules and regulations." In the Complaint, the Cities requested that the Commission take certain actions, including setting rates and ordering TSE to reimburse the Cities for the reasonable costs of consultants, accountants, auditors, attorneys, engineers or any combination thereof, to conduct investigations, present evidence, advise and represent the Cities in this proceeding. On April 13, 1999, the Commission issued Orders in Gas Utilities Docket (GUD) Nos. 8749-8754, wherein the Commission ordered "that all issues related to reimbursement of rate case expenses are hereby severed from this case for consideration in another docket." The current docket, GUD No. 8941, was created for the consideration of such rate case expenses.

After hearing the evidence and reviewing the arguments of the parties, the Examiner recommends that the Commission take the following action:

- a. Order TSE to reimburse the Cities for their reasonable rate case expenses in the amount of \$393,813.79;
- b. Authorize TSE to charge a surcharge to recover the Cities' rate case expenses it is ordered to pay herein, over a period of two years; and
- c. Deny TSE's request to be allowed to charge a surcharge for its attorneys fees expended in Docket Nos. 8749-8754. If the Commission wishes to allow TSE to recover its attorneys fees from the Cities, TSE's reasonable attorneys fees and expenses are \$149,188.12.

II. Jurisdiction and Notice

The Commission has jurisdiction over the matters at issue in this proceeding under TEX. UTIL. CODE ANN. §§ 102.001(a), 121.051, and 121.151 (Vernon 1998). The statutes and rules involved include, but are not limited to, TEX. UTIL. CODE ANN. § 103.022 (Vernon 1998) and 16 TEX. ADMIN. CODE § 7.57 (West 2000). The Notice of Hearing issued in this Docket on June 10, 1999, to TSE and the Cities satisfied the requirements of 16 TEX. ADMIN. CODE §1.45 (West 1999) and of TEX. GOV'T. CODE ANN. § 2001.052 (Vernon 2000).

III. Issues

A. List of Issues and Recommendations:

Issue No. 1: Should TSE be ordered to reimburse the Cities for their reasonable rate case expenses?

Recommendation: The Examiner recommends that TSE be ordered to reimburse the Cities for the amount of the Cities' reasonable rate case expenses in the amount of \$ 393,813.79.

This issue includes discussion of five sub-issues concerning specific categories of expenses and whether each should be included in the total amount of rate case expenses awarded to the Cities. The categories are as follows:

- (a) Should the Cities be reimbursed at the "value rate" set out in fee agreements or the "discount rates" actually charged to the Cities? The Examiner recommends the discount rate.
- (b) Should the Cities be reimbursed for fees and expenses incurred for participation in the TSE Audit docket, GUD No. 8784? The Examiner recommends that the Cities not be reimbursed for fees and expenses related to GUD No. 8784.
- (c) Should expenses attributable to the Grimes County litigation be included in the rate case reimbursement by TSE to the Cities? The Examiner recommends that those Grimes County litigation expenses actually included in complaint docket billings should be allowed.
- (d) Should TSE be required to reimburse the Cities for fees and expenses associated with addressing the *High Plains* issue in the complaint dockets? The Examiner recommends that those fees and expenses are recoverable by the Cities from TSE.
- (e) Are the Cities' fees and expenses excessive because of the inclusion of Gaylord Hughey's fees and/or when compared to the results achieved or to TSE's fees and expenses? The Examiner recommends that the Cities met their burden of establishing that the fees requested are reasonable and not excessive.

Issue No. 2: How should the Cities' rate case expenses be reimbursed?

Recommendation: The Examiner recommends that each City receive a percentage of the rate case expenses based on the amount of MMBtus taken by each City during calendar year 1996.

Issue No. 3: Should TSE be allowed to collect a surcharge to recover the rate case expenses it is ordered to pay to the Cities?

Recommendation: The Examiner recommends that TSE be allowed to recover, through a surcharge, the amount of fees and expenses it reimburses to the Cities.

Issue No. 4: If the Commission approves a surcharge, how should it be structured?

Recommendation: If the Commission approves a surcharge, the Examiner recommends that the Commission approve an allocation based upon each Cities' consumption during the first year during which Commission-set rates applied and that the recovery be spread over a two-year period.

Issue No. 5: Should TSE be allowed to recover its attorneys fees from the Cities?

Recommendation: The Examiner recommends that TSE not be allowed to recover its attorney's fees.

B. Discussion of Issues:

Issue No. 1: Should TSE be ordered to reimburse the Cities for their reasonable rate case expenses?

Recommendation: The Examiner recommends that TSE be ordered to reimburse the Cities for the amount of the Cities' reasonable rate case expenses in the amount of \$ 393,813.79.

The Cities have requested that the Commission order TSE to reimburse the Cities for the reasonable costs of consultants, accountants, auditors, attorneys, engineers, or any combination thereof, to conduct investigations, present evidence, advise and represent the Cities in this proceeding. The Examiner recommends that the Commission find that the Cities reasonably expended \$393,813.79 on this rate proceeding, and order TSE to pay such expenses to the Cities.

The Commission has the authority to determine the reasonableness of the Cities' rate case expenses, and to require the utility to reimburse the Cities for those expenses, under Texas Utility Code (TUC) Section 103.022:¹

¹ TEX. UTIL. CODE ANN. § 103.022 (Vernon 1998).

(a) The governing body of a municipality participating in or conducting a ratemaking proceeding may engage rate consultants, accountants, auditors, attorneys, and engineers to:

(1) conduct investigations, present evidence, and advise and represent the governing body; and

(2) assist the governing body with litigation or a gas utility ratemaking proceeding before a regulatory authority or court.

(b) The gas utility in the ratemaking proceeding *shall* reimburse the governing body of the municipality for the reasonable cost of the services of a person engaged under Subsection (a) *to the extent the applicable regulatory authority determines reasonable*. (Emphasis added.)

In addition, TUC Section 104.055(d) provides that “[t]he regulatory authority may adopt reasonable rules complying with this section with respect to including and excluding certain expenses in computing the rates to be established.”² The Commission has adopted Rule 7.57, which authorizes a municipality to claim reimbursement of rate case expenses in any rate proceeding if the municipality proves their reasonableness by a preponderance of the evidence.³

The Cities have proven by a preponderance of the evidence that their rate case expenses in the amount of \$393,813.79 are reasonable. The Examiner recommends that the Cities’ reasonable recoverable rate case expenses include the discounted attorneys fees and expenses actually paid by the Cities, rather than the contingent “value rate” fees, plus expert witness fees and estimates of court proceedings, minus expenses associated with the audit docket. The sum of the Cities’ expenses as shown on Cities’ Exhibit No. 9 are \$415,245.79. Subtraction of audit docket costs (\$21,432) results in a sum of \$393,813.79.

a. **The reasonable attorneys fees are the discounted attorneys fees actually paid, not the full “value rate” (contingency fees).**

The Examiner recommends that the Cities should not be allowed to recover the “value rate,” because it represents attorney fees which were not actually paid by the Cities. Instead, the Cities should be allowed to recover the “discount rate” and reasonable expenses actually paid by the Cities.

² TEX. UTIL. CODE ANN. § 104.055 (Vernon 1998).

³ 16 TEX. ADMIN. CODE § 7.57 (West 1999).

The Hays Law Firm and the Hughey Law Firm both agreed to reduce their rates to the Cities, and agreed that additional amounts would be payable only to the extent they are recovered from TSE as attorneys fees before the Railroad Commission.⁴ The Cities request that the full “value rate” be reimbursed. The Cities argue that caselaw indicates that “the contingent nature of the fee is a factor to be taken into account, because it increases the risk that the attorneys are bearing, and nothing in the law suggests that it renders a fee not a fee.”⁵ Further, the Cities claim that the full “value” hourly rates for the cities’ attorneys are well within reasonableness.

Nevertheless, only expenses that are actually incurred can be reimbursed. As TSE points out, “a reimbursement contemplates an actual expenditure.”⁶ The contracts provide that the “standard hourly rates” would be payable “only to the extent that any such additional amounts are recovered from Texas Southeastern Gas Company.”⁷ Thus, “costs that are hypothetical or not actually incurred by the city in a ratemaking proceeding are not reimbursable.”⁸

The Examiner recommends that the Commission allow the Cities reimbursement of their actual costs paid, or the “discount” rate. Even though the Cities claim that the full “value” rates are reasonable because of the “risk premium” undertaken by the attorneys, the Examiner does not find this persuasive, in light of the caselaw and the actual expenditures of the Cities. Even though the Cities claim that a contingent fee is still a “fee,” it has not actually been paid by the Cities, and is not an actual cost. To allow the Cities to recover more than the amount spent would give them an unexpected boon. Therefore, the Commission may reasonably find that the actual expenses expended are those that should be recovered.

b. The Cities’ audit docket expenses should be disallowed.

The Cities claim that the audit docket (GUD No. 8784) expenses should be reimbursed because the audit issues could have been included in the complaint docket (GUD Nos. 8749-8754) and that the Cities had to participate in the audit docket to protect their interests in the complaint docket. The Examiner agrees with TSE that the audit docket expenses should be separated from the complaint docket expenses and denied.

Work by the Cities’ attorneys in the audit docket may have been relevant and necessary in the audit docket, but the Examiner fails to see how the audit docket expenses were either part of the complaint docket or were reasonably necessary in the complaint docket. The statute contemplates

⁴ GUD No. 8941, Cities Ex. No. 4; GUD Nos. 8749-8754, Cities Ex. 22, Parts 1 & 2, p. 3.

⁵ *Reply of the Cities to TSE’s Closing Statement*, p. 12; citing *Arthur Andersen & Co. v. Perry Equipment Corp.*, 945 S.W.2d 812, 818 (Tex. 1997); *Borg-Warner Protective Services Corp v. Flores*, 955 S.W.2d 861 (Tex. App.—Corpus Christi 1997); *Strong v. Bellsouth Telecommunications, Inc.*, 137 F.3d 844 (5th Cir.—1998).

⁶ *City of El Paso v. PUC*, 916 S.W.2d 515, 526 (Tex. App.—Austin 1996).

⁷ GUD No. 8941, Cities Ex. No. 4; GUD Nos. 8749-8754, Cities Ex. 22, Parts 1 & 2, p. 3.

⁸ *Texas Southeastern Gas Company’s Closing Statement*, pp. 22-23.

recovery of rate case expenses incurred in presenting a rate case.⁹ Also, Commission Rule 7.57 lists as a factor “whether the work was relevant and reasonably necessary to the proceeding.”¹⁰ The Cities presented a rate case in the complaint docket, but have failed to demonstrate that their costs incurred in the audit docket were necessary in order to present their rate case in the complaint docket.

The Examiner agrees with TSE that the Cities have not shown why its audit docket expenses should be recovered in this complaint docket. As TSE correctly points out, “The Cities can propose, and TSE can contest, reimbursement of the Cities’ audit docket costs in the audit docket itself.”¹¹ The Cities only participated in the audit docket “to protect their interests in the Complaint Dockets.”¹² TSE is correct that this is the rationale rejected by the Austin court of appeals in the *El Paso* cases. Even though the Cities may have needed to participate in the audit docket, this fact does not make the costs of such participation reimbursable in this docket.¹³ These cases support TSE’s argument that the audit docket is a separate proceeding, though related to the complaint docket, and the Cities’ expenses therein are not reimbursable.

⁹ TEX. UTIL. CODE ANN. § 103.022 (Vernon 1998).

¹⁰ 16 TEX. ADMIN. CODE § 7.57 (West 1999).

¹¹ *Texas Southeastern Gas Company’s Closing Statement*, p. 16.

¹² *Closing Statement of the Cities of Brenham, Hempstead, Navasota, Sealy, Tomball, and Waller*, p. 6.

¹³ *Southwestern Public Serv. Co. v. PUC*, 962 S.W.2d 207, 219 (Tex. App.—Austin 1998, pet. den.) (“although the result of a proceeding may eventually affect rates, the proceeding is not a ratemaking proceeding unless it is exclusively devoted to rates.”); *El Paso Electric Co. v. PUC*, 917 S.W.2d 846, 863 (Tex. App.—Austin 1995, writ dismissed by aft., 917 S.W.2d 872) (rejecting expense reimbursement despite fact that “proceedings were so closely connected to ratemaking that [city] had to participate to effectively discharge its statutory duty as a regulator”). *City of El Paso v. PUC*, 609 S.W.2d 574, 576, 578-79 (Tex. Civ. App.—Austin 1980, writ refused n.r.e.) (denying reimbursement of expenses from separate dockets combined for hearing purposes).

TSE also argues that the audit docket is not a “ratemaking proceeding,” and that caselaw dictates that non-ratemaking issues may not be recovered in a ratemaking proceeding. However, the Examiner believes that it is not necessary for the Examiner, or the Commission, to determine, in the complaint docket, whether the audit docket is a “ratemaking proceeding” under TUC 103.022.

The Examiner has subtracted the audit docket expenses of \$21,432 from the total of the Cities’ rate case expenses. As calculated on page 17 of TSE’s Closing Statement, the Cities’ cost of participating in the audit docket is \$21,432. TSE’s Exhibit No. 1 shows the Cities’ discounted cost of participating in the audit docket as \$19,547.50. When multiplied by the ratio of disallowed costs and allowed costs (9.64%), the audit docket total is \$21,432 ($\$19,547.50 + [\$0.0964 \times \$19,547.50]$). The purpose of this ratio was described by the Cities’ expert witness, Glenn Johnson:

there was an allocation made of the amount of time actually allowed and the total amount billed and applied to those expenses that were general expenses not identifiable with specific activities, copy charges, telephone charges, things such as that that would be a charge that would not be specifically identifiable with any specific bill, and that was applied to reduce the expenses proportionally.¹⁴

The Examiner concludes that the audit docket cost of \$21,432 should be disallowed.

c. Expenses directly attributable to the Grimes County Lawsuit should be excluded, while expenses related to the Grimes County Lawsuit, but included in the complaint docket billings, should be allowed.

By agreement, the Cities have not included the Grimes County litigation expenses from their request for recovery of expenses in this docket. However, the Cities have included the Cities’ costs in the Grimes County litigation that were related to the complaint docket and included in the complaint docket billings.¹⁵ TSE does not argue against the Grimes County litigation expenses that were related to the complaint docket. The Examiner believes that the Cities have adequately proven these expenses to be reasonable and recoverable.

d. The Examiner disagrees with TSE’s argument that the Cities are not entitled to reimbursement of their costs relating to the *High Plains* issue in the complaint docket.

TSE argues that the *High Plains* issue is not a “ratemaking proceeding,” and the expenses associated with the issue should be denied.¹⁶ TSE claims that expenses can only be recovered for the rate case portion of the docket, because trial matters that merely affect rates, rather than the actual

¹⁴ Tr. Vol. 1, p. 48.

¹⁵ *Closing Statement of the Cities of Brenham, Hempstead, Navasota, Sealy, Tomball, and Waller*, p. 6.

¹⁶ *Texas Southeastern Gas Company’s Closing Statement*, p. 17.

setting of rates, are not reimbursable.¹⁷ TSE claims that the proper segregation is to deny recovery of one-half of the fees as related to the *High Plains* issue.¹⁸

The Examiner agrees with the Cities that they were required to address the *High Plains* issue as part of the rate case, so the expenses are recoverable. In the complaint docket, the Examiner and the Commission found that the *High Plains* issue must be addressed before the Commission could set rates. In fact, the Examiner ruled that the Cities had the burden of proof on the *High Plains* issue, and TSE had the burden of proof on the cost of service issue.¹⁹ The Commission is not required by law to determine the *High Plains* issue separately from the other issues in the ratemaking proceeding. In fact, the Commission included the issue as a necessary part of the ratemaking proceeding. Because it was a necessary part of the rate case, the expenses related to the *High Plains* issues are reimbursable.

The Examiner's recommendation is consistent with caselaw on the subject. The Cities correctly point out that the more recent *Southwestern Public Service* case²⁰ distinguishes the *City of El Paso* cases cited by TSE.²¹ In the *Southwestern Public Service* case, the court determined that fuel reconciliation proceedings were ratemaking proceedings for purposes of reimbursing city rate case expenses.²² Also, the Cities correctly point out that the determination of the *High Plains* affirmative defense was directly related to the determination of the amount of compensation TSE is able to collect from its customers, consistent with *Southwestern Public Service*.²³

TSE, on the other hand, argues that the same *Southwestern Public Service* case means that the *High Plains* issue expenses are not reimbursable because reimbursement is proper "only when the proceedings are held to set rates, or when otherwise "directly devoted to setting rates" such as a utility's fuel reconciliation application.²⁴ However, the Examiner disagrees with TSE's analysis. The *Southwestern Public Service* case dealt with a fuel reconciliation proceeding which was determined to be a ratemaking proceeding. The court said that even though it was not a "Statement

¹⁷ *Southwestern Public Service Co. v. Public Utility Commission*, 962 S.W.2d 207, 219 (Tex. App.—Austin, 1998, writ denied); *El Paso Electric Co. v. PUC*, 917 S.W.2d 846, 863 (Tex. App.—Austin 1995, writ dismissed by aft., 917 S.W.2d 872) (rate case expenses recoverable only in "Statement of Intent" dockets); *City of El Paso v. PUC*, 609 S.W.2d 574, 576, 578-79 (Tex. Civ. App.—Austin 1980, writ refused n.r.e.) (Denying recovery of expenses despite consolidation with rate case for hearing purposes).

¹⁸ *Texas Southeastern Gas Company's Reply to Cities' Closing Statement*, p. 9.

¹⁹ GUD Nos. 8749-8754, Examiner's Letter No. 13, July 16, 1997.

²⁰ *Southwestern Public Service Co. v. Public Utility Commission*, 962 S.W.2d 207, 219 (Tex. App.—Austin, 1998, writ denied).

²¹ *Reply of the Cities to TSE's Closing Statement*, p. 13.

²² *Southwestern Public Service Co.*, 962 S.W.2d at 217-218.

²³ *See Southwestern Public Service Co.*, 962 S.W.2d at 219-220.

²⁴ *Texas Southeastern Gas Company's Closing Statement*, p. 15, citing *Southwestern Public Service Co.*, 962 S.W.2d at 219.

of Intent” case, the proceeding was a ratemaking proceeding because it would result in an immediate change in the utility customer’s bills.²⁵ Again, the *High Plains* issue is not a separate proceeding, but is a necessary issue in the rate case. As such, the *High Plains* issue was part of the proceeding held to set rates, and the expenses associated with the *High Plains* issue are reimbursable.

The Examiner does not interpret any of the cases cited by the parties to require the Commission to sever out the *High Plains* issue from the rate case for purposes of determining reasonable ratemaking expenses. The first *El Paso* case dealt with a hearing which included both a CCN proceeding and a rate case. The court found that the time spent on the CCN application, which required a separate application at the Commission, was not part of the reimbursable rate case expenses.²⁶ The *High Plains* issue, in contrast, is a necessary issue to this rate case, not a separate application. The second *El Paso* case dealt with separate dockets closely related to a ratemaking proceeding and the issue was whether the separate dockets were ratemaking proceedings. The Commission correctly determined that the separately docketed matters were related, but were not part of the rate case for which expenses were reimbursable.²⁷ The *High Plains* issue, in contrast, is a necessary issue to this rate case, not a separately-docketed matter.

TSE also cites the *Ft. Worth* case as support for its contention that the Commission first had to determine whether TSE’s contracts with the Cities should be set aside, as contrary to the public interest under the *High Plains* standards, before the Commission could have jurisdiction to set TSE’s rates.²⁸ TSE’s argument is that fees and expenses incurred in satisfying the *High Plains* test are not reimbursable because setting aside contracts is not a ratemaking proceeding.

The Examiner does not agree that the *Ft. Worth* case requires the Railroad Commission to institute a separate jurisdictional proceeding to determine the *High Plains* issue before instituting a ratemaking proceeding. The *Ft. Worth* case dealt with a Texas Water Code statute, which required such a jurisdictional finding: “The statute does not allow the agency to institute a rate proceeding without a ‘public interest’ finding, even if all parties request that it do so.”²⁹ Texas Water Code Section 13.043(j) is nearly identical to Texas Utilities Code Section 104.003(a), in its requirement that the Commission ensure that rates are not unreasonably preferential, prejudicial, or discriminatory. After the *Ft. Worth* decision, the Texas Natural Resource Conservation Commission (previously the Texas Water Commission) promulgated rules which set out a “bifurcated” hearing process to determine the “public interest” issue before conducting a hearing on cost-of-service rates.³⁰

²⁵ *Southwestern Public Service Co.*, 962 S.W.2d at 219.

²⁶ *El Paso Electric Co. v. PUC*, 917 S.W.2d 846, 863 (Tex. App.--Austin 1995, writ dismissed by aft., 917 S.W.2d 872).

²⁷ *City of El Paso v. PUC*, 609 S.W.2d 574, 576, 578-79 (Tex. Civ. App.--Austin 1980, writ refused n.r.e.).

²⁸ *Texas Southeastern Gas Company’s Closing Statement*, p. 17; *Texas Water Comm’n v. City of Ft. Worth*, 875 S.W.2d 332, 336-37 (Tex. App.--Austin 1994, writ denied).

²⁹ *Texas Water Comm’n v. City of Ft. Worth*, 875 S.W.2d at 337.

³⁰ 30 TEX. ADMIN. CODE §§ 291.128-291.138 (West 1999).

The Railroad Commission, in contrast, did not hold a bifurcated hearing in the complaint docket, but instead determined the *High Plains* issue as part of its rate proceeding. As part of the proceeding, the Commission determined that *High Plains* was applicable, and made the necessary “public interest” findings as part of its ratesetting Order. Further, nothing in the Railroad Commission’s statutes or rules, or *High Plains* itself, indicates that the Commission is required to hold separate proceedings or determine the “public interest” apart from setting rates. In any event, the *Ft. Worth* decision does not address the issue of whether expenses may be recovered for the “public interest” issue apart from the ratemaking “cost of service” issue.

TSE is correct that failure to segregate costs when a case involves multiple claims, only some of which permit recovery of attorneys fees, can result in the denial of litigation expenses.³¹ However, these cases dealt with separate claims for recovery, whereas it was necessary for the Commission to determine the *High Plains* issue as part of a ratemaking proceeding. The Examiner also made this distinction with the *El Paso* and *Southwestern Public Service* cases above, which dealt with separately docketed applications or matters which are related to each other.³²

Finally, it is difficult, or impossible, to determine from the record which expenses were devoted exclusively to the *High Plains* issue apart from the “cost of service” issue. The Commission asserted jurisdiction in the complaint dockets over the rates and services of TSE, under particular statutes.³³ The only “claim” for which the Cities were seeking relief was the setting of rates, and there were no “multiple claims” for which to separate out expenses. The Commission had no reason to make the *High Plains* findings and set aside the rates in the contracts unless the Commission was setting rates. The Commission’s jurisdiction over contracts is limited to ratesetting issues, unlike the courts, who have jurisdiction to settle contract disputes and award damages based on breach of contract claims. Therefore, the *High Plains* issue should not be considered a separate “claim,” but should be considered part of the ratemaking proceeding.

The Examiner believes that the *High Plains* issue is part of the rate case, rather than a separate proceeding, and therefore cannot be separated. Furthermore, it was necessary for the Cities to address the issue. Therefore, the Cities’ expenses in dealing with the *High Plains* issue should be recoverable.

e. **The Examiner disagrees with TSE’s argument that the City’s fees and expenses are excessive because of inclusion of Gaylord Hughey’s fees and/or when compared to the results achieved or to TSE’s fees and expenses.**

(1.) Hughey’s fees:

³¹ *Green Int’l, Inc. v. Solis*, 951 S.W.2d 384, 389 (Tex. 1997); *U.S. for Use of Wallace v. Flintco Inc.*, 143 F.3d 955, 971 (5th Cir. 1998); *International Security Life Ins. Co. v. Finck*, 496 S.W.2d 544, 546-47 (Tex. 1973); *Texas Southeastern Gas Company’s Reply to Cities’ Closing Statement*, p. 8.

³² See, e.g., *El Paso Electric Co. v. PUC*, 917 S.W.2d 846, 863 (Tex. App.--Austin 1995, writ dismiss’d by aft., 917 S.W.2d 872), in which the hearing included both a CCN proceeding and a rate case, under separate applications.

³³ TEX. UTIL. CODE §§ 102.001, 121.051, and 121.151.

TSE argues that one of the Cities' lawyers, Gaylord Hughey, charged too much to draft a complaint, that Mr. Hughey's work is duplicative, that he lacks experience, and that he was overly expensive.³⁴

First, TSE claims that Mr. Hughey charged too much to perform relatively little work, claiming that "Mr. Hughey spent \$25,166 simply developing and filing a two page *High Plains* complaint. It should not cost more than \$10,000 to develop a two page complaint."³⁵ While TSE makes a strong argument, and the Commission could reduce the amount recovered for individual items, the case cited by TSE is not dispositive of the issue, and TSE does not cite any testimony or evidence to support this claim.³⁶ Even if the facts were supported by the record, TSE has not presented evidence that the amount of Mr. Hughey's time and charges is unreasonable, and only cites the numbers to which Mr. Hughey and Mr. Johnson testified.

Second, TSE claims that Mr. Hughey's work duplicates work done by the Hays Law Firm, and that the Cities have not demonstrated why it was necessary to have two senior lawyers review every document and consult with each other before any action could be taken in the docket. However, the Cities' witness, Mr. Johnson, testified as to the rationale and reasonableness of this arrangement: "Mr. Hughey having the relationship with the Cities and Mr. Hays with perhaps more of an emphasis on expertise in gas utility matters, there was not a great deal of overlap and the Cities benefitted greatly by having the perspectives from both Mr. Hughey and Mr. Hays."³⁷

Third, TSE claims that Mr. Johnson never explained how or why the Cities benefitted or addressed any of the relevant factors, so Mr. Johnson's conclusory testimony is not substantial evidence.³⁸ The court in the *Gulf States* case points out various factors which the Commission should have considered, rather than relying on only the expert witnesses' statements regarding the ratepayers' contribution to depreciation in determining the allocation of proceeds from the sale of a utility.

In its argument on this point, however, TSE does not explain which factors were not addressed by the Cities, or what factors should have been considered instead, as the commission did in the *Gulf States* case. Commission rule 7.57 lists factors which the party claiming reimbursement should address, including, but not limited to:

³⁴ *Texas Southeastern Gas Company's Closing Statement*, pp. 19-22; *Texas Southeastern Gas Company's Reply to Cities' Closing Statement*, p. 10.

³⁵ *Texas Southeastern Gas Company's Closing Statement*, p. 20.

³⁶ *Ripley v. City of Jackson, Miss.*, 2 F. Supp.2d 864, 877 (S.D. Miss. 1997) (reducing time from 2 hours to .5 hours to draft a letter because the attorney recovered for 1.2 hours spent in conference with the same people).

³⁷ Tr. Vol. 1, p. 33.

³⁸ *PUC v. Gulf States Utilities Co.*, 809 S.W.2d 201, 211 (Tex. 1991) (PUC decision, based on testimony of two experts who did not consider all factors and did not explain reasons for conclusions reached, was not supported by substantial evidence).

the amount of work done; the time and labor required to accomplish the work; the nature, extent, and difficulty of the work done; the originality of the work; the charges by others for work of the same or similar nature . . . whether the request for a rate change was warranted, whether there was duplication of services or testimony, whether the work was relevant and reasonably necessary to the proceeding, and whether the complexity and expense of the work was commensurate with both the complexity of the issues in the proceeding and the amount of the increase sought as well as the amount of any increase granted.³⁹

This rule does not necessarily bind the Commission to address every factor, in part because the rule refers to reimbursement under PURA, rather than the GURA statute under which the Cities are claiming reimbursement. Nonetheless, the rule provides the types of factors the Commission may consider.

The Examiner agrees with the Cities, who cite to the testimony of Mr. Johnson, who points out Mr. Hughey's contributions.⁴⁰ The evidence and testimony of Mr. Johnson support Mr. Hughey's work and fees. Also, the Cities point to Cities Exhibit 3A, Appendix B, a compilation of the areas of contribution, as directly gleaned from and supported by Mr. Hughey's billing records. TSE, in contrast, cites no evidence or testimony to refute the Cities' showing that Mr. Hughey's fees were relevant, necessary and reasonable. On cross examination, Mr. White questioned Mr. Hughey about some charges which did not belong in this docket, rather than the reasonableness of the work done by him, or whether it was in fact duplicative of the work done by Mr. Hays.⁴¹ The lack of evidence to the contrary leads the Examiner to the recommendation that Mr. Hughey's fees were reasonable.

TSE recommends disallowing all hours reported by Mr. Hughey for reviewing and consulting on the Hays Law Firm's Commission work, or, in the alternative, a more reasonable amount of review and consultation time, such as 50 hours per year, should be the most that is reimbursed. Nonetheless, the Examiner cannot point to any evidence in the record to support such a recommendation.

Therefore, the Cities have shown Mr. Hughey's fees to be reasonable, and they should be allowed at the discount rate. TSE calculates this to be \$22,065 for Hughey's work done before the hiring of the Hays Law Firm, and \$74,568 for Hughey's work done after the hiring of the Hays Law Firm, a total of \$96,633.⁴² Inasmuch as this amount is included in Cities' Exhibit No. 9, which summarizes the "discounted rate" legal fees for all attorneys, the Examiner recommends recovery of this amount for Mr. Hughey's rates and expenses.

³⁹ 16 TEX. ADMIN. CODE § 7.5 (West 1999).

⁴⁰ Tr. Vol. 1, pp. 33-34.

⁴¹ Tr. Vol. 2, pp. 41-63.

⁴² *Texas Southeastern Gas Company's Closing Statement*, p. 20.

(2.) Comparison to results achieved:

The Examiner disagrees with TSE's argument that the Cities' fees are excessive in relation to the results achieved.

TSE claims that the total reimbursement requested by the Cities is larger than the worth of the rate decrease they achieved. TSE claims that the 1.5 year's worth of volumes remaining to be sold under the Cities' contracts total \$211,343, or \$178,985 when Tomball is excluded, since they are leaving TSE's system. Also, TSE argues that because the Commission set rates below TSE's costs, TSE was forced to immediately file its own rate case, so that the rates set by the Commission will only be in effect for a short time. TSE then argues that the Cities failed to achieve any benefit because they "spent \$278,921 to achieve rate reductions worth approximately \$105,671."⁴³ Finally, TSE claims that the Commission's ordered refunds were not a "value achieved through the litigation" because they were illegally ordered by the Commission.⁴⁴

However, the Cities presented evidence that the complexity and expense of the work was commensurate with the complexity of the issues before the Commission. The Cities correctly characterize Mr. Johnson's testimony as depicting "the amount of work accomplished by the Cities experts, the time and labor required to accomplish the work, the nature, extent, difficulty and originality of the work," as well as the fact that the "matter was vigorously contested and extremely protracted. It involved one of the first times that an informal complaint proceeding had been utilized and raised seldom adjudicated issues of law, such as the *High Plains* issue."⁴⁵

The Examiner finds TSE's argument unconvincing. The purpose of the Cities' petition was to have the Commission set rates. However, the testimony and evidence in this case, as well as its procedural history, indicate that TSE opposed the Commission's exercise of its jurisdiction in this matter, and opposed the setting of rates. In fact, TSE failed to present a rate case to the Commission, and subsequently initiated a "Statement of Intent" rate case to present cost of service evidence it should have presented in the complaint docket. TSE's argument that no benefit was achieved through this complaint case illustrates the Cities' argument that TSE contributed nothing to the setting of rates, and that the Cities' expenses were reasonable, since the Cities did all the work to present the Commission with evidence which could be used to set rates. The Cities argue that TSE used obstructionist tactics and stonewalled in order to drive up the price of getting a rate set, and contributed nothing to the rate case. Therefore, TSE's argument appears to support, rather than refute, the Cities' argument that TSE forced them to spend more than would have been necessary and to take longer than necessary to complete the case, had it not been for the evasive actions of TSE and its failure to present a rate case. The result is that the Cities' expenses are reasonable as those necessary to allow the Commission to set a rate.

⁴³ *Id.*, p. 25.

⁴⁴ *Id.*

⁴⁵ *Closing Statement of the Cities of Brenham, Hempstead, Navasota, Sealy, Tomball, and Waller*, p. 5; Tr., Vol. I, pp. 29-30, 35-36.

(3.) Comparison to TSE’s expenses:

The Examiner found TSE’s comparison of the Cities’ expenses to TSE’s expenses to be unpersuasive. On page 21 of its Closing Statement, TSE suggests that the Cities’ expenses are unreasonable because they are more than those filed by TSE. However, the Cities correctly point out that TSE submitted only the expenses of Rex White, rather than those of Lidell, Sapp, Zivley, Hill & LaBoon (Gary Compton) or Graves, Dougherty, Hearin & Moody (Pete Schenkan, Tom Hudson, and Robin Melvin). Also, TSE did not present a cost of service rate case, which could explain the difference between its expenses and the Cities, who actually presented rate case evidence. Therefore, the Examiner does not find TSE’s argument in this regard persuasive.

Issue No. 2: How should the Cities’ rate case expenses be reimbursed?

Recommendation: The Examiner recommends that each City receive a percentage of the rate case expenses based on the amount of MMBtus taken by each City during calendar year 1996.

The Cities do not recommend any particular method of reimbursement to the Cities. However, TSE proposed a methodology (in its argument that it should be allowed to charge a surcharge to recover any fees ordered to be reimbursed) that can be adapted to the question of how the reimbursement to the Cities should be structured. TSE proposed an allocation based upon the amount of MMBtus taken by each City during the test year of 1996.⁴⁶ The Examiner finds this proposal to be a reasonable method of allocating the reimbursement to each City, absent any alternate suggestion by the Cities. The 1996 gas usage, as calculated by TSE from GUD Nos. 8749-8754 Cities Exhibit No. 1, and the percentage of the \$393,813.79 total, is as follows:

Brenham	625,077 MMBtu	44.365%	\$174,715.48
Hempstead	191,920 MMBtu	13.621%	\$ 53,641.38
Navasota	154,997 MMBtu	11.001%	\$ 43,323.46
Sealy	180,937 MMBtu	12.842%	\$ 50,573.57
Tomball	215,718 MMBtu	15.311%	\$ 60,296.83
Waller	40,304 MMBtu	02.850%	\$ 11,223.69

Issue No. 3: Should TSE be allowed to collect a surcharge to recover the rate case expenses it is ordered to pay to the Cities?

Recommendation: The Examiner recommends that TSE be allowed to recover, through a surcharge, the amount of fees and expenses it reimburses to the Cities.

The Examiner recommends that TSE be allowed to recover, through a surcharge, the amounts reimbursed to the Cities because the costs were incurred, by the Cities, in order for the Commission

⁴⁶ *Texas Southeastern Gas Company’s Closing Statement*, pp. 29-30 and Attachment A; GUD Nos. 8749-8754, Cities Ex. 1, Schedule TAG-6.

to set rates. The Examiner recommends that the Commission consider the amount TSE is required to pay the Cities to be a “reasonable and necessary operating expense” which may be recovered through a surcharge. A surcharge is a “rate” under the definition found in TUC Section 101.003(12). As such, the surcharge may be recovered by TSE by billing its customers. It is Commission practice to treat the reimbursed expenses as a reasonable cost of service of the gas utility and to authorize the gas utility to recover the reimbursed rate case expenses in a surcharge to its rates.

TSE claims that it may recover amounts paid to the Cities through a surcharge, under TUC Section 104.051, which requires the Commission to “establish the utility’s overall revenues at an amount that will permit the utility a reasonable opportunity to earn a reasonable return on the utility’s invested capital used and useful in providing service to the public in excess of its reasonable and necessary operating expenses.”⁴⁷ Nonetheless, the Commission’s authority is tempered by Section 104.052, which prohibits the Commission from establishing “a rate that yields more than a fair return on the adjusted value of the invested capital used and useful in providing service to the public.”⁴⁸ Still, the Commission may reasonably consider the amount reimbursed to the Cities to be a reasonable cost of having TSE’s rates set by the Commission.

Although it may appear to be a circuitous transaction to allow TSE to charge back to the Cities the amounts it reimburses them, the surcharge may instead be a mechanism by which the Cities may immediately recover their reasonable expenses, and TSE may recover the funds over time through a surcharge to the Cities, which the Cities may pass along to the end-use customers if they so choose. Ultimately, the funds will come from the end-use customers through the Cities to TSE, whether it is from the Cities’ coffers or from a pass-through of costs to the end-use customers.

In addition, the Examiner recommends that the Commission approve TSE’s recovery of the amount reimbursed to the Cities because TSE claims that denial of such recovery would impair TSE’s opportunity to earn any return on its invested capital and recovery of its reasonable and necessary expenses: “Obviously, TSE must first recover its reasonable and necessary operating expenses before it will have any opportunity to earn a reasonable return.”⁴⁹ TSE points out that Mr. Johnson could not identify a single fully contested case in which rate case expenses required to be paid to a city were not recovered by the utility through rates.⁵⁰ To deny TSE recovery of the amounts paid to the Cities could be inconsistent with previous Commission practice and would impair TSE’s ability to recover its expenses.

TSE also argues that the Commission may not deny TSE’s recovery of amounts paid to the Cities as a punishment or equitable remedy for abuse of the process. TSE argues that GURA does not “authorize the Commission to disallow cost recovery whenever the Commission determines that equity favors such action or that denying cost recovery would promote compliance with the Act.”⁵¹

⁴⁷ TEX. UTIL. CODE ANN. § 104.051 (Vernon 1998).

⁴⁸ TEX. UTIL. CODE ANN. § 104.052 (Vernon 1998).

⁴⁹ *Texas Southeastern Gas Company’s Closing Statement*, p. 2.

⁵⁰ *Id.*; Tr. Vol. 1, pp. 185-186.

⁵¹ *Texas Southeastern Gas Company’s Closing Statement*, p. 13.

Instead, TSE argues that GURA provides that a utility can recover all reasonable and necessary operating costs, and does not create an exception for the litigation costs of successful complainants: “GURA already contains penalty provisions to promote compliance with the law and Commission regulations. No new authority is necessary or permissible in light of the Commission’s existing express authority.”⁵²

The Cities argue that the Commission is not *required* to allow TSE the right to bill back to the Cities reimbursed expenses⁵³ and the Examiner agrees with that argument. However, the Commission has been given the authority to determine whether or not certain costs of providing utility services are “reasonable” and whether any expenses incurred by the utility should be recovered through its rates. The Commission is required to allow TSE the opportunity to recover its reasonable and necessary operating expenses, but it has the authority to determine the reasonableness of those expenses, so it is not bound as TSE implies. Instead, the Commission has discretionary authority to determine what expenses are reasonable and necessary.

In addition, the Cities recommend that the Commission follow a “loser pays” policy and determine that the reimbursed amounts are not reasonable and necessary and, therefore, may not be recovered by TSE. The Commission could determine that the amount TSE is required to reimburse the Cities is not a reasonable rate case expense for TSE because of its failure to present a rate case, and deny TSE recovery of those expenses.

The Examiner recommends against this option, because TSE argues that a Commission order requiring TSE to pay the Cities’ requested legal fees without a surcharge would render TSE insolvent and could harm TSE’s other customers. TSE further argues that such an order would render the Commission’s rate orders in GUD Nos. 8749-8754 confiscatory and unlawful.⁵⁴ TSE points to its actual operating income and expenses from 1996, the test year in GUD Nos. 8749-8754, where TSE shows a loss of \$43,319.⁵⁵

The Cities claim that TSE should not be allowed to recover the amounts paid to the Cities because of TSE’s abusive and obstructionist tactics. The Cities argue that the Commission should

⁵² *Id.*, citing *Cobra Oil & Gas Corp. v. Sadler*, 447 S.W.2d 887, 892 (Tex. 1968); *Cole v. Texas Army National Guard*, 909 S.W.2d 535 (Tex. App.–Austin 1995, writ den.). The *Cobra* case involved a mandamus action by a mining corporation to require the Commissioner of the General Land Office to accept its tender of rentals. The Supreme Court held that the statutory methods for declaring a forfeiture provided the only method for such a declaration. Similarly, *Cole* does not stand for TSE’s proposition. The *Cole* case involved a suit by a Texas Army National Guard officer for declaratory relief and ancillary relief on the basis that his discharge from the Guard was illegal. In that case, a statute required that a discharge based on cause required a cause determination by a court martial or by an “efficiency board legally convened for that purpose.” Since that determination had not been made, and the method of the exercise of authority was prescribed, the discharge was not proper.

⁵³ *Reply of the Cities to TSE’s Closing Statement*, p. 8.

⁵⁴ *Texas Southeastern Gas Company’s Reply to Cities’ Closing Statement*, p. 2.

⁵⁵ TSE Annual Report to Railroad Commission, p. 10, line 20. In GUD Nos. 8749-8754, the Examiner took official notice of the Annual Report. GUD Nos. 8749-8754, Tr. 8/15/97, p. 5.

adopt a “loser pays” policy for this case, rather than following the “American Rule.”⁵⁶ The American Rule is that every party pays its own legal costs unless and except to the extent a statute provides otherwise, or a court grants a sanctions motion.⁵⁷

In this case, though, the Commission has at least two different statutes which allow the Commission to determine reasonable rate case expenses for both the Cities and TSE.⁵⁸ Therefore, the Commission is not bound by either of these rules. Rather, the Commission has the authority to determine the reasonableness of the expenses and the amount allowed to be recovered by both parties.

The Cities correctly point out that the issue is “whether or not TSE’s reimbursement to the Cities should be considered a reasonable expense of TSE for ratemaking purposes, which, in the discretion of the Commission, should be billed by TSE back to the very Cities to whom it is paid.”⁵⁹ The Cities argue that the Commission should require TSE to “stand the cost of the litigation required to bring it to justice,” due to “TSE’s tactics, its refusal to even put on a rate case, and the findings that it was engaged in discriminatory and anti-competitive practices and was charging excessive rates.”⁶⁰ Specifically, the Cities cite TSE’s failure to participate in informal settlement discussions, timely produce discovery, and file adequate testimony.⁶¹

However, TSE denies the Cities’ allegations of TSE’s abuse of the hearing process in its Closing Statement and Response to Cities Closing Statement.⁶² Though the record indicates that TSE made it difficult for the Cities to prosecute their case by throwing up roadblocks, the Examiner at the time made no official finding of abuse of the process by TSE. The Commission did, however, find in GUD Nos. 8749-8754 that TSE engaged in discriminatory practices and was charging excessive rates. TSE’s failure to present a rate case resulted in rates which TSE claims are too low, and it filed a Statement of Intent rate case a mere three months after the completion of the complaint docket. While the Commission could deny TSE’s recovery of the amounts reimbursed to the Cities and base its decision on TSE’s failure to present a rate case, the Examiner does not recommend such action.

Because the Examiner is recommending that the Cities be reimbursed for their *reasonable* expenses, the Examiner also recommends that TSE be allowed to collect a surcharge so that it can be reimbursed for those reasonable expenses as a part of the cost of providing utility service.

⁵⁶ *Closing Statement of the Cities of Brenham, Hempstead, Navasota, Sealy, Tomball, and Waller*, p. 8.

⁵⁷ *Travelers Indem. Co. of Conn. V. Mayfield*, 923 S.W.2d 590, 593 (Tex. 1996). *Texas Southeastern Gas Company’s Closing Statement*, p. 14.

⁵⁸ TEX. UTIL. CODE ANN. § 103.022 (Vernon 1998); TEX. UTIL. CODE ANN. § 104.051 (Vernon 1998).

⁵⁹ *Reply of the Cities to TSE’s Closing Statement*, p. 15.

⁶⁰ *Id.*

⁶¹ *Id.*, pp. 15-17.

⁶² *Texas Southeastern Gas Company’s Reply to Cities’ Closing Statement*, pp. 3-7.

Issue No. 4: If the Commission approves a surcharge, how should it be structured?

Recommendation: If the Commission approves a surcharge, the Examiner recommends that the Commission approve an allocation based upon each City's consumption during the first year during which Commission-set rates applied and that the recovery be spread over a two-year period.

a. Allocation of surcharge amount:

If the Commission approves a surcharge, the Examiner recommends that the Commission authorize TSE to allocate a percentage of the total surcharge to each City based on the volume used by each from May 1, 1999 to May 1, 2000. In this manner, each City will be required to pay its share of the surcharge that is based on the benefit each received from the rate reduction that was approved by the Commission in April 1999.

TSE recommends that the Commission determine that the surcharge be recovered from each City according to the MMBtus of gas either purchased by, or transported for, each City in 1996.⁶³ While the Examiner recommends this method of determining the amounts TSE must pay each City, the Examiner believes that using the percentage of gas each City either purchased or had transported from May 1, 1999 to May 1, 2000 is a more fair and accurate method of matching the surcharge amounts to the benefits received by each City from the rate reduction achieved in the complaint docket.

Though this method might result in different amounts charged to the Cities than they recover from TSE, the Examiner finds it fair, absent any evidence on the amount of expenses paid by each City. In this way, the Cities will recover their expenses based on 1996 amounts, which represent each City's relative risk at the time they filed the complaint. In like manner, each City will be required to reimburse TSE an amount based on the benefit each received through the rate reduction received, which should indicate the reasonableness of each City's investment in the complaint docket.

b. Timing of surcharge:

The Examiner recommends that TSE be allowed to charge the surcharge over a two-year period, rather than before September 30, 2000, as recommended by TSE.

TSE requests that the surcharge be designed to allow recovery from Brenham, Hempstead, Navasota, and Sealy before September 30, 2000, when the primary terms of the contracts expire, in order to ensure that TSE is actually allowed the opportunity to recover its reasonable and necessary expenses. TSE also points out that the primary term of TSE's contracts with Tomball and Waller

⁶³ *Texas Southeastern Gas Company's Closing Statement*, pp. 29-30 and Attachment A; GUD 8749-8754, Cities Ex. 1, Schedule TAG-6.

have already expired, and those cities are in year-to-year extensions. In addition, the record shows that Tomball intended to cease being a TSE customer.⁶⁴

Nonetheless, the Examiner recommends that the surcharge be authorized for a two-year period, to be paid in equal monthly installments. TSE has not shown whether the Cities' contracts will be renewed, or whether TSE is in danger of losing the Cities as customers after their contracts expire. Therefore, the Examiner can find no compelling reason to force recovery of all of the surcharge by September 30, 2000. Instead, the Examiner recommends recovery of the surcharge over a two-year period, so that the surcharge is not too large a percentage of each Cities' overall bill.

It is impossible to determine exactly what surcharge amounts would result for each City from the Examiner's recommendation, as the 1999-2000 total volumes are not in the record; however, it is possible to calculate an estimate of the distribution by using the 1996 volumes which are in the record. Using those volumes to calculate estimates, the surcharge that would be allocated to each City is approximately 2/3 of that portion of the annual bill for each City which results from the \$.425 per MMBtu component of the new rates approved in April 1999, without the "index" component of the rate. If the surcharge is charged from June through September 2000, the monthly amount of the surcharge would be significantly higher than that portion of the monthly bills. If the surcharge is spread out over two years, however, it will be only about 1/3 of that portion of each City's annual bill, which is more reasonable, considering that the end-use customers are the ones who ultimately pay the costs of the service provided to them.

Using the Examiner's recommended rate case expenses of \$393,813.79, and using 1996 volumes for purposes of estimating 1999-2000 volumes, the Examiner calculated the estimated surcharge and the above-described portion of each City's estimated annual bill for the year from May 1, 1999 to May 1, 2000 as follows:

Brenham: Brenham's share of costs equals \$174,715.48 (.44365 X \$393,813.79).
The estimated 1999-2000 bill is \$265,657.72/yr (625,077MMBtu
[Brenham's 1996 annual volume] X \$.425/MMBtu).

Hempstead: Share of costs: .13621 X \$393,813.79 = \$53,641.38
Estimated annual bill: 191,920 MMBtu X \$.425/MMBtu = \$81,566

Navasota: Share of costs: .11.001 X \$393,813.79 = \$43,323.455
Estimated annual bill: 154,997MMBtu X \$.425 = \$65,873.73

Sealy: Share of costs: .12842 X \$393,813.79 = \$50,573.57
Estimated annual bill: 180,937 MMBtu X \$.425 = \$76,898.23

Tomball:* Share of costs: .15311 X \$393,813 = \$60,296.83

⁶⁴ *Texas Southeastern Gas Company's Closing Statement*, p. 29.; GUD 8749-8754 Tr. 8/14/97, p. 107.

Estimated annual bill: 215,718 MMBtu X \$.425 = \$91,680.15

Waller: Share of costs: .02850 X \$393,813 = \$11,223.693
Estimated annual bill: 40,304MMBtu X \$.425 = \$17,129.20

* Tomball and TSE have indicated to the Examiner in GUD No. 8881⁶⁵ that Tomball left TSE's system on March 12, 2000. Therefore, it received the benefit from the lower rates only until March 12, 2000, and its share of the surcharge will most likely be slightly smaller.

Because the volumes used from May 1, 1999 to May 1, 2000 are not in the record, TSE should be required to calculate the percentage of gas used by each City for that time period, and should be authorized to charge a surcharge to each City based on that percentage.

TSE requests that it be ordered to reimburse each City's costs as funds are received. TSE also requests that the order require TSE to track the recovery of the costs assigned to each City, and require TSE to pay all amounts received through the surcharge from each City over to the City as they are received and to cease imposing the surcharge once the costs assigned to a specific City have been recovered from that City. The Examiner does not find this recommendation reasonable, because it delays the Cities' reimbursement of expenses already spent. Also, there is no support in the record for such a provision. TSE did not present sufficient evidence to establish that its financial condition necessitates tying the timing of reimbursements to collection of surcharges.

c. Exit fee provision:

In the case of Tomball and Waller, TSE requests that the order provide that upon a substantial reduction in the use of TSE's system, the City so reducing its usage should pay an exit fee - a lump sum equal to any remaining rate case expenses that have not been recovered through a surcharge.⁶⁶

The Examiner recommends against the imposition of an exit fee. Though TSE is attempting to assure its recovery of its expenses, there is no support for such a charge in the record. TSE is allowed "a reasonable opportunity to earn a reasonable return . . . in excess of its reasonable and necessary operating expenses,"⁶⁷ not an assurance that it will do so.

Because Tomball has already left TSE's system, TSE's method of calculating a surcharge for Tomball based on the MMBtus used each month, and the use of an exit fee, is unworkable. TSE offered no alternative method of calculating and recovering its surcharge from Cities that leave its system. Instead, the Examiner recommends calculating Tomball's portion of the surcharge based on its usage from May 1, 1999 to March 12, 2000, and authorizing TSE to charge a surcharge over two years in equal installments to allow it the opportunity to recover its costs.

⁶⁵ Tex. R.R. Comm'n, *Application of Texas Southeastern Gas Company for Approval of Abandonment of Services to the City of Tomball*, Gas Utilities Docket (GUD) No. 8881.

⁶⁶ *Texas Southeastern Gas Company's Closing Statement*, p. 30.

⁶⁷ TEX. UTIL. CODE ANN. § 104.051 (Vernon 1998).

d. Tracking of TSE's cost recovery:

TSE recommends that the order require TSE to track the recovery of the costs assigned to each City. The Examiner finds this recommendation reasonable and has included it in the draft order.

Issue No. 5: Should TSE be allowed to recover its attorneys fees from the Cities?

Recommendation: The Examiner recommends that TSE not be allowed to recover its attorney's fees.

The Examiner recommends that the Commission deny TSE's request for recovery of its attorney's fees because they were not requested or contemplated in GUD Nos. 8749-8754, the Commissioners probably did not intend to remand the issue for hearing, and even if they did, TSE's attorneys fees are not reasonable and necessary expenses for ratesetting purposes.

In support of its request for reimbursement of its attorneys fees from the Cities, TSE cites the statutory requirement that the Commission shall establish the utility's overall revenues at an amount that will permit the utility a reasonable opportunity to earn a reasonable return on the utility's invested capital used and useful in providing service to the public in excess of its reasonable and necessary operating expenses.⁶⁸ The Examiner agrees with TSE that the Commission has the statutory authority to allow TSE to recover its attorneys fees through its rates. However, the Examiner recommends against such action, as discussed below.

a. Failure to raise claim in previous docket - Res Judicata:

The Cities argue that TSE's recovery of its rate case expenses is "barred by the doctrines of merger and bar that hold that a final order disposes of all claims that were brought or should have been brought in the case."⁶⁹ TSE, on the other hand, claims that the doctrine of *res judicata* does not preclude subsequent litigation of claims that the first court severed or separated for trial.⁷⁰ Since the Commission's Order in GUD No. 8749 states that "all issues related to reimbursement of rate case expenses are hereby severed from this case for consideration in another docket,"⁷¹ TSE claims that merger and bar are "part and parcel" of the doctrine of *res judicata*, and the doctrine of *res judicata*

⁶⁸ TEX. UTIL. CODE ANN. § 104.051 (Vernon 1998).

⁶⁹ *Closing Statement of the Cities of Brenham, Hempstead, Navasota, Sealy, Tomball, and Waller*, p. 10, n. 5.

⁷⁰ *Van Dyke v. Boswell, O'Toole, Davis & Pickering*, 697 S.W.2d 381, 384 (Tex. 1985) (malpractice action could proceed despite fact that it could have been tried in prior divorce action and malpractice issues were discussed in divorce action); *S.O.C. Homeowners Ass'n v. City of Sachse* 741 S.W.2d 542, 544 (Tex. App.–Dallas 1987, no writ) (*res judicata* "cannot preclude litigation of claims that a court expressly separates or severs from that action."); Restatement (Second) of Law of Judgments § 26(1)(b); Restatement (Second) of the Law of Judgments § 26(1)(b); See also *Jones v. Rainey*, 168 S.W.2d 507, 509 (Tex. Civ. App.–Texarkana 1943, writ ref'd) (failure to request damages issue in first trial did not preclude raising the issue in second trial).

⁷¹ GUD No. 8749, Ordering paragraph on p. 19 of Order; *Also see* Finding of Fact 156 (severing "all issues relating to reimbursement of rate case expenses"); and Conclusion of Law 35 (same language).

does not preclude the issue of TSE's reimbursement in this docket.⁷² In this case, TSE did not expressly raise the issue or make a claim for reimbursement of its expenses in GUD Nos. 8749-8754, and no such issue was presented to the Commission for consideration, so no such issue was explicitly remanded by the Commission.

The Examiner agrees with TSE that the doctrine of *res judicata* does not bar TSE's attempt to raise the issue of TSE's reimbursement of its attorneys fees because the entire issue of reimbursement of attorneys fees was not determined by the Commission, but was instead remanded for hearing in a separate docket. If the Commission had determined the issue of attorneys fees, TSE would be barred from bringing its claim for attorneys fees by *res judicata* even though TSE failed to raise the issue in GUD Nos. 8749-8754, because *res judicata* also applies to claims which should have been raised in the first trial. In this case, the doctrine of *res judicata* does not bar TSE's attempt to raise the issue of TSE's reimbursement of its attorneys fees.

b. Commission's intent:

It is unclear whether, on remand, the Commissioners intended to gather evidence on a claim by TSE for recovery of attorneys fees. The Commission may limit its remand to any issues the Commission deems fit. As noted above, the Commission's Order in GUD No. 8749 states that "all issues related to reimbursement of rate case expenses are hereby severed from this case for consideration in another docket."⁷³

The Examiner believes that the Commissioners were not contemplating TSE's recovery of its own attorney's fees in the remand, because the issue had not been raised by TSE in GUD Nos. 8749-8754, and the Commissioners demonstrated no intent to hear evidence and arguments on TSE's recovery of its attorney's fees. The Examiners' PFD in GUD Nos. 8749-8754 dealt with only the Cities' request for rate case expenses, as they were the only parties who raised the issue, and TSE did not request reimbursement of its expenses. At the March 23, 1999 Conference, Commissioner Matthews moved to "take the rate case expenses and separate them from this part of the case unless somebody can stand up here and tell me that you've got a real good feel of what those dollar amounts are." Therefore, the Examiner can find no intent demonstrated by the Commission to expand the scope of the issues presented to the Commissioners. Rather, it appears that they simply needed dollar amounts for the Cities' rate case expenses.

The Cities point to the Notice of Hearing as evidence of the Examiner's intent to limit issues to the Cities' reimbursement. The Notice of Hearing states that "In this docket, the Commission will consider rate case expense issues severed from Gas Utilities Docket Nos. 8749-8754."⁷⁴ While the Notice of Hearing may demonstrate the Examiner's mindset at the time of issuance of the Notice, the Notice is not necessarily dispositive of all of the issues that will ultimately be considered. Also, the Notice is ambiguous enough to include TSE's request for reimbursement. However, the Examiner

⁷² *Texas Southeastern Gas Company's Reply to Cities' Closing Statement*, p. 12.

⁷³ GUD Nos. 8749, Ordering paragraph on p. 19 of Order; *Also see* Finding of Fact 156 (severing "all issues relating to reimbursement of rate case expenses"); and Conclusion of Law 35 (same language).

⁷⁴ GUD 8941, Notice of Hearing (June 10, 1999).

believes that the Commission's intent was not to hear an additional issue, but to get evidence on the Cities' request for reimbursement of rate case expenses. The Commission may determine that they never intended to hear a claim by TSE for attorneys fees, and deny the claim. However, the Examiner has provided an analysis of the evidence on TSE's claim for reimbursement below, if the Commission wishes to consider it.

c. Fairness of recovery by TSE:

The Examiner recommends that the Commission deny TSE's request for reimbursement of attorneys fees and expenses because they were not reasonably spent in pursuit of ratemaking, and are therefore not reasonable operating expenses. The Examiner recommends that it would be inherently unfair and unreasonable to have the Cities bear both their own expenses and TSE's. The Examiner is recommending that TSE recover, through a surcharge, the amount that it must pay the Cities in rate case expenses. In this manner, TSE will recover the expenses which were reasonably expended by the Cities in prosecuting this docket. As the Cities point out, TSE did everything it legally could to prevent rates from being set, rather than asking the Commission to set rates. TSE should not, therefore, be allowed to also recover its own attorney's fees which were expended to try to prevent the Commission from setting rates. Since the end-use customers are the ones ultimately footing the bill, it is not reasonable to allow TSE to recover its own attorneys fees for a rate case it failed to present.

First, TSE did not comply with the Examiner's ruling which assigned TSE the burden of proof on the cost of service issue. In GUD Nos. 8749-8754, on July 16, 1997, in Examiner's Letter No. 13, the Examiner issued a ruling assigning the burden of proof to Cities on the issue of discrimination and to TSE on the issue of cost of service. That ruling also established a schedule for prefiled written testimony consistent with the assignments of the burden of proof. On July 18, 1997, TSE filed with the Commissioners an *Interlocutory Appeal and Motion for Stay*, which appealed the ruling on burden of proof. According to rule § 1.30 of the Commission's General Rules of Practice and Procedure, TSE's appeal of the ruling assigning the burden of proof was filed timely and was denied by operation of law on September 2, 1997. TSE still argued against the decision on the burden of proof in its Closing Statements in GUD Nos. 8749.⁷⁵ Then TSE failed to present a cost of service rate case. Even Commissioner Matthews stated at Conference that "It's been difficult for the Commission to deal with this case because Texas Southeastern did not put on a rate case, and so it made it hard for us to try to decide what was the fairest thing to do."⁷⁶ Therefore, TSE's costs incurred in this proceeding are not reasonable and necessary operating costs.

The Cities argue that TSE pushed up the Cities' costs by failing to present its own rate case, while laying behind the log, waiting to file its own rate case after the Cities had finally achieved a Commission-set rate. In fact, TSE filed a rate case, GUD No. 8958, three months after losing the complaint case. Therefore, the Cities are still expending more funds to fight TSE's proposed rate increase. TSE also claims that the Cities have presented no evidence that demonstrates how their

⁷⁵ GUD Nos. 8749-8754, *Exceptions of Texas Southeastern Gas Company to the Proposal For Decision and Request for Oral Argument*, pp. 5-10.

⁷⁶ Commission Conference, March 23, 1999.

costs would have been different had TSE presented a rate case. Nonetheless, the Cities presented cost of service evidence in GUD Nos. 8749-8754, while TSE did not, and TSE's failure to present a rate case in GUD Nos. 8749-8754 is still costing the Cities money to protect their interests in GUD No. 8958.

Therefore, TSE's legal expenses should not be reimbursed, because they were not reasonably expended in the setting of rates before the Commission. Rather, TSE pursued the *High Plains* issue in an attempt to deny the Commission jurisdiction over rate setting. The Commission set rates largely because of the Cities' efforts and expense, not TSE's. Therefore, the Examiner recommends that the Commission deny TSE recovery of its attorney's fees from the Cities.

If the Commission decides to allow TSE to recover its attorneys fees from the Cities, the Examiner has concluded that TSE demonstrated that their attorneys fees and expenses are \$149,188.12. If the Commission wishes to allow TSE reimbursement of only their expenses spent litigating the *High Plains* issue, TSE argues that it spent half that amount on the *High Plains* issue, or \$74,594.06.

IV. Conclusion

Based upon the evidence presented and after considering the arguments of the parties, the Examiner recommends that TSE be required to reimburse the Cities for their reasonable rate case expenses of \$393,813.79 and that TSE be allowed to recover that amount through a surcharge over a two-year period. The Examiner does not recommend that TSE be allowed to recover its attorneys fees.

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