Decision ALTERNATE ORDER OF COMMISSIONER CARL WOOD
(Mailed March 7, 2002)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's Own Motion Into the Status, Rates, Rules, Operations, Service, Facilities, Contracts, and Practices of the Union Pacific Railroad Company in the Supply, Distribution, and Sale of Water by the Keene Water System to the Communities of Keene and Woodford in Kern County.	Investigation 00-05-020 (Filed May 18, 2000)

(See Appendix A for a list of appearances.)

INTERIM OPINION FINDING KEENE WATER SYSTEM DEDICATED TO PUBLIC USE

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This decision addresses the issue of whether the Keene Water System operated by Union Pacific Railroad Company (Union Pacific or Respondent) has been dedicated to public use. We find that a dedication has occurred and that Union Pacific is operating a public utility water system in the communities of Keene and Woodford in Kern County.

I. Procedural Background

On May 18, 2000, we issued an order instituting investigation (OII) to determine whether the Keene Water System, which is currently operated by Union Pacific, is a public utility water system, as defined by Section 2701 of the Public Utilities Code.[1]

This Commission has never regulated the Keene Water System as a public utility. However, based on the information in the declarations of employees of the Department of Health Services and of Commission staff member, the OII stated that the Keene Water System may by its conduct have become a public utility as described in Section 2701 and, thus, subject to the Commission's jurisdiction. Accordingly, the Commission, on its own motion, instituted this investigation.

As noted in exhibits to our investigation, this matter is also in Kern County Superior Court where the California Department of Health Services (DHS) has petitioned to appoint a receiver. DHS has found an individual who has experience in operating the Keene Water System and who has agreed to be appointed receiver. The court ordered Union Pacific not to abandon ownership of the Keene Water System, to continue to operate and maintain it, and to

[1] Unless otherwise stated, all statutory references are to the Public Utilities Code.

continue to provide water to existing residents and customers pending the results of the Commission's investigation and further hearing on the petition.

Today's decision examines whether the operation of the water system has changed over the intervening years, as the railroad's water use for railroad operations declined and ceased altogether, and the railroad entered into agreements with various customers and modified and updated the system.

Two days of hearings were held on February 13 - 14, 2001, and two public participation hearings were held on August 4, 2000, and January 29, 2001. No customers were present at the first PPH. At the second PPH, several customers, including Bridget Beard (Beard), expressed their concerns about poor water quality, resale prospects for their homes, and the connection of Tony Martin to the line as a special favor when others similarly situated had requested and been denied a direct connection. The following parties presented testimony: Union Pacific; the Office of Ratepayer Advocates, Water Branch (ORA); Stonybrook Corporation (Stonybrook); and Beard. The assigned administrative law judge granted Stonybrook and Beard leave to serve testimony late and ORA leave to serve supplemental testimony. Parties filed opening briefs on March 12, 2001, and reply briefs on March 19, 2001.

II. Historical Background

Union Pacific and its predecessor have operated the Keene Water System for over 80 years. Originally, the system served the railroad's steam locomotives. The Keene Water System is the sole remaining segment of Southern Pacific

Transportation Company's (SP)[2] former water supply line that ran from Tehachapi to Caliente. The water supply line was installed in the early 1900's.

During the era of steam locomotives, SP constructed, operated and maintained a water system mainly for the purpose of supplying water for steam locomotives and railroad facilities. A pipeline carried water from the City of Tehachapi to railroad facilities in Keene. During this time, the railroad provided water to a variety of users.

In the 1960's, with the retirement of steam locomotives, the railroad's need for water in the area substantially diminished. SP continued to supply water to its existing customers, and provided water to certain additional neighbors when they encountered difficulties with their own water supplies.

In 1972, this water supply system was deemed a public water system subject to the State's drinking water regulatory program, and a public water supply permit was issued to Keene Water System. The Kern County Environmental Health Services Department administered the State's Safe Drinking Water Programs for water systems in Kern County with fewer than 200 connections (such as Keene). On July 1, 1993, DHS assumed those responsibilities and commenced direct regulatory oversight of the safety of the Keene Water System's supply.[3]

Stonybrook filed a complaint at the Commission in 1989. We required SP to supply water to Stonybrook during the pendency of the complaint. We

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[2] In 1996, Union Pacific merged with SP, and thereby acquired the Keene Water System.

[3] Regulation by DHS is more limited than the regulation to which the Keene Water System would be subject if found to be a public utility. As a "public water system," the Keene Water system will continue to be subject to the State's drinking water standards regardless of whether it is a public utility.

dismissed the complaint in 1997, without prejudice, for lack of prosecution. Union Pacific's witness Whitcomb notes that Union Pacific continued to provide water to Stonybrook, as Union Pacific and Stonybrook worked to find a new owner for the Keene Water System.

III. Position of Union Pacific

In early 1994, SP abandoned the pipeline that brought water down the railroad's right of way from Tehachapi to Keene. Union Pacific alleges this occurred in order to lower tunnels on the rail line to allow for double stack containers carried on rail cars. The water line from Tehachapi was destroyed.

In 1994, following the removal of the water line, SP drilled new water supply wells in Keene, which were tied into the existing water storage and distribution system. In 1997, Union Pacific (which had merged with SP in 1996) performed substantial repairs to the system. At that time, Union Pacific was not using the water for its own needs. Union Pacific asserts it spent $609,226 to replace the original water distribution lines in order to bring the water system into compliance with the requirements imposed by DHS.

The record discloses several agreements under which SP or Union Pacific has provided water from the Keene Water System. A summary of these agreements is contained in Appendix A. Union Pacific argues that these agreements demonstrate that Union Pacific never intended to dedicate its water system to public use. Rather, Union Pacific contends that these agreements show an explicit intent to provide water only as an "accommodation" under Section 2704.

IV. Position of ORA

ORA contends that by "developing, storing, supplying, distributing and selling water for irrigational, municipal and domestic use" the Keene Water

System has become a public utility water system subject to the Commission's regulation. ORA argues that Union Pacific's claim that water is provided only as an accommodation should be dismissed because water was provided following abandonment in 1994 of the pipeline from Tehachapi.

Further, ORA argues that Union Pacific drilled new wells for the exclusive purpose of serving existing Keene Water System customers. ORA also argues that since Keene Water System no longer provides any service to Union Pacific, the system has been dedicated to public use.

V. Position of Stonybrook Corporation

Stonybrook asserts that the act of deliberately engaging in the business of producing and selling water to residents in Keene and Woodford constitutes a dedication of the Keene Water System for public use, and thereby subjects the system to the jurisdiction of this Commission.

Stonybrook also claims a dedication has occurred because the operation of the Keene Water System has been for the "sole and exclusive" benefit of the communities of Keene and Woodford. Further, a dedication has occurred because Union Pacific drilled new wells to provide water to the community of Keene and not to support any railroad operation. Specifically, Stonybrook asserts that by the abandonment of the Tehachapi pipeline in 1994 and the development of a new water system and sources so as to continue to supply water to Keene and Woodford customers, Union Pacific showed its intent to act as a public water utility regardless of its contractual relationships, and in fact dedicated its system for the public's benefit.

Stonybrook also asserts that Union Pacific's predecessor, SP, dedicated the Keene Water System facilities for public use when it submitted an application dated November 22, 1996, to the Kern County Board of Supervisors for a

non-exclusive road franchise agreement to construct a new delivery line for the Keene Water System, on a Kern County roadway. In its franchise application, SP represented to the Board of Supervisors that the new pipeline would be used to "furnish water for railroad use and for community use."

VI. Position of Beard

Beard contends that Union Pacific's operation of Keene Water System falls within the statutory definition of a water utility. Beard contends that Section 2704 does not exempt Union Pacific because the water is not "primarily used for domestic or industrial purposes" by Union Pacific. Beard argues that once the railroad was no longer the primary user of the water distributed by the Keene Water System, the railroad's sale of the water distributed by the Keene Water System no longer qualified as an "accommodation" as defined in Section 2704, and the railroad became a public utility under Section 2701.

VII. Discussion

Before we decide whether a dedication of property to public use has occurred, we note the impact our decision will have on the local community. The record reflects that most of the housing in Keene was built by the railroad for its employees. The railroad subsequently sold those houses to non-employees. Nothing provided prospective house buyers with constructive notice of the railroad's intention to provide the water strictly on a surplus basis and as an accommodation. Most current homeowners purchased their homes believing the railroad would continue to provide water for the community. Currently, the community is highly dependent on the Keene Water System for its water needs since every resident of Keene and Woodford except the U.S. Postal Services uses water from the Keene Water System.

The key issue is whether the Keene Water System is a "public utility" under the Public Utilities Code. If it is, the system comes under our jurisdiction. The Commission's power to regulate corporations operating water systems relies chiefly on Sections 216 and 2701. Sections 216 lists the different types of public utilities and includes, in relevant part:

> "(a) . . . every . . water corporation . . . where the service is performed for, or the commodity is delivered to, the public or any portion thereof.
>
> (b) Whenever any . . . water corporation . . . performs a service for, or delivers a commodity to, the public or any portion thereof for which any compensation or payment whatsoever is received, that . . . water corporation . . . is a public utility subject to the jurisdiction, control, and regulation of the commission and the provisions of this part."

Section 2701 defines a Commission-regulated water utility:

> "Any person, firm, or corporation … owning, controlling, operating, or managing any water system within this State, who sells, leases, rents, or delivers water to any person, firm, corporation, municipality, or any other political subdivision of the State, whether under contract or otherwise, is a public utility, and is subject to the provisions of Part 1 of Division 1 and to the jurisdiction, control, and regulation of the commission, except as otherwise provided in this chapter."

Sections 216 and 2701 must be read in conjunction with Section 2704, which contains exceptions to Commission jurisdiction, for situations where the owner of a water supply provides surplus water or water as an "accommodation":

> "Any owner of a water supply not otherwise dedicated to public use and primarily used for domestic or industrial purposes by him or for the irrigation of his lands, who (a) sells or delivers the surplus of such water . . . or (c) sells or delivers a portion of such water supply as a matter of accommodation to neighbors to whom no other supply of water . . . is equally

> available, is not subject to the jurisdiction, control, and regulation of the commission."

Another exception to Commission jurisdiction results from judicial decisions. Specifically, in 1912, the California Supreme Court applied a requirement of common law, not expressed in these statutes today or as previously codified, that conditions public utility status on the "dedication" of utility property to the public use. (See *Thayer v California Development Co.* (1912) 164 Cal. 117.) Later, in *Allen v. Railroad Commission* (1918) 179 Cal. 68, 85, the Court wrote that "to hold property has been dedicated to public use is not trivial thing . . . and such dedication is never presumed without evidence of unequivocal intention." The Court later explained that the act of dedication occurs if someone had:

> "held himself out, expressly or impliedly, as engaged in the business of supplying [a service or commodity] to the public as a class, not necessarily to all of the public, but to any limited portion of it, such portion, for example, as could be served by his own system, as counterdistinguished from his holding himself out as serving or ready to serve only particular individuals, either as a matter of accommodation or for other reasons peculiar and particular to them."
> (*Van Hoosear v Railroad Commission* (1920) 184 Cal. 553, 554.)

In *Richfield Oil Corp. v Public Utilities Commission* (1960) 54 Cal.2d 419, the Court reviewed the case law and left the dedication doctrine intact. The Court concluded that "the Legislature by its repeated reenactment of the definitions of the public utilities without change has accepted and adopted dedication as an implicit limitation on their terms." (*Id.* at 430.)

While we acknowledge that dedication is a prerequisite to declaring a water system to be a public utility, dedication can be manifested in many different ways. Whether or not dedication has occurred is a factual question.

(*Haynes v. MacFarlane* (1929) 207 Cal. 529, 532.) Where dedication has occurred, it may be either express or implied, and in the latter case, "it may be inferred from the acts of the owner and his dealings and relations to the property." (*Cal. Water & Tel. Co. v. Public Utilities Commission* (1959) 51 Cal.2d 478, 494; see also *Yucaipa Water Co. No. 1 v. Public Utilities Commission* (1960) 54 Cal.2d 823.)

Neither Union Pacific nor its predecessor has manifested an *express* intent to dedicate the Keene Water System to public use. To the contrary, the agreements contained in Appendix A reflect a written intent on the part of Union Pacific and its predecessor to provide water only as an accommodation. Therefore, if we are to find that a dedication has occurred, it must be implied from the acts of Union Pacific or its predecessor. Here, there is a long course of conduct by Union Pacific and SP from which implied dedication arises. For example:

- since the 1960s, water has been sold for the primary use of the community and not the railroad;
- in 1994, existing plant was removed and replaced with a new well for the primary benefit of the community and not the railroad; and
- in 1996, SP applied for a non-exclusive franchise agreement to construct a pipeline on county roadway to furnish water for railroad and community use.

In this instance and many others, the Commission and the courts have found dedication implied by conduct. For instance, in *Producers Transp. Co. v. Railroad Commission* (1917) 176 Cal. 499, the dedication of an oil pipeline to a public use was implied from the corporation installing the pipeline via eminent domain. This case parallels *Producers Transportation*. There, the Court stated that a "potent reason" for upholding the finding of implied dedication was the fact that petitioner availed itself of the right of eminent domain in condemning

property for the right of way over which it constructed its pipeline. The Court stated such action:

> must be deemed conclusive evidence of a dedication of such property to public use, since it could not have exercised such right other than in "behalf of a public use" (Code Civ. Proc., sec. 1238), as "an agent of the state or person in charge of such use." (Civ. Code, sec. 1001.)

A similar rationale applies to franchises. Municipalities grant franchises for the purpose of furnishing a service or commodity for the public use. (*See* Cal. Gov. Code Section 26001.)[4] Public use is defined as "a use which concerns the whole community or promotes the general interest in its relation to any legitimate object of government." (*Bauer v. County of Ventura* (1955) 45 Cal.2d 276, 284.) Thus, the exercise of a franchise right to install a water line is tantamount to a declaration that such property is for public use. By requesting a franchise from Kern County to build a water pipeline to furnish water for community use, Union Pacific's predecessors implicitly dedicated the water pipeline to public use.[5]

Having found that a dedication has occurred, we conclude that the Keene Water System falls under the jurisdiction of this Commission as a water utility. Further, we agree with Beard that Section 2704 does not exempt

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[4] Cal. Gov. Code § 26001 says in relevant part,

"Any general law applicable to the granting of franchises by municipal corporations and counties throughout the State for purposes involving the furnishing of any service or commodity to the public or any portion thereof shall be complied with in the granting of any franchises by the board of supervisors."

[5] Although the franchise application states that the water pipeline will also serve the railroad, the record shows that the railroad has not primarily used its water for its own purposes since the 1960's.

Union Pacific. Section 2704 only exempts an owner of a water supply from Commission jurisdiction if such water supply is "primarily used for domestic or industrial purposes" by the owner of the water supply or for the irrigation of the owner's lands. Union Pacific, as operator of the Keene Water System, and its predecessor cannot claim an exemption under Section 2704 since they have not been the primary user of the water supply for almost four decades.

We therefore hold that the Keene Water System is a water utility subject to our jurisdiction. Until further notice, Union Pacific should continue to serve all existing customers as of May 18, 2000, when we initiated this OII.

VIII. Remaining Issues

In this investigation we stated we would determine whether:

- The terms and conditions of Union Pacific's service are just and reasonable;
- Union Pacific should file tariffs for furnishing water; and
- Union Pacific's abandonment of service would be in the public interest.

A. Water Rate

Union Pacific currently charges customers $4.00 per thousand gallons of water used. Union Pacific requests that the Commission establish a new rate of $21.42 per thousand gallons. ORA proposes a rate of $11.80 per thousand gallons for residential customers.

Union Pacific determined its total costs as follows:

Operating Costs	$152,752
Depreciation	$20,543
Return on Capital (9%)	$55,468
TOTAL COST	**$228,763**

1. Operating Cost

Union Pacific used 1999 recorded costs of $152,752 to determine its operating costs. For comparison purposes, Union Pacific provided incomplete cost data for 1997 and 1998 as well as eleven months of recorded cost information ($149,750) for 2000. Union Pacific broke down its operating costs into 10 cost categories and provided background description for such costs.

ORA challenges Union Pacific's request in two ways. First, it notes that Union Pacific has failed to show that these expenses are reasonably incurred. It refers to three recent Commission approved revenue requirements for other systems ranging in size from 45 service connections to 250 service connections. Although water systems vary enormously in their costs basis, and system cannot be easily compared, the 250 customer system requires only $60,000 in operating expenses per year.

2. Depreciation and Return on Capital

Union Pacific reports $616,313 in capital expenditures incurred in 1997 and 2000. In 1997, Union Pacific asserts it incurred capital improvement costs of $609,226 for replacement of a water line from its storage tank to customer meters. In 2000, Union Pacific states it incurred capital improvement costs of $7,087 for replacement of a water line over Three Peaks Ranch.

Union Pacific also asserts that it made these capital expenditures to bring the water system into compliance with DHS requirements and address the deteriorating condition of 100 year old line. Union Pacific provided a letter from DHS concerning the water line that was the subject of the year 2000 improvement. The letter confirms a conversation with a property owner (not

Union Pacific) and primarily emphasizes health issues over drinking water quality.

ORA points out that costs of the pipeline relocation that make up the majority of the rate base also resulted in the pipeline being removed from Union Pacific's right-of-way, which was beneficial to the railroad, indication that some apportioning of these costs may be appropriate.

3. Water Consumption

Union Pacific projected water consumption of 10,680,854 gallons for year 2000.[6] However, Union Pacific contends in its initial testimony (Exhibit 3) that water consumption should be adjusted in calculating rates to account for the fact that one customer, the Edwards Family (which owns the Three Peaks Ranch), receives approximately 48,000 gallons of free water per month. Further, Union Pacific believes water consumption should be adjusted if the Commission finds that Union Pacific is not obligated to serve particular customers.

ORA established during cross-examination of Union Pacific's witness, Mr. Lyon, that Union Pacific provided free water to customer Edwards in exchange for the railroad having access across the Edwards property. Lyon testified during ORA's cross-examination that such access provides a benefit to the railroad by giving it access to railroad property that the railroad may not be able to get to on its own right-of-way roads. Lyon testified that the water system might also benefit because "a piece of the water line" goes across the Edwards property and serves two customers, including Edwards.

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[6] Union Pacific used actual consumption amount for January 2000 through November 2000 of 9,859,250 and projected December 2000 consumption of 821,604 gallons.

Union Pacific clearly benefits from providing free water to Edwards. Union Pacific admits use of a right-of-way for its own railroad operations. Union Pacific's claim that the customers of the water system benefit from giving free water to Edwards is not persuasive. Union Pacific's lack of detail on the necessity of running a line on the Edward's property in order to serve the Cummings Ranch is not persuasive. The situation is analogous to the railroad bartering water for a service or benefit. To the extent Edwards takes water from the Keene Water System, Union Pacific should pay for the cost of such water since it receives a benefit from Edwards.

4. Water Rates

Clearly, this proceeding does not have an adequate record to set proper rates. Union Pacific is operating the system at rates it established. There is no reason at this time to increase them.

B. Abandonment of Service

Although we stated in the OII we would consider abandonment of service, Union Pacific did not submit sufficient testimony to address the impact on customers from abandonment. Union Pacific may file an application to transfer the system.

IX. Objections to Stonybrook's Testimony

Union Pacific objected to the admission of portions of Stonybrook's testimony. We agree with Union Pacific, and will strike those portions of Stonybrook's testimony identified by Union Pacific as argumentative and legal conclusion.

On July 11, 2001, Union Pacific also filed a motion requesting permission to suspend service to two customers. In a letter dated July 27, 2001, Union Pacific withdrew its motion.

X. Comments on Proposed Decision

On November 19, 2001, the principal hearing officer's proposed decision was filed with the Commission and served on the parties in accordance with Section 311(d) of the Public Utilities Code and Rule 77.1 of the Commission's Rules of Practice and Procedure. Comments were filed by Union Pacific on January 9, 2002. We discuss those comments below.

A. Estoppel

Union Pacific contends that the Commission is estopped from asserting jurisdiction over Union Pacific in relation to its operation of the Keene Water System. Union Pacific states that the Commission is estopped because the Commission previously held in D.97-09-014 that the Keene Water System is not a public utility system and nothing has changed since that holding was made.

The standard for estoppel is as follows:

> Generally speaking, four elements must be present in order to apply the doctrine of equitable estoppel: (1) the party to be estopped must be apprised of the facts; (2) he must intend that his conduct shall be acted upon, or must so act that the party asserting the estoppel had a right to believe it was so intended: (3) the other party must be ignorant of the true state of facts; and (4) he must rely upon the conduct to his injury.

(Driscoll v. City of Los Angeles (1967) 67 Cal.2d 297, 305.) In the case of estoppel against a government agency the person asserting estoppel must also "demonstrate that the injury to his personal interest if the government is not estopped exceeds the injury to the public interest if the government is estopped." (Stewart v. City of Pismo Beach (1995) 35 Cal.App.4th 1600, 1607.)

In this instance, Union Pacific fails to meet the second prong for establishing estoppel. Union Pacific appears to suggest that the Commission is estopped by D.97-09-014 from exercising jurisdiction over Union Pacific with

respect to its operation of Keene Water System. Union Pacific places far too much weight on D.97-09-014. In C.89-06-051, the docket was inactive for approximately six years.[7] The specific conduct or action the Commission took in D.97-09-014 was to order dismissal of C.89-06-051 without prejudice for lack of prosecution. We find that a Commission order dismissing a case without prejudice for lack of prosecution fails to establish conduct upon which the Commission can be estopped from exercising jurisdiction over Union Pacific concerning its operation of the Keene Water system.

Even assuming the Commission were estopped from relying on Union Pacific's conduct prior to 1991 in exercising jurisdiction over Union Pacific. Such an estoppel would not immunize Union Pacific from being found a water utility for conduct occurring subsequent to 1991. In fact, the OII acknowledged D.97-09-014 and stated that a review of D.97-09-014 and D.75769 (a prior complaint) reveals that neither complaint against SP was resolved on the merits. The OII stated:

> Both cases were truncated and the Commission never reached the question of SP's public utility status. Because the Commission's 1997 decision (D.97-09-014) does not reveal the changes in SP's water service activities that occurred during the 1990's.

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[7] C.89-06-051 was filed on June 26, 1989, the National Farm Workers Service Center (the service center is now occupied by Stoneybrook Corporation) asserted among other things that SP had dedicated portions of the Keene Water system to the public use. Further, the Farm Workers asserted that such dedication rendered SP a water public utility with respect to the operations of the Keene Water System. In C.89-06-051, the parties requested time for discovery leading to a possible motion for a possible summary judgment for SP. It appears that no such motion was ever made and D.97-09-014 was subsequently issued on September 3, 1997, dismissing the case without prejudice for lack of prosecution.

Thus, the OII stated that activities in the 1990's may have relevance on the status of the railroad as a public utility with respect to its operation of the water system.

B. Customers

Union Pacific asserts that the PD fails to specify which customers should be served. Union Pacific contends that all customers are not similarly situated and that all are not entitled to water service. In support of its position, Union Pacific cites an agreement with Steve Cummings not to supply water and also D.97-09-014 for the proposition that Stonybrook is estopped from establishing a right to receive water.

As discussed above, D.97-09-014 dismissed a complaint without prejudice for lack of prosecution. It should not provide a basis for terminating service to Stonybrook. In this proceeding, we did not single out any existing customer for termination of service in the event the Keene Water System was found to be a water utility. Union Pacific should continue to provide water to all existing customers as of the date of the initiation of this OII so long as the water consumed is paid for.

C. Abandonment of Service

Union Pacific asserts that the PD fails to address Union Pacific's proposed abandonment of service. In its comments Union Pacific cites the following testimony to support its request for abandonment:

> "As the Commission has recognized, the railroad has long desired to terminate its involvement with the water system, and it should be permitted to abandon the system." (Exhibit 3 at page 21.)

In this proceeding the Commission stated it would consider the issue of abandonment and further provided the parties an opportunity to address the

issue of abandonment of service in the event Union Pacific was found to be a water utility with respect to its operation of the Keene Water System. However, Union Pacific did not present sufficient evidence for the Commission to consider this issue. The one sentence of testimony identified by Union Pacific clearly expresses its desire to abandon service but does not provide a basis for allowing an abandonment of service. This decision has clarified the state of the record regarding abandonment. In fact, that Union Pacific provided insufficient testimony to justify abandonment of the Keene Water System.

D. Dedication

Union Pacific asserts that the evidence does not support the PD's finding of implied dedication. Union Pacific suggests that the railroad's application requesting a franchise from Kern County to build a water pipeline is insufficient evidence to conclude that a dedication has occurred.

Union Pacific contends that the PD too narrowly interprets Gov. Code Section 26001. Union Pacific argues that a franchise may be granted for "all lawful purposes," not uses limited to the "public use" as the PD suggests. Thus, Union Pacific argues that a franchise may be granted for purposes other than "public use." Consequently, Union Pacific explains that the railroad simply applied for the "privilege" of placing a new water pipeline along the county roadway in order to address the concerns of DHS over the condition of the existing water main.

Although, Union Pacific offers a broader statutory interpretation of Gov. Code Section 26001, it offers no specific examples of franchises being granted which do not involve "public use" or discuss "privileges." However, we need not resolve that issue here because the facts are inconsistent with Union Pacific's position. The railroad's application for a franchise does not

mention the concerns of DHS. Further, Union Pacific's franchise application states that the pipeline is to furnish water for "community use." Moreover the railroad states that in the franchise application that the existing line is not in the count right-of-way. The record does not contain any documented directive from DHS to replace an existing pipeline on county roadway.

Although Union Pacific offers a theoretical alternative interpretation of Gov. Code Section 26001, the facts of this case still support a conclusion that the railroad dedicated the water pipeline when it made representations of community use in applying for a franchise to locate a pipeline on county roads.

E. Rates

Union Pacific contends that the PD arbitrarily and unconstitutionally fails to establish water rates reflective of the costs of providing service and capital expenditures. Union Pacific contends that the issue of establishing a water rate for the system is a central part of this proceeding since its inception. Union Pacific observes that the ALJ and parties agreed at the August 4, 2000 PHC, that the evidentiary hearing should be delayed until February 2001, so that parties could address rates.

Unfortunately, despite the efforts of ORA and Union Pacific, the record is inadequate to properly set rates. At a minimum ratemaking requires an audit (formal or informal), a results of operations report, a public meeting, a summary of earnings, properly designed rates and adopted quantities[8]. The record in this proceeding contains only a summary of earnings and a public meeting.

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[8] These requirements have been in place for well over twenty years and are presently reflected in Water Division Standard Practices U-3-SM and U-9-SM available from the CPUC website at

Footnote continued on next page

Furthermore, in establishing rates for all water utilities, the requirements of sections 739.8 and 728 of the Public Utility Code must be considered. Section 739.8 requires that rates be affordable. Section 728 prohibits discriminatory or preferential rates. In the past, the Commission has determined that in circumstances where free water is provided to some customers while filed rates are charged to other customers, the free rates may be unreasonably discriminatory (See *Application of Francis Land and Water Co.* (1961) 58 Cal. P.U.C. 506). In this case, Union Pacific provides free rates to at least one customer, single metered rates to some customers and further, a shared meter rate to several, unrelated customers in separate dwellings under circumstances where no individual party or dwelling can ascertain individual usage. Such a plan could be discriminatory. Therefore, the question of discrimination as well as the issue of whether rates are affordable for Keene ratepayers must be addressed. With respect to the rates proposed by Union Pacific, the record in this proceeding does not address these issues.

Finally, the rate base upon which Union Pacific seeks to earn a rate of return is a curiosity that has not been explained. It would seem that the intent of the Union Pacific's financial expenditure at the time it was made should influence, if not determine, the character of the expenditure as an investment or as a contribution of plant. In all of the plant expenditures, it is reasonable for one to ask: (1) Did the expenditure benefit the railroad in fact, (either as a quid pro quo for rights of way of some customers or simply as a designated business loss in the financial records or taxes of the railroad)? (2) Did the railroad ever signal

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http://www.cpuc.ca.gov/static/industry/water/downloadable+reports/water+standard+practices/index.htm.

its expectation of the plant expenditures as investments by seeking reimbursement or a return on investment in the rates that it did charge the customers? and, (3) What implications reasonably can be drawn about the character of the financial expenditures when the railroad notified customers of its intent to walk away from the water utility?

When it comes to ratemaking, Union Pacific's Keene Water System is an anomaly. Union Pacific's revenues are significantly greater than any class A water utility. Yet as a water purveyor, it serves 50 customers placing it among the smallest class D water utilities. It is axiomatic that the rate design and ratemaking for class A and class D water companies differ in complexity and regulatory expectations. The distinctions in ratemaking employed by this Commission for small and large water utilities are beneficial to the utility and to its respective ratepayers. Because the Water Division staff has expertise in the development of rates for small water companies, we shall request their assistance in addressing the ratemaking issues that we have discussed in a ratemaking report which shall include rate proposals for the Keene Water System. Said report shall be submitted to the Administrative Law Judge in this proceeding by September 6, 2002. All parties shall have an opportunity to comment on the Water Division report.

F. Keene Housing

Union Pacific objects to the discussion in the PD concerning housing in Keene. The PD states that:

> "The record reflects that most of the housing in Keene was built by the railroad for its employees. The railroad subsequently sold those houses to non-employees. Nothing provided prospective house buyers with constructive notice of the railroad's intention to provide the water strictly on a surplus basis and as an

> accommodation. Most current homeowners purchased their homes believing the railroad would continue to provide water for the community."

Further, finding of fact number 8 states:

> "Most current homeowners purchased their homes believing the railroad would continue to supply water to the Community."

The discussion and finding of fact 8 stem from the testimony of Brigit Beard whose testimony is based upon discussions with her neighbors. Union Pacific contends that reliance upon such hearsay fails to preserve its substantial rights. Additionally, Union Pacific asserts that the discussion and proposed finding do not clearly relate to the issues of this case. Lastly, Union Pacific also makes a procedural objection to the admission of Beard's testimony.[9]

We do not agree with the suggestion that hearsay testimony automatically precludes admission of testimony. We observe that much of the testimony of Union's Pacific's witness Lyon is based on hearsay conversations with former employees. Also we do not agree with Union Pacific that finding of fact 8 has minor relevance to the issues we resolve. Union Pacific does not dispute the fact that, when the railroad sold housing that included water service to non-employees, that the new owners had a reasonable expectation that water service would continue to be provided by the water purveyer, the railroad. Accordingly, we will maintain finding of fact 8.

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[9] Union Pacific also appears to object to the admission of testimony submitted by Stonybrook. However, Union Pacific filed a motion to strike the testimony of Stonybrook which the PD granted. Thus, we fail to understand Union Pacific's objection concerning Stonybrook.

Findings of Fact

1. Over 80 years ago, SP constructed, operated, and maintained a water system for the purpose of supplying water for steam locomotives and railroad facilities. A pipeline carried water from Tehachapi to Keene and Caliente.

2. In the 1960's, SP's need for water substantially diminished with the retirement of steam locomotives.

3. Starting in the 1990's, and continuing to the present time, the Keene Water System was and is not primarily used by SP or Union Pacific for their own domestic or industrial purposes or for the irrigation of lands owned by SP or Union Pacific.

4. In 1994, SP abandoned the pipeline from Tehachapi to Keene.

5. In 1994, SP drilled new water supply wells in Keene.

6. In 1996, SP applied for a nonexclusive franchise to build a water pipeline for community use.

7. Union Pacific (after merging with SP) performed substantial repairs to the water system in 1997, at a time when the system was no longer used in railroad operations.

8. Most current homeowners purchased their homes believing the railroad would continue to supply water to the Community.

9. D.97-09-014 dismissed C.89-06-051 without prejudice for lack of prosecution.

10. The Edwards Family who owns the Three Peaks Ranch receives free water service from Union Pacific.

11. Edwards or Union Pacific should pay for water delivered from the Keene Water System to Edwards or the Three Peaks Ranch.

12. Union Pacific benefits from having access across the Edwards property.

13. Union Pacific is operating the system at rates that it established.

14. The testimony of Stonybrook contains legal argument.

Conclusions of Law

1. To constitute a public utility, there must be a "dedication" of property to the public use. Dedication may be express or may be implied from conduct.

2. Based on the conduct of Union Pacific and SP, the Keene Water System has been dedicated to public use.

3. The Keene Water System is a public utility water system under Section 2701.

4. Section 2704 does not exempt the Keene Water System from Commission regulation.

5. D.97-09-014 does not estoppe the Commission from exercising jurisdiction over the operation of the Keene Water system.

6. Union Pacific should continue to provide water to all existing customers as of the date of the initiation of this OII so long as the water consumed is paid for.

7. Union Pacific did not present sufficient evidence for the Commission to consider the issue of abandonment.

8. The fact that Edwards Family and Three Peaks Ranch receives free water service from Union Pacific should be considered in the development of rates for the Keene Water System.

9. The record is insufficient to establish just and reasonable rates for water service.

10. Water rates should not change at this time.

11. Water Division's expertise in developing rates for small water companies should be employed to address the establishment of rates for the Keene Water System.

12. The Director of the Water Division should analyze Union Pacific's proposed rates and prepare a report on the rates appropriate for the Keene Water System and submit said report by September 6, 2002.

13. Today's decision should be made effective immediately so that the operation of the Keene Water System may be swiftly brought into conformity with statutes and regulations governing public utilities.

O R D E R

IT IS ORDERED that:

1. Union Pacific shall continue to serve all existing water customers.
2. Union Pacific may file an application to transfer the Keene Water System.
3. The motion of Union Pacific to strike portions of the testimony of Stonybrook Corporation is granted in full.
4. The Director of the Water Division shall prepare a ratemaking report on Union Pacific's Keene Water System, including proposed rates and a discussion of the rate issues raised in this decision by September 6, 2002.
5. Union Pacific Railroad shall cooperate in providing the Water Division with information requested for the purpose of completion of the Water Division's ratemaking report on the Keene Water System.
6. This proceeding will remain open to consider the rates proposed by the Water Division.

This order is effective today.

Dated _____, at San Francisco, California.

APPENDIX A:
List of Appearances

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(END OF APPENDIX A)