BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

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Order Instituting Rulemaking on the Commission's Own Motion to Develop Standard Rules and Procedures for Regulated Water and Sewer Utilities Governing Affiliate Transactions and the Use of Regulated Assets for Non-Tariffed Utility Services	R.09-04-012 (Filed April 16, 2009)

RESPONSE OF THE UTILITY REFORM NETWORK TO THE PETITION FOR MODIFICATION OF D.10-10-019 OF THE CALIFORNIA WATER ASSOCIATION

April 25, 2011

THE UTILITY REFORM NETWORK

115 Sansome St., Suite 900
San Francisco, CA 94104
(415) 929-8876, x. 312 (Phone)
(415) 929-1132 (Fax)

Christine Mailloux
Staff Attorney
cmailloux@turn.org

Regina Costa
Research Director
rcosta@turn.org

I. INTRODUCTION

Pursuant to Rule 16.4 of the Commission's Rules of Practice and Procedure, The Utility Reform Network ("TURN") hereby responds to the Petition for Modification of D.10-10-019 of the California Water Association ("Petition for Modification" or "Petition"). TURN urges the Commission to reject most of the proposals made by the California Water Association ("CWA") in its Petition. First, the Petition is a procedurally improper attempt to re-litigate issues previously briefed and resolved in the docket itself. CWA has provided only vague assertions of "further investigations" while mainly re-arguing positions it took in the docket. Second, the Petition's proposals, for the most part, serve to narrow the scope of the adopted affiliate transaction rules in Attachment 1 of D.10-10-019, and make changes to those rules that will weaken their effectiveness. While there are a few places where the Petition raises valid concerns that the Commission could address, the Commission should reject the majority of the Petition.

II. DISCUSSION

A. The Petition for Modification is Procedurally Improper

The Petition is an improper attempt to re-litigate specific issues that the Commission previously considered just a few months before. While, as discussed below, TURN does not oppose all of the CWA's proposed revisions, several of them are far-reaching, substantive changes that would result in outcomes contrary to the Commission's intent in adopting D.10-10-019. TURN notes that CWA did not file an Application for Rehearing of this Decision. Yet, this Petition is arguing that the Decision contains errors of fact and is also contrary to the record in the proceeding.[1] For example, although the Petition avoids using the specific terminology, the Petition appears to argue that the Commission did not base its decision on the record or findings

[1] Petition for Modification at p. 2 arguing that the rules conflict with the stated objectives of the Commission as enumerated in the Final Decision and that the rules fail to address ambiguities and inconsistencies and will cost consumers money for compliance.

in the case. This is one of the basis for an Application for Rehearing.[2] In the past, the Commission has not allowed parties to use a Petition for Modification as a "substitute" for an Application for Rehearing.[3] Even the courts have weighed in on similar issues, finding that a Petitioner "cannot now cure its failure seasonably to seek judicial review of the certificate decision by the device of a series of late-filed petitions…If such a device were allowed, one obtaining a certificate from respondent commission could never safely act under it without fear of later attack."[4]

Further, the Commission has denied Petitions for Modification on the grounds that the petitioner is "merely re-arguing its point and is not providing any new or changed facts."[5] The Commission looks, at least in part, to see if the facts and circumstances presented by a petition have already been considered and, if no new or changed facts or circumstances were presented in the petition, then there is no good cause to modify the Decision.[6] Indeed, in one case, the Commission found that a Petition for Modification and the Application for Rehearing of the

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[2] Pub. Util. Code §1757.1

[3] *See*, 2009 Cal. PUC. LEXIS 334 *10 [D.09-07-014, *Order Instituting Rulemaking to Examine the Commission's Post-2005 Energy Efficiency Policies, Programs, Evaluation, Measurement, and Verification*, and Related Issues (R.06-04-010), Denying CE Council Petition for Modification as the improper procedural vehicle]; *See also*, 2007 Cal. PUC LEXIS 6, [D.07-01-007, *In the Matter of the Joint Application of Verizon Communications and MCI to Transfer Control,* (A.05-04-020), Denying Greenlining Petition as untimely Application for Rehearing with no reasonable basis for treating request as Petition for Modification)

[4] *Northern California Association to Preserve Bodega Head and Harbor Inc. v. Public Utilities Commission* 61 Cal. 2d 126, 135 (Denying Petition of citizens' group and finding that the group failed to take advantage of the procedural avenues available.)

[5] 2009 Cal. PUC LEXIS 334 *13 (*CE Council*); *See also*, D.08-07-028, *In the Matter of the Application of the Exposition Metro Line Construction Authority* (A.06-12-005 and related matters), denying the Petition of the Los Angeles Unified School District.

[6] D.08-07-028 (*Exposition Metro*) at p. 5 and 6; See also, 2007 Cal. PUC LEXIS 6 (*Greenlining*), Denying Greenlining Petition describing Petition to Modify as seeing changes "generally in light of changes occurring since the decision was issued." ; *See also*, 2008 Cal. PUC LEXIS 81, * 6 [D.08-03-009, *Order Instituting Rulemaking to Review Policies Concerning Intrastate Carrier Access Charges*, (R.03-08-018) (Denying AT&T Petition for failure to provide "intervening and unexpected legal or factual events which would support changing the outcome of the [Decision]")

decision denying that Petition constituted an "impermissible collateral attack" on the original decision.[7]

Generally the Commission has authority to "rescind, alter or amend" one of its decisions.[8] However, the Commission recognizes that its authority "should be exercised with great care and justified only by extraordinary circumstances." And that "only a persuasive indication of new facts or a majority change in material circumstances…would cause us to reopen the proceedings."[9] Further, the Commission has also clearly stated that the petitioner bears the burden of demonstrating that the recent decision should be modified.[10] As discussed below, CWA fails to meet its burden.

B. CWA's Proposed Changes to the Definition of Affiliate Would Unduly Narrow the Scope of the Rules

CWA proposes several changes to the definition of affiliate as adopted in D. 10-10-019. It requests that: 1) the term "parent" or "parent company" and parent holding company be removed from the definition (and added into specific rules where appropriate); 2) an explicit exemption be added to the definition where the water utility does not have a controlling interest, such as when a utility participates on a board or quasi-governmental water authority; and 3) the definition exclude non-profit mutual water companies. The Commission rejected each of CWA's concerns during the proceeding.[11] CWA raises no new information or arguments in this Petition beyond what they argued to the Commission previously except for vague assertions of

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[7] 2009 Cal. PUC LEXIS 74 *10, [D.09-02-032, *In the Matter of the Application of the Exposition Metro Line Construction Authority* (A.06-12-005 and related matters] citing to Public Utilities Code §1709 declaring final orders and decisions of the Commission to be "conclusive" and noting that LAUSD's failure to file an Application for Rehearing of the original decision rendered that decision final.

[8] Pub. Util. Code §1708

[9] 2009 Cal. PUCLEXIS 74 *14 (*Exposition Metro*) citing to D.03-10-057 and 4 Cal. PUC 2d 139, 149-150

[10] 2008 Cal. PUC LEXIS 81, * 4 (*Access Charges*)

[11] *See*, the discussion in D.10-10-019, at p. 41 which, as described below, explicitly rejects attempts to exclude "parent company" from the definition of affiliate and also fails to address the scenarios raised by CWA in its comments on the Proposed Decision at p. 7-8 except to reject CWA's proposal to create a threshold of 50% interest for the definition of affiliate. D.10-10-019 at p. 41

"potential and unnecessary costs" to customers. The Commission should, generally, reject the Petition on these points.

There is a single issue raised by CWA relating to the definition of affiliate that the Commission could consider. In its Petition, CWA proposes adding language to Rule II E. clarifying that participation by the water utility in public agencies where the utility has no controlling interest, despite a greater than 10% interest in voting shares, would be exempt from the definition of affiliate.[12] In response to CWA's previous arguments on this point, TURN pointed out that these scenarios are "red herrings" because it is clear that the affiliate transaction rules are not meant to apply and the rule could remain silent. If, however, the Commission finds that adding explicit language would add clarity to the rules, then the proposed edit (listed as #3 on page 9 of the Petition) could be adopted, with the further qualification that the utility is a "member or shareholder with a non-controlling interest". In addition, the term "mutual water company" should be deleted from the proposed language.

CWA also raised its concern regarding non-profit and for profit entities in comments on the Workshop Report and the Commission did not see fit at the time to make the requested changes.[13] TURN does not find CWA's discussion in the Petition regarding non-profit mutual water companies persuasive. Even if an affiliate is nonprofit, there would still be risks to ratepayers from cross subsidy or favorable dealing and, although less likely, risks to competitors for non-tariffed products and services.[14]

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[12] Petition at p. 3-6.

[13] CWA Opening Comments on the Workshop Report, May 7, 2010 at p. 12.

[14] The example cited by CWA of San Gabriel's shares in the Fontana water company relate more to the use of shared services and less to the treatment of Fontana as an affiliate. (Petition at p. 6) The transactions between the two companies should be treated as affiliates, but perhaps, as discussed below, the shared services should be allowed. There is nothing the Rules that would require San Gabriel to find a different supply of water.

The remaining proposed edits to the definition of affiliate relate to the elimination of parent company from the definition. TURN urges the Commission to reject this proposal. In the Final Decision the Commission, very clearly, "highlight[s] that the Rule II.E definition of "affiliate" includes the utility's parent company."[15] The need to highlight this issue was precisely because the water utilities argued to eliminate "parent company" from the definition in their comments during the proceeding.[16] Indeed, the Commission did make changes to the rules in order to accommodate certain utilities' unique corporate structure, such as California American Water.[17] However, CWA's proposed elimination of the term parent from the definition of affiliate to supposedly fix inconsistencies in the rules is a perfect example of "throwing the baby out with the bath water." It is completely unnecessary to make the term affiliate unacceptably narrow by eliminating parent company from the definition in order to resolve some potential inconsistency in other rules. This proposal should be rejected and the Commission should consider more targeted clarifications.

C. Any Change to Shared Corporate Services Should Be Accompanies By Clear Rules on Cost Allocation and Monitoring

CWA proposes moving certain listed shared services from Rule V.D. over to the list of permitted shared services in Rule V.C.[18] Rule V was heavily discussed during the proceeding and CWA has not demonstrated any new information or changed circumstances that would justify a change to the current Rule. The discussion on Rule V in the docket focused primarily on shared corporate governance and on the use of proprietary information. From what TURN can determine from the documents that it reviewed, the services highlighted by CWA in this

[15] D.10-10-019 at p. 42

[16] See, for example, CWA's Opening Comments on the Proposed Decision at p. 9-10. They are also argued that the definition of parent company related to the inclusion of parent in the definition of affiliate. CWA Opening Comments on the Workshop Report, May 7, 2010 at p. 11.

[17] D.10-10-019 at p. 45-46.

[18] Petition for Modification at p. 10

Petition were not the source of significant discussion during the proceeding, however some examples such as engineering services were cited to and more general reference to the electricity affiliate transaction rules was included. [19]

In light of the fact that the treatment of these specific services may not have been directly addressed in the docket, it appears from the scenarios provided by CWA in its Petition, that it may be prudent for the Commission to reconsider the issue of whether these specific services should be subject to sharing. However, TURN is not familiar enough with the potential unintended consequences to support CWA's proposal and we defer to DRA on this issue. What is clear from the proceeding is that if the Commission was to grant CWA's request on this point, then the sharing of these services must be subject to "strict and efficient cost allocation procedure" and compliance and reporting procedures, including access to parent and affiliate records.[20]

D. CWA's Proposal to Narrow the Requirement to Notify the Commission of New Affiliates Goes Too Far

Rule VIII.D. requires water utilities to notify the Commission upon the creation of a new affiliate. CWA requests that the Commission narrow the reporting requirement to the creation of affiliates "whose primary business is a water industry-related activity in California."[21] Further, CWA requests that the Rules require the utility to notify the Commission through an informational-only filing instead of the current Tier 3 advice letter requirement.[22] CWA claims that the burden on the utility and the Commission from this filing outweighs the benefit. Again, CWA's proposal relates to an issue already litigated in the docket. Throughout the discussions, the utilities attempted to narrow the applicability of all of the rules only to those affiliates that

[19] Opening Comments of CWA on the Proposed Decision at p. 14-15, citing to "engineering services"
[20] DRA Comments on Staff Report, May 7, 2010, at pg. 7.
[21] Petition for Modification at p. 14.
[22] Petition for Modification at p. 15.

operate in California and only those affiliates engaged in a "competitive market" in California for water-related services, and other language that would make the rules less effective.[23] In the Final Decision, the Commission adopted some of CWA's proposal and, for example, limited the rules to transactions between affiliates that are not regulated by other state regulatory commissions.[24] However, the Commission rejected other utility attempts to unnecessarily limit the rule by proposing to exclude out of state affiliates, for example. Ultimately, the Commission recognized that many different types of water utility affiliates may affect the California utility operations and that, "the Commission, not the utility, should determine whether an affiliate is subject to these Rules."[25] It was the Commission's intent to draft Rule VIII.D. broadly and CWA's attempts to unduly narrow the requirement should be rejected.

While we do agree with CWA that a Tier 3 filing, requiring a Commission resolution, for every affiliate notice would be burdensome for both the Commission and the utility, an information-only filing, is insufficient because the filings are not subject to protest and would not be closely reviewed by Commission Staff. TURN recommends that the rule be revised to require a Tier 2 advice letter for the filings referenced in Rule VIII D. Tier 2 is not burdensome on either staff or the utility. Under G.O. 96-B, a Tier 2 advice letter is subject to protest, provides sufficient notice to the interested parties, and requires staff to provide a written disposition of the advice letter, but not a resolution. If, however, the industry division determines that the advice letter includes a request to exempt the affiliate from the Rules, and such exemption is not clear (i.e., it is not clear that the affiliate is regulated by another regulatory commission), then the staff can request that the utility re-file as a Tier 3 advice letter. Staff can only rule on advice letters if

[23] See, for example, CWA Opening Comments on the Workshop Report at p. 14 proposing to limit the applicability of Rule III to affiliates operating "in a competitive environment."

[24] Affiliate Transaction Rules I.B.

[25] D.10-10-019 at p. 75

such a ruling would be a ministerial act; otherwise, under G.O. 96-B, such a determination would have to be a Tier 3 advice letter. Therefore, while Rule VIII.D. should be modified, the Commission should reject CWA's specific proposals.

E. CWA's Objection to Shareholder Payment for the Biennial Audit Was Explicitly Rejected by the Commission

TURN did not address this issue to any significant degree during the proceeding and, as such, cannot speak directly to this issue. However, TURN notes that CWA made the same exact arguments that it makes here about the requirement for shareholders to pay for the audit in its comments on the Proposed Decision, and the Commission rejected those arguments by maintaining the requirement that shareholders pay for the audit in its Final Decision.[26]

It appears that CWA misses the point regarding the cost sharing of the audit. This is a cost caused by the utility's affiliate transactions and corporate structure. The Commission does not require the utility to engage in these transactions or to offer unregulated services. The risk from these transactions, even if they are deminimus today, should not be borne by the ratepayer who may not be aware of nor benefit from the existence of these affiliates. Indeed, in response to CWA's concerns, the Commission limited the requirement for the audit to those situations where the sum of all unregulated affiliates' revenue over two years equals 5% of the total revenue of the utility during that period.[27] So, in those situations where the affiliate transactions and operations of the unregulated affiliates are significant enough to cross the 5% threshold, the Commission has determined that it is the shareholders benefiting from the transactions and therefore it is the shareholders that should foot the bill for the necessary review of those transactions. The repeated requests by CWA to have the costs of the audit solely borne by the ratepayer should be rejected.

[26] CWA Opening Comments on the Proposed Decision at p. 19 and D.10-10-019 at p. 77.
[27] Affiliate Transaction Rules VIII.E.

F. CWA's Request to Delete Reference to Indirect Costs Has Unintended Consequences and Should Be Deleted

CWA requests changes to Rule X.D. related to cost allocation of Non Tariffed Products and Services ("NTP&S").[28] While the Petition only requests the deletion of a single word – indirect—this change could potentially have significant consequences for ratepayers. Again, as with most of the proposals in this Petition, CWA is requesting the Commission make a change that it already considered, albeit not explicitly, in the docket itself. There, as here, CWA argued that the revenue sharing mechanism set out in the rules was a proxy for cost allocation and therefore the cost allocation sections of the Rules should be deleted as duplicative or possibly causing double recovery for ratepayers.[29] DRA and TURN disagreed. The Commission partially accepted CWA's argument, as described in the Petition, and deleted reference to non-incremental investments and costs incurred for jointly used labor and capital. However, it did not delete the entire concept of cost allocation in the Rules.[30]

This is a complicated issue where language and terms of art must be used carefully. By deleting the word "indirect" the Commission could leave ratepayers to bear an inequitable burden of the costs of NTP&S. As TURN pointed out in its comments in the docket, it is difficult to ensure that the revenue sharing mechanism will adequately account for all indirect costs because indirect costs are by their nature difficult to identify and allocate.[31] The Commission should not look at the revenue sharing mechanism as a one-for-one substitute for cost allocation, but rather as one of the means to that end. Therefore, while TURN acknowledges that the sentence as drafted may lead to confusion based on the treatment of indirect costs in the Rules, the term "indirect" should not be removed entirely. Perhaps the

[28] Petition for Modification at p. 18.
[29] CWA Opening Comments on the Proposed Decision at p. 20-21.
[30] D.10-10-019 at p. 87.
[31] TURN Reply Comments on the Workshop Report, May 17, 2010 at p. 5-6.

sentence could be revised to suggest that a "portion of" or "equitable share" of these indirect costs should not be recovered through tariffed rates and it could reference the revenue sharing provision above. But the purpose of leaving the term "indirect" in Rule X.D. is to acknowledge the inverse -- some portion and types of indirect costs, as described in the definitions Rule II.F. should be recovered through the offering of NTP&S, whether through revenue sharing or another means.

III. CONCLUSION

Overall, CWA's Petition is procedurally improper and makes requests for changes that would violate the Commission's intent to adopt a comprehensive and effective set of affiliate transaction rules. While, as discussed above, the Rules could be revised based on some issues raised by CWA in its Petition, those changes should be narrowly tailored to meet the discussed concern. CWA's proposals, even where the Rules may need some clarification, are too broad.

_____/S/_____

Filed, April 25, 2011

Christine Mailloux
The Utility Reform Network
115 San Sansome Street, Suite 900
San Francisco, CA 94104
(415) 929-8876 (ext 353)
cmailloux@turn.org

CERTIFICATE OF SERVICE

I, Larry Wong, certify under penalty of perjury under the laws of the State of California that the following is true and correct:

On April 25, 2011, I served the attached:

RESPONSE OF THE UTILITY REFORM NETWORK TO THE PETITION FOR MODIFICATION OF D.10-10-019 OF THE CALIFORNIA WATER ASSOCIATION

on all eligible parties on the attached list **R.09-04-012** by sending said document by electronic mail to each of the parties via electronic mail, as reflected on the attached Service List.

Executed this April 25, 2011, at San Francisco, California.

/S/
Larry Wong

Service List for R.09-04-012

amx@cpuc.ca.gov
ayk@cpuc.ca.gov
bkelly@swwc.com
blake@consumercal.org
case.admin@sce.com
cem@newsdata.com
chh@cpuc.ca.gov
cmailloux@turn.org
cpolina@winston.com
dadellosa@sgvwater.com
dave.stephenson@amwater.com
des@cpuc.ca.gov
dmbatt@sgvwater.com
dmg@cpuc.ca.gov
DNiehaus@SempraUtilities.com
doug@parkwater.com
ed.jackson@parkwater.com
hsm@cpuc.ca.gov
jadarneylane@gswater.com
jef@cpuc.ca.gov
jeguzmanjr@gmail.com
jgaron@gswater.com
jhawks_cwa@comcast.net
jkarp@winston.com
joh@cpuc.ca.gov
KSwitzer@gswater.com
ldolqueist@manatt.com
leigh@parkwater.com
lmcghee@calwater.com
mlane@nossaman.com
mmattes@nossaman.com
nwales@calwater.com
olivia.para@bingham.com
palle_jensen@sjwater.com
rcosta@turn.org
robert.maclean@amwater.com
sarah.leeper@amwater.com
sharon.yang@sce.com
terry.houlihan@bingham.com
tjryan@sgvwater.com
tkaushik@manatt.com
tolea@swwc.com
tsmegal@calwater.com
wstrickland@bhfs.com
ypinedo@gswater.com