

Decision **ALTERNATE PROPOSED DECISION OF PRESIDENT PEEVEY**
(Mailed 8/11/2014)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the Commission's Own Motion into Addressing the Commission's Water Action Plan Objective of Setting Rates that Balance Investment, Conservation, and Affordability for the Multi-District Water Utilities of:
California-American Water Company (U210W), California Water Service Company (U60W), Del Oro Water Company, Inc. (U61W), Golden State Water Company (U133W), and San Gabriel Valley Water Company (U337W).

Rulemaking 11-11-008
(Filed November 10, 2011)

**DECISION PROVIDING FURTHER GUIDANCE FOLLOWING
RELEASE OF STAFF REPORT**

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Attachment A: Report on Balanced Rate Rulemaking

DECISION PROVIDING FURTHER GUIDANCE FOLLOWING RELEASE OF STAFF REPORT

Summary

Following workshops, a workshop report by the Commission's Division of Water and Audits, and multiple rounds of comments, we provide guidance on rate balancing for Commission-regulated, multi-district water utilities for use in their next general rate case (GRC) applications or Tier 3 GRC Advice Letter (AL) filings. We direct all of these multi-district water utilities to review their own districts for high-cost and affordability problems and to report on the review in their next GRC applications or AL filings, on the timelines specified. Where high-cost and affordability problems exist, each multi-district water utility must propose one or more intra-utility solutions, which may include a Rate Support Fund or other cross-subsidization mechanism, some form of additional district consolidation, or other relief, as further discussed in this decision. The record, on balance, does not support a single, prescriptive approach or solution.

1. Background

The Commission issued this Order Instituting Rulemaking (OIR) on November 10, 2011 to address a major policy objective in the Water Action Plan as it affects multi-district water utilities.¹ That policy objective, the sixth among the six objectives identified in the plan, is to set rates that balance investment,

¹ The Water Action Plan serves as a guide in the Commission's regulation of investor-owned water utilities. The original plan, adopted by the Commission in 2005, is available on the Commission's website at this link:

ftp://ftp.cpuc.ca.gov/PUC/hottopics/3water/water_action_plan_final_12_27_05.pdf

The current Water Action Plan, adopted on October 28, 2010, updates the 2005 plan and is available at this link: <http://docs.cpuc.ca.gov/PUBLISHED/Graphics/125501.PDF>

conservation, and affordability.² The Commission focused this OIR on balancing investment, conservation, and affordability in multi-district water utilities.

To advance the discussion, the OIR posed eight preliminary questions and requested comments from the named respondents (the five Commission-regulated, multi-district water utilities and the Division of Ratepayer Advocates (DRA)) and from any other interested persons and entities.³ Thereafter, by ruling on April 18, 2012, Administrative Law Judge (ALJ) Gary Weatherford called for prehearing conference (PHC) statements, which parties filed on May 16, 2012. The Commission held a PHC on May 23, 2012 and, as required by Pub. Util. Code §1701.1(b), the assigned Commissioner, Commissioner Sandoval, issued a scoping memo following the PHC.⁴

Based on all of the filed comments and statements as well as the PHC discussion, the scoping memo clarified and slightly revised the OIR's preliminary statement of scope to focus on *intra*-utility policy solutions and to exclude consideration of *inter*-utility transfers or other *inter*-utility adjustments.

² The other five objectives are these: (1) maintain highest standards of water quality; (2) strengthen water conservation programs to a level comparable to those of energy utilities; (3) promote water infrastructure investment; (4) assist low income ratepayers; and (5) streamline CPUC regulatory decision-making. (See 2005 Water Action Plan at 4; 2010 Water Action Plan at 4.)

³ The five multi-district water utilities are: California-American Water Company; California Water Service Company (CWS); Del Oro Water Company, Inc. (Del Oro); Golden State Water Company (GSWC); and San Gabriel Water Company. The Division of Ratepayer Advocates (DRA) has since been renamed the Office of Ratepayer Advocates (ORA).

The following parties filed initial comments on March 1, 2012: all respondents, as well as the Natural Resources Defense Council and The Utility Reform Network (TURN). On March 22, 2012, the following parties filed reply comments: all respondents except Del Oro, TURN and Jeffrey Young, a CWS ratepayer.

⁴ *Assigned Commissioner's Scoping Memo and Ruling*, filed June 20, 2012.

The scoping memo recognized that any thoughtful, fair discussion of new, inter-utility rate balancing mechanisms should not be limited solely to the respondent multi-district water utilities, but also should include Commission-regulated single-district utilities. Thus, the scoping memo expressly excluded inter-utility mechanisms from consideration in this rulemaking, as follows:

The scope of this rulemaking is to consider adopting new or revised guidelines for consolidation of districts, some variation of a high cost fund within multi-district utilities, and another mechanism or a combination of them as a means to advance the Commission's water action plan objective of setting rates that balance investment, conservation, and affordability. Inter-company mechanisms will not be explored in this proceeding. Any consideration of mechanisms in addition to consolidation guidelines and a High Cost variant will be informed and bounded by the analysis in this proceeding's workshops, data requests and responses, comments and reply comments, and other information submitted in the record of this proceeding. (Scoping Memo at 3-4, *emphasis added*.)

The scoping memo also set two workshops, required preparation of a draft workshop report, and provided for comments on the draft report, followed by release of a final workshop report. Though the scoping memo's initial schedule was revised, the Commission followed this procedural plan and held two workshops in 2012, on July 17-18 and on November 6-7. Thereafter, the parties requested additional scheduling adjustments and as they requested, ALJ Weatherford, by ruling filed November 14, 2012, authorized comments on materials discussed at the second workshop. Those comments were filed on December 12, 2012.

On July 12, 2013 the Commission's Division of Water and Audits released a draft report titled Report on Balanced Rate Rulemaking (R.) 11-11-008 and

served it on the OIR service list. On August 7, 2013, by ruling of the Chief ALJ, ALJ Jean Vieth was co-assigned with ALJ Weatherford. At the request of several parties, the Commission extended the period for comments on the draft staff report; accordingly, comments were filed on August 23, 2013 and reply comments on September 13, 2013. On October 7, 2013 the assigned Commissioner filed an amended scoping memo to confirm various administrative matters and to update the procedural schedule, given the prior, incremental revisions to it. On February 12, 2014, the final version of the staff report, dated January 30, 2014, was served on the service list for this rulemaking and posted on the Commission's website.⁵ The final version extensively revised the earlier draft. We refer to the final version as the staff report and append it to this decision as Attachment A.

2. Issues Before the Commission

The staff report identifies and discusses two broad issues where Commission guidance via today's decision will shape future General Rate Case (GRC) applications or Tier 3 GRC Advice Letter (AL) filings by multi-district water utilities.⁶ The first issue concerns options for mitigating bills in high-cost districts, either by establishment of an intra-utility Rate Support Fund (RSF) or alternatively, by further consolidation of districts. The second issue focuses on the existing consolidation guidelines negotiated by parties in 1992, and asks whether they should be revised, and if so, how.

⁵ The staff report is available at this link:

<http://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M088/K240/88240939.PDF>

⁶ Del Oro files district-specific, Tier 3 AL GRCs; the other utility respondents file GRC applications.

3. Discussion

Today's decision provides policy guidance, on an intra-utility basis, for use by multi-district water utilities as they plan future GRC applications or Tier 3 GRC AL filings. The OIR has shaped our inquiry, both as to subject and process, by providing:

As part of advancing the sixth objective in the Water Action Plan, the Commission will consider mechanisms such as a "High-Cost" fund or consolidating districts and rates within the multi-district water utilities. In this proceeding, the Commission will consider these mechanisms on a general policy basis and will not consider the application of the mechanisms to a specific multidistrict utility. To the extent this Rulemaking results in the adoption of new mechanisms, utilities can include requests to utilize these mechanisms in their respective GRCs or other appropriate rate-setting applications. (OIR at 4.)

However, as the assigned Commissioner's scoping memo determined, due process and fundamental fairness necessarily limit the scope of this rulemaking to intra-utility mechanisms that respondent multi-district water utilities might employ to achieve balanced rates.

Pages 5 through 7 of the OIR recount the Commission's long history of setting rates for water utilities in what has become a standard, case-by-case, locale-by-locale manner, though there are exceptions as well. The traditional approach is attributable largely to the significant variability in supply and distribution costs for different water utilities and for different districts within multi-district water utilities (based on the different costs linked to local or imported water sources, water quality protection and contamination remediation, infrastructure needs, etc.). This cost variability among water utilities contrasts markedly to the comparative uniformity across electric utilities, which operate with statewide "postage stamp" rates.

Thus, the OIR described this rulemaking's approach as a broad, non-exclusive review:

With the Commission's adoption of its 2010 Water Action Plan, and in light of the Commission's continuing efforts to set rates that balance investment, conservation, and affordability we institute this Rulemaking to consider modifying the 1992 guidelines or establishing new consolidation guidelines for high cost areas for the multi-district water utilities. The Rulemaking will also consider a "High-Cost" fund mechanism. (OIR at 7.)

The record for this rulemaking consists of all the filings, including the parties' written comments, as well as the workshop discussions. Because the attached staff report provides an overview of the comments and the workshop discussions, we do not duplicate that effort here. The record persuades us that the district-specific conditions within each multi-district water utility remain too variable for prescriptive guidelines on an RSF or other cross-subsidy mechanism. Moreover, the record does not compel a choice between authorizing cross-subsidy mechanisms within multi-district water utilities and authorizing further consolidation.

For example, CWS's successful experience demonstrates that an RSF is a tool that should be considered where the particular circumstances in one or more districts within a multi-district water utility warrant rate balancing efforts. Similarly, other cross-subsidy mechanisms can be useful. The record continues to support consolidation and persuades us that the guidelines developed in 1992 by the then-DRA and the Class A water utilities, titled, "1992 Guidelines for Combining Water Utility Districts for Ratemaking and Public Utilities Commission Reporting Purposes," are no longer relevant and can be used by parties to argue against consolidation request, ironically in cases where consolidation makes the

most sense; *e.g.* areas that have high water rates, areas that have vulnerable water supplies, etc.

Though the Commission has never formally adopted these guidelines, the parties have relied upon them a number of times in proposed district consolidation applications.⁷ The 1992 guidelines identify four criteria for consideration in district rate consolidations -- proximity, rate comparability, water supply and operation. The parties who negotiated the 1992 guidelines and memorialized them in a settlement agreed that no districts would be combined for the express purpose of having one district subsidize another. As the record shows, each of the four criteria can be used to argue against consolidation of any sort, counter to the scope of this rulemaking which was to consider adopting “new or revised guidelines for consolidation of districts,...to advance the Commission’s water action plan objective of setting rates that balance investment, conservation and affordability.”⁸

We agree with the DWA staff report (Attachment A, at 19) which states that “...the existing guidelines become a convenient “fall-back” position for utilities, parties and the Commission alike.” We are persuaded to eliminate the guidelines in their entirety and signal that the Commission is open to consolidation requests that balance investment, conservation and affordability.

⁷ See for example: Decision (D.) 05-09-004 [denying CalAm’s request to consolidate rates for its Monterey and Felton districts]; D.08-05-018 [denying CalAm’s request to consolidate rates for its Larkfield and Sacramento districts]; and D.10-12-017, as modified in other respects by D.11-08-010 [approving merger of CWS’s South San Francisco and Mid-Peninsula Districts].

⁸ *Assigned Commissioner’s Scoping Memo and Ruling*, filed June 20, 2012.

Based on the record established here, we do not adopt additional prescriptions for rate balancing within multi-district water utilities. However, we conclude that each multi-district water utility should assess, before filing its next GRC application or any district-specific Tier 3 GRC ALs, whether as RSF or further consolidation of its districts will yield rates that more effectively balance investment, conservation and affordability. The record supports use of the following approach. First, each multi-district utility should review all of its separate ratesetting districts to determine whether high-cost and affordability problems exist. (One tool available for making such a determination is the high cost and affordability screening framework found at Appendix A of the staff report.) Then, if high-cost and affordability problems exist in one or more districts, the multi-district water utility should propose a solution or solutions, together with a specific implementation plan, in its next GRC application or in appropriate district-based Tier 3 GRC ALs. At a minimum, each multi-district water utility should report on its district-specific review in its next GRC application or in its Tier 3 GRC ALs. The report should be included in the application tendered as a notice of intent under the process and schedule required by the rate case plan.⁹

Proposals for rate balancing, based on identified high-cost and affordability problems, may include one or more of the following strategies but need not be limited to them:

1. an RSF or similar cross-subsidy fund;

⁹ See D.07-05-062, which revised the Rate Case Plan for Class A water utilities approved by D.04-06-018.

2. reduction in high costs (*see* the staff report [Attachment A] and particularly, the decision tree for the high-cost track in Appendix A to the staff report);
3. consolidation in some form, such as:
 - a. rate consolidation;
 - b. cost consolidation;
 - c. rate base consolidation; and
 - d. operational consolidation.
4. intra-company grant/loan funding;
5. rate design (affordability through the first rate tier); and
6. budget plans.

This approach is consistent with the recommendations in the staff report, which does not urge a single approach. Rather, the staff report observes that the record for this rulemaking, though it shows no unanimity among parties, does support several, non-exclusive options. The staff report states:

[T]he commission may wish to consider one or more of the following options for the establishment of a rate support fund (RSF); (1) Authorize multi-district water utilities to propose a RSF mechanism for their districts; (2) Establish prescriptive guidelines for the RSF with regards to affordability, usage and subsidy type; and (3) Do not authorize any future RSF mechanisms, and instead, encourage district consolidation as a means to mitigate bills and high-cost districts. (Report on Balanced Rate Rulemaking (R.11-11-008), January 30, 2014 at 2.)

4. Conclusion

We find no single solution should be adopted to mitigate all high-cost and affordability problems found to exist within one or more districts of a multi-district water utility. Rather, an appropriate solution may incorporate establishment of an intra-utility RSF or some variation, or additional, district-based consolidation. Each multi-district water utility should perform a

district-based rate review, report on the review in its next GRC application or in Tier 3 GRC ALs (as applicable) and propose one or more, appropriate rate balancing solutions to mitigate any high-cost and affordability problems. The report should be included in the application tendered at the notice of intent stage under the rate case plan or as part of the Tier 3 GRC ALs. GSWC should be authorized to file its report 90 days beyond July 15, 2014, the date on which it must file its next GRC, and the Commissioner or ALJ assigned to that GRC application may authorize additional time, as warranted.

5. Next Steps

This proceeding also raised several issues regarding affordability and rates that were not contemplated in the original scope but which are fundamentally related to balanced rates. It is appropriate for the Commission to address these issues presently, especially in light of Governor Brown's January 2014 drought declaration. The Commission will open a new OIR to analyze and propose actions on issues regarding affordability and rate design, including but not limited to conservation rate design such as tiered rate structures, and accounting mechanisms such as Water Revenue Adjustment Mechanisms. We anticipate that a new OIR will issue shortly.

6. Comments on Alternate Proposed Decision

The alternate proposed decision of Commissioner Peevey in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Opening Comments were filed by the Office of Ratepayers Advocate (ORA), The Utility Reform Network (TURN), the National Consumer Law Center (NCLC), and California Water Service Company (CWS). Reply comments were filed by ORA and NCLC.

Opening comments are summarized in this paragraph. ORA claims that the idea to eliminate the Guidelines is not in the record. TURN claims that the idea to eliminate the Guidelines is not in the scope of the proceeding. NCLC argues that the Guidelines are useful while also proposing additional criteria. CWS is generally supportive of the Alternate Proposed Decision and the intent to allow consideration of more consolidation requests.

Reply comments are summarized in this paragraph. ORA supports the comments of TURN and NCLC. ORA claims that CWS is conflating affordable water rates with a statewide average rate. NCLC posits that elimination of the Guidelines will result in criteria that are too broad if left to the goals of investment, conservation, and affordability.

After a review of the opening and reply comments, we find that there were no persuasive arguments to make any changes to the Alternate Proposed Decision.

7. Assignment of Proceeding

Catherine J.K. Sandoval is the assigned Commissioner and Gary Weatherford and Jean Vieth are the co-assigned ALJs in this proceeding.

Findings of Fact

1. Supply and distribution costs for different water utilities and for different districts within multi-district water utilities vary significantly, based on the different costs linked to local or imported water sources, water quality protection and contamination remediation, infrastructure needs, etc. This cost variability among water utilities contrasts markedly to the comparative uniformity across electric utilities, which operate with statewide “postage stamp” rates.

2. District-specific conditions within each multi-district water utility remain too variable for prescriptive guidelines on a Rate Support Fund or other cross-subsidy mechanism.

3. The record does not compel a choice between authorizing cross-subsidy mechanisms within multi-district water utilities and authorizing further consolidation of districts.

4. The record persuades us that the guidelines developed in 1992 by the then-DRA and the Class A water utilities, titled, “*1992 Guidelines for Combining Water Utility Districts for Ratemaking and Public Utilities Commission Reporting Purposes,*” are no longer relevant and can be used by parties to argue against consolidation requests, ironically in cases where consolidation makes the most sense, *e.g.* areas that have high water rates. Areas that have vulnerable water supplies, etc.

5. We eliminate the guidelines in their entirety and signal that the Commission is open to consolidation requests that balance investment, conservation and affordability.

6. Rate balancing solution(s) to mitigate high-cost and affordability problems may include any of those discussed in the body of this decision and identified in the Ordering Paragraphs, but need not be limited to them.

Conclusions of Law

1. Fundamental fairness and due process limit the scope of this rulemaking to intra-utility rate balancing mechanisms for the respondent multi-district water utilities.

2. Any unresolved requests or motions filed in this rulemaking should be denied.

3. This decision should be effective today to provide timely notice to respondent multi-district water utilities in advance of their next GRC filings.

O R D E R

IT IS ORDERED that:

1. Prior to the next General Rate Case (GRC) applications or Tier 3 GRC Advice Letter filings required by each respondent (other than the Office of Ratepayer Advocates), the respondent shall perform a district-based rate review to assess whether high-cost and affordability problems exist in any of its districts. One tool available for determining whether high-cost and affordability problems exist is the high-cost and affordability screening framework found at Appendix A of the Report on Balanced Rate Rulemaking (Rulemaking 11-11-008), dated January 30, 2014, by the Division of Water and Audits and appended to this decision as Attachment A.

2. Each respondent to this rulemaking (other than Golden State Water Company (GSWC) and the Office of Ratepayer Advocates) must report on the review required by Ordering Paragraph 1 in its next General Rate Case (GRC) application or in each district-specific Tier 3 GRC Advice Letter (AL) filing (as applicable). Because GSWC has been scheduled to file its GRC application on July 15, 2014, it shall report on that review within 90 days of the effective date of this decision. If the review determines that high-cost and affordability problems exist in one or more districts, the GRC application or Tier 3 GRC ALs also must propose one or more solutions to mitigate those problems, as further specified in Ordering Paragraph 3.

3. The proposed solution(s) referenced in Ordering Paragraph 2 may include the following but need not be limited to them:

- a. a Rate Support Fund or similar cross-subsidy fund;
 - b. reduction in high costs;
 - c. consolidation in some form (i.e., rate consolidation, cost consolidation, rate base consolidation, operational consolidation);
 - d. intra-utility grant/loan funding;
 - e. rate design (affordability through the first rate tier); and
 - f. budget plans.
4. Any unresolved requests or motions filed in this rulemaking are denied.
5. Rulemaking 11-11-008 is closed.

This order is effective today.

Dated _____, at San Francisco, California.