

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA



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In the matter of the Application of the Golden State Water Company (U133W) for an order authorizing it to increase rates for water service by \$20,327,339 or 20.12% in 2010; by \$2,646,748 or 2.18% in 2011; and by \$4,189,596 or 3.37% in 2012 in its Region II Service Area and to increase rates for water service by \$30,035,914 or 32.67% in 2010; by \$1,714,524 or 1.39% in 2011; and by \$3,664,223 or 2.92% in 2012 in its Region III Service Area.

And Related Matters.

Application 08-07-010  
(Filed July 1, 2008)

Application 07-01-014  
(Filed January 5, 2007)

**APPLICATION FOR REHEARING OF  
THE DIVISION OF RATEPAYER ADVOCATES  
OF DECISION 10-11-035**

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BEFORE THE PUBLIC UTILITIES COMMISSION  
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In the matter of the Application of the Golden State Water Company (U133W) for an order authorizing it to increase rates for water service by \$20,327,339 or 20.12% in 2010; by \$2,646,748 or 2.18% in 2011; and by \$4,189,596 or 3.37% in 2012 in its Region II Service Area and to increase rates for water service by \$30,035,914 or 32.67% in 2010; by \$1,714,524 or 1.39% in 2011; and by \$3,664,223 or 2.92% in 2012 in its Region III Service Area.

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DECISION 10-11-035**

**I. INTRODUCTION**

Pursuant to Rule 16.1 of the Rules of Practice and Procedure of the California Public Utilities Commission the Division of Ratepayer Advocates (“DRA”) hereby submits its Application for Rehearing of Decision 10-11-035. DRA raised a number of the concerns it addresses below in its comments on both the proposed decision and the alternate proposed decision, however, the latter document was subsequently adopted without major modification. As a result some of the legal and factual errors DRA noted in its earlier comments remain outstanding in D.10-11-035. Moreover, while DRA is aware that prior Commission decisions cannot bind future Commissions, D.10-11-035 varies so markedly from prior Commission rulings on several issues, that it appears to be arbitrary and capricious and thus legally invalid. Specifically D.10-11-035’s holdings on the issue of recovery of regulatory commission expenses, the La Serena plant upgrades

and four factor expenses are particularly troubling. If this decision is allowed to stand the Commission will have substantially modified its policy on four-factor allocations, the treatment of regulatory commission expenses and how it applies Rule 15 all without a compelling rationale or a solid evidentiary basis. Moreover, the Commission needs to recognize that in many particulars, D.10-11-035 has *de facto* modified the rate case plan decision to the detriment of the Commission's review process. In short, these flaws require the Commission to rehear this decision and provide consistent policy guidance to future Commission analysts and administrative law judges.

## **II. THE COMMISSION IMPROPERLY APPLIED TARIFF RULE-15 REGARDING THE LA SERENA PLANT EXPANSIONS**

Decision 10-11-035 errs in allocating approximately 30% of the cost of the new facilities developed to serve new customers to existing ratepayers. GSWC's Tariff Rule-15 states that if at least 50% of the new facilities' design capacity is required to supply the main extension, the cost of such facilities may be included in the advance:

If special facilities consisting of items not covered by Section C.1.a. are required for the service requested and, when such facilities to be installed will supply both the main extension and other parts of the utility's system, at least 50% of the design capacity (in gallons, gpm, or other appropriate units) is required to supply the main extension, the costs of such special facilities may be included in the advance, subject to refunds, as hereinafter provided, along with refunds of the advance of the cost of the extension facilities described in Section C.1.a. above." Rule 15 Section C.1.b. Revised Cal. P.U. Sheet No. 393-W.

In D.05-12-020, p. 18, the Commission recognized that the cost of all necessary facilities including wells, tanks, and treatment facilities should be recovered in the facilities charge, and not imposed on the existing customer base:

"Constructing all the provisions of Apple Valley's Rule 15, we conclude that the cost of all necessary facilities to serve new customers, including wells, tanks and treatment facilities, when clearly attributable to new customers, should be recovered in facilities charge, and not imposed on the existing customer base."

While DRA recognizes that prior Commission's cannot bind future Commissions with their decisions, this does not mean that the Commission has a carte blanche to overturn the precedent set by earlier rulings as a matter of caprice or whim. While the language of Rule 15 uses the word "may" instead of "shall" in describing when advance payments from developers will be sought to pay for upgrades or expansions, until the instant case the Commission has required developers to pay all or virtually all of these costs in prior decisions. Given this history, if the Commission decides to modify a long-standing practice, the change needs to be based on a solid evidentiary basis and/or changes in circumstances that justify the adoption of a new policy direction. Neither of those situations applies to the La Serena expansion. The record is unambiguous that over 50% of the La Serena Plant will be devoted to serving new customers and/or the fire flow needs of a new school that was built to accommodate the children of those new customers. Moreover, the Decision does not cite any change in circumstances that justify this change in interpretation of Rule 15.

The Commission should be mindful that it risks sowing confusion in the water industry if it changes its interpretation of Rule 15 over time. The water utilities have successfully operated and earned ample profits for decades under the former interpretation of this Rule. Indeed in D.75205 (1969) the Commission initially revised Tariff Rule 15 into its current form. In that case the Commission rejected the efforts of developers to shift the cost of serving new customers to existing ratepayers instead of the developers. This sound policy has guided the Commission for the past four decades, however, this policy has been modified in D.10-11-035 apparently due to intense ex parte lobbying by GSWC, rather than being based on a compelling evidentiary grounds or a clear cut legal rationale. In short, this change in policy is the type of "arbitrary and capricious" decision that appellate courts find suspect and frequently overturn.

Simply put the Decision commits legal error by not assigning the entire cost of the La Serena Plant to the developers in the form of a facility charge. In assigning 29.4% of the cost of the facility to Golden State's existing customers, the Decision is also factually inconsistent in that although it accepted DRA's analysis (that demonstrated that 70.6% of

the La Serena facilities will be used to serve new customers), it incorrectly applied the Rule 15 requirement that when greater than 50% of the cost of the new facilities are attributable to the need to serve new customers, developers are required to pay for all of the expenses of the upgrade. The language of Rule 15 is unambiguous. Since greater than 50% of the La Serena facility will serve new customers, under Rule 15 all of the expenses of building this facility should be levied on the developers via a facilities charge.

The 50% Rule discussed above is part of Standard Practice U-17. The Standard Practice was created as a result of Rulemaking 90-07-004. Nothing about the La Serena project provides grounds for deviating from the long-standing Commission practice of attributing the cost of these types of new facilities to developers, not existing customers.

#### **A Calculation Error in the Final Decision**

DRA notes that footnote 24 of the Decision miscalculates the amount of refund for the La Serena Plant. The decision requires GSWC to issue a one-time credit of \$582,832. However, the decision – even if it uses DRA’s formula for calculating this credit - made a computation error because it assumes the La Serena Plant was only in ratebase from January 2008 through January 2009 when in fact almost three years have elapsed since it first entered ratebase. Thus, the correct time factor is 2.91 years. (January 2008 through November 2010). Using the correct time factor and the adjusted cost of \$1,843,956 the correct credit value is \$848,021 and not \$582,832 as follows:  $\$848,021 = 2.91 \text{ years} \text{ times } (\$1,843,956 \text{ disallowed cost times } .0887 \text{ rate of return times } 1.78172 \text{ net-to-gross multiplier})$ .

### **III. THE COMMISSION’S APPROACH TO FOUR-FACTOR ALLOCATIONS FOR THE NUMBER OF CUSTOMERS IS INCONSISTENT WITH PRIOR DECISIONS**

In issuing decisions on general rate case applications the Commission needs to be mindful of a number of factors including whether the decision either directly or indirectly overturns prior Commission policies or practices that have guided both the utilities and DRA in reviewing utility applications. In D.10-11-035, the Commission accepted

GSWC's argument that services provided to the federal government on military bases through its affiliated companies should be counted as a single customer since GSWC's affiliates do not deal with individual customers on the bases. In reaching this conclusion, the Commission ignored the approach it used in D.03-05-078 wherein it rejected Suburban's argument to use "zero" as the number of customers Suburban's affiliates (that are part of Southwest) serve under its service contracts on various military bases. Instead the Commission decided to allocate costs based on three instead of four-factors thereby removing the number of customers served as a consideration in how costs were allocated.

Similarly, in D.07-10-034, one of GSWC's prior rate case decisions, the Commission cited D.03-05-078 and stated that traditional four factor allocations premised on the notion that contracts to serve military bases are tantamount to a single customer are biased against GSWC's captive ratepayers. In D.07-10-034, the Commission established an "Equivalent Number of Customer" factor which attached a lower weight (but not zero weight) to customers served under military contracts on the rationale that individual customers on the bases do not receive full utility services from GSWC's affiliates even though the affiliates do provide their water service. This "Equivalent Number of Customers" factor acknowledges that GSWC's affiliates do not perform billing and individualized customer contacts on the military bases.

Decision 10-11-035 – by contrast – accepts GSWC's argument (that it had rejected three years earlier) that the military constitutes a single customer for the purpose of four- factor allocations. While again, the Commission is not strictly bound by prior Commission rulings, it also does not have unfettered discretion to modify earlier practices simply as a matter of wont. Moreover, this modification in the Commission's interpretation of the four-factor allocation process engenders confusion among parties that participate in Commission proceedings. Neither DRA nor the utilities are well served by a vacillating policy that is not based either on compelling evidence or a consistent legal interpretation. Instead, the zigzag course followed by the Commission over the past seven years on this issue evinces an indefensible portrait of a decision-making process that is neither consistent nor readily understandable. Rather than sow

additional misunderstanding among DRA and the water utilities on the proper application of the four-factor formula for allocating the number of customers served, D.10-11-035 should be modified so that it is consistent with either D.03-05-078 or D. 07-10-034.

**IV. DECISION 10-11-035 IMPROPERLY AUTHORIZES GSWC TO AMORTIZE A MEMORANDUM ACCOUNT FOR REGULATORY COMMISSION EXPENSES EVEN THOUGH GSWC HAD LACKED COMMISSION AUTHORIZATION TO BOOK EXPENSES INTO THIS ACCOUNT**

Decision 10-11-035's holding on regulatory commission expenses represents a reversal of long-standing Commission practice regarding the treatment of routine utility expenses during the rate case cycle and it *de facto* overturns the rate case plan ("RCP"), D.04-06-018's, affirmation of the use of future test years to forecast utility revenue requirements. In addition, D.10-11-035 authorizes GSWC to amortize *historical* regulatory expenses even though GSWC has never received Commission authorization to book these expenses into a memorandum account. Not only is D.10-11-035 legally flawed it also – in effect – rewards GSWC for booking expenses into an account even though it had no authority to do so.

In considering DRA's request for rehearing on this issue the Commission should be mindful that allowing GSWC to recover regulatory Commission expenses on a retrospective basis, i.e., via a memorandum account would make whatever expenditures GSWC is seeking to recover from its customers for this account subject to a reasonableness review and a likely protest from DRA. Thus, rather than affording certainty to GSWC that its regulatory expenditures would be recovered, giving these expenses memorandum account treatment may well lead into extensive discovery efforts and the type of 20/20 hindsight review that the use of a prospective test year avoids. For example, DRA may scrutinize whether GSWC used a competitive bidding process in the selection of its outside counsel and/or consultants and may conduct an inquiry into the reasonableness of their compensation levels. Other previously incurred regulatory expenses may be challenged as well. In short, rather than providing the type of certainty of recovery that GSWC craves for its regulatory expenditures, memorandum account

treatment will likely lead to protracted litigation over seemingly routine *past* expenditures.

It should be noted that memorandum accounts cannot be established by utilities absent Commission authorization. GSWC never obtained Commission authorization before it began booking regulatory commission expenses into Account 146 and thus any recovery of amounts booked into this account would in effect be retroactive ratemaking and reward GSWC for failing to follow established Commission procedures for establishing memorandum accounts.

In D.04-06-018, the Commission reiterated the four situations where memorandum accounts are appropriate; 1) the expense is caused by an event of an exceptional nature that is not under the utility's control; 2) the expense cannot have been reasonably foreseen in the utility's last GRC and will occur before the utility's next scheduled rate case; 3) the expense is of a substantial nature in the amount of money involved; and 4) the ratepayers will benefit by the memorandum account treatment. None of these conditions is extant for GSWC's regulatory commission expenses. These expenses were not only foreseeable; the timing of GSWC's GRC application had previously been scheduled by the Commission. In addition, regulatory commission expenses are largely within the utility's control, and were not substantial in view of the company's overall revenue requirement. Moreover, because affording memorandum account treatment to these expenses will lead to additional expensive and unnecessary litigation over the reasonableness of the expenditures, establishing a memorandum account for these normal business expenditures will work to the detriment of GSWC's customers.

In short, regulatory commission expenses are among the least deserving candidates for memorandum account treatment in that they meet none of the four prongs of the memorandum account test. As the Commission noted in D.04-06-018, "The Commission's current practice for water utilities is to use two forecasted test years. Using a forecast allows the utility to project expected costs and determine the revenue required to recover those costs, and the Commission to tailor the rate changes to match

anticipated cost changes.” Nothing in the RCP authorized a deviation from the general rule of *prospective* test years for regulatory commission expenses. If the Commission is serious about adhering to the basic principle behind *prospective* ratemaking, i.e., that revenue requirements in GRCs are set on the basis of an estimated future test year, it cannot allow an exception to that rule for regulatory commission expenses – an expense item that is not only readily predictable, it is scheduled in advance by the Commission.

Decision 10-11-035 in essence rewrites this long-standing Commission practice and overturns this provision of the RCP decision. In D.09-07-021, in denying Cal Am’s request for deferred regulatory expense recovery, the Commission reiterated its earlier position (adopted in D.03-06-036) that “Regulatory expense is included in revenue requirement on a forecasted basis.” Decision 10-11-035 repudiates this holding by finding that the Uniform System of Accounts allows Class A water utilities to charge these expenses to Account 146 and be amortized to Account 797 over time. Even though the Commission has repeatedly found that regulatory commission expenses do not qualify for memorandum account treatment (including as recently as 2009), D.10-11-035 asserts : “For all practical purposes, Account 146 is treated as a memorandum account to accumulate regulatory commission costs for which recovery has yet to occur. This has been a long-standing practice of the Commission.” (p. 48.)

Either D.10-11-035’s conclusion about the proper treatment of regulatory commission expenses is wrong or D.09-07-021, D.04-06-018, and all other prior general rate case decisions of this Commission involving Class A utilities are wrong (and similar prior GRC decisions for electric and gas utilities). The memorandum account treatment given these expenses by D.10-11-035 or the future test year treatment that the Commission has given regulatory commission expenses (as a forecasted cost) in the legion of other decisions cited above cannot both be the “long-standing practice of the Commission.” Thus, in reality rather than being consistent with long-standing Commission practice, D.10-11-035’s authorization to allow GSWC to recover regulatory commission expenses (via a memorandum account) is the polar opposite of the “long standing Commission practice” the decision claims to follow.

**A. D.10-11-035 Needs to Be Modified to Prevent Double Recovery of Regulatory Commission Expenses**

According to response 2(a) in GSWC’s data response to DRA’s Data Request EM-14, (dated May 28, 2009), (see Attachment A)<sup>1</sup> the amount GSWC reported in its 2008 annual report to the Commission for Regions II and III for “rate case charges” of \$2,550,276 includes \$1,316,018.97 of regulatory expenses that are properly attributable to Golden State’s Bear Valley Electric Company, i.e., these expenses have nothing to do with providing water service to GSWC’s customers. GSWC’s Response 2(a) states that it is not requesting to recover Bear Valley Electric regulatory expenses in Application 08-07-010, however, to DRA’s knowledge this incorrect entry in GSWC’s 2008 Annual Report has never been corrected. If these expenses remain in GSWC’s Account 146 the GSWC would be able to charge its captive water ratepayers for regulatory commission expenses it has already recovered from its Bear Valley Electric customers. At a minimum D.10-11-035 needs to be modified to ensure that GSWC is not allowed to double recover these regulatory commission expenses – once from its Bear Valley Electric customers and once from GSWC’s ratepayers. Absent a provision along these lines, D.10-11-035 (as written) creates an unacceptable risk that GSWC’s water ratepayers would be billed for Bear Valley Electric’s regulatory expenses.

**V. CONCLUSION**

While the original proposed decision of ALJ Rochester properly and *legally* decided the issues presented by A.08-07010, D.10-11-035 contains several serious legal and factual errors that must be rectified. In particular, the Commission must rehear this case to prevent D.10-11-035 *de facto* repudiation of the rate case plan decision by allowing traditionally forecasted regulatory commission expenses to be given memorandum account treatment despite years of Commission decisions to the contrary.

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<sup>1</sup> Note: This attachment does not include the entire data response. It consists of the cover page and the page where response 2(a) appears. Response 2(a) is highlighted in the attachment.

The Commission's application of Tariff Rule 15 regarding the La Serena upgrades violates the specific language of the Rule and long-standing Commission practice. D.10-11-035's treatment of the four factor test represents an improper continuation of inconsistent and varying interpretations of the number of customers factor in allocating expenses between the utility and its affiliates. Finally, as DRA noted above, D.10-11-035 should be changed to prevent GSWC from recovering regulatory commission expenses for Bear Valley Electric from its water ratepayers.

Respectfully submitted,

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December 22, 2010

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day *served* a copy of “**APPLICATION FOR REHEARING OF THE DIVISION OF RATEPAYER ADVOCATES OF DECISION 10-11-035**” to the official service lists in **A.08-07-010 and A.07-01-014** by using the following service:

**E-Mail Service:** sending the entire document as an attachment to all known parties of record who provided electronic mail addresses.

**U.S. Mail Service:** mailing by first-class mail with postage prepaid to all known parties of record who did not provide electronic mail addresses.

Executed on **December 22, 2010** at San Francisco, California.

/s/ HALINA MARCINKOWSKI

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Halina Marcinkowski

**SERVICE LISTS for**  
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