STATE OF CALIFORNIA ARNOLD SCHWARZENEGGER, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

June 9, 2009 File No.: 602-19

TO: All Interested Parties

Enclosed is draft Resolution W-4768 of the Division of Water and Audits. It will be on the Commission's July 9, 2009 agenda. The Commission may then act on this Resolution or it may postpone action until later.

When the Commission acts on the draft resolution, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare a different resolution. Only when the Commission acts does the resolution become binding on the parties.

Parties to this matter may file comments on this draft resolution. An original and 2 copies of the comments, with a certificate of service, should be submitted to:

Division of Water and Audits, Third Floor
Attention: James Boothe
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Parties may submit comments on or before July 2, 2009. The date of submission is the date the comments are received by the Division of Water and Audits. Parties must serve a copy of their comments on Suburban Water Systems on the same date that the comments are submitted to the Division of Water and Audits.

Comments shall be limited to five pages in length plus a subject index listing the recommended changes to the draft resolution, a table of authorities and appendix setting forth the proposed findings and ordering paragraphs.

Comments shall focus on factual, legal or technical errors in the draft resolution, and shall make specific reference to the record or applicable law. Comments which fail to do so will be accorded no weight and are not to be submitted.

Persons interested in comments of parties may write to James Boothe or telephone him at (415) 703-1748.

/s/ RAMI KAHLON
Rami Kahlon, Director
Division of Water and Audits

Enclosures: Draft Resolution W-4768
Certificate of Service
Service List

DRAFT

AGENDA ITEM #8614

DWA/JB5/TKM/jlj

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

DIVISION OF WATER AND AUDITS **RESOLUTION NO. W-4768**
Water and Sewer Advisory Branch **JULY 9, 2009**

R E S O L U T I O N

(RES. W-4768), SUBURBAN WATER SYSTEMS (SUBURBAN). ORDER REJECTING REQUEST TO ESTABLISH A HOLDING COMPANY PROCEEDING MEMORANDUM ACCOUNT AND AN AFFILIATE TRANSACTION RULES PROCEEDING MEMORANDUM ACCOUNT.

By Advice Letters Nos. 262-W and 263-W, filed on April 24, 2009.

SUMMARY

This Resolution denies Suburban Water Systems (Suburban) the authority requested in Advice Letters Nos. 262-W and 263-W to establish memorandum accounts to track expenses associated with its participation in its Holding Company Application and the Affiliate Transaction Rulemaking, R.09-04-012.

Suburban submitted these advice letters with a Tier 2 designation in accordance with Industry Rule 7.3.2 of General Order 96-B. Suburban requested that these advice letters become effective upon staff approval, but no latter than May 25, 2009. However, in Application (A.) 06-11-010, Suburban requested a similar memorandum account to track costs for developing and establishing a conservation rate design, including legal and consulting services associated with its consolidated application. In Decision (D.) 08-02-036, the Commission stated that further requests for memorandum accounts to track costs associated with participating in generic proceedings shall be made by advice letter and the Division of Water and Audits (DWA) shall prepare a resolution for the Commission's consideration. See D.08-02-036 at p.45. Based on this direction, Advice Letters Nos. 262-W and 263-W are being processed as Tier 3 filings requiring Commission resolution. On May 8, 2009, DWA suspended Advice Letters Nos. 262-W

and 263-W to provide time for this Resolution to be drafted for the Commission's consideration.

BACKGROUND

On March 12, 2009, the Commission issued D.09-03-007, authorizing a general rate increase for Suburban and approving a related Settlement Agreement with the Division of Ratepayer Advocates (DRA). Ordering Paragraph 4 of the decision stated: "*Suburban shall file a formal application within 120 days of the effective date of today's decision to establish a holding company.*" Suburban filed Advice Letter No. 262-W on April 24, 2009 requesting establishment of a Holding Company Proceeding Memorandum Account (HCPMA) to track the costs of participating in its Holding Company Application proceeding.[1]

On April 16, 2009, the Commission issued Rulemaking (R.) 09-04-012 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. Suburban filed Advice Letter No. 263-W on April 24, 2009, requesting establishment of an Affiliate Transaction Rules Proceeding Memorandum Account (ATRPMA) to track the legal, consulting, and related costs that Suburban will incur in R.09-04-012.[2]

On May 14, 2009, DRA protested Advice Letters Nos. 262-W and 263-W. DRA's objects that Suburban's requests fail to satisfy several of the criteria for establishing a memorandum account as outlined in the Commission's Standard Practice U-27-W.

The Commission has established a four-pronged test to determine if a memorandum account is appropriate for tracking specific expenses for future consideration of their

[1] Advice Letter No. 262-W states "Suburban will need the assistance of outside legal counsel and establishment to participate in the proceeding." (Advice Letter No. 262-W at p. 1)
[2] Advice Letter No. 263-W states "Suburban will participate in this proceeding, and because of the complexity of the issues, Suburban will need the assistance of outside legal counsel." (Advice Letter No. 263-W at p. 1)

recovery in utility rates. Res. W-4276 states that memorandum accounts are appropriate when the following conditions are met:

1. The expense is caused by an event of an exceptional nature that is not under the utility's control;
2. The expense could not have been reasonably foreseen in the utility's last general rate case and will occur before the utility's next scheduled rate case;
3. The expense is of a substantial nature in the amount of money involved; and
4. The ratepayers will benefit by the memorandum account treatment.[3]

The four-prong test is included as part of the Commission's Standard Practice U-27-W for establishing memorandum accounts.

DISCUSSION

In determining whether to authorize memorandum accounts for costs associated with Suburban's participation in its Holding Company Application and the Affiliate Transaction Rulemaking, we look to see if the above four prongs are met.

What are the timing for expenses associated with these proceedings?
The first and second prongs of the test refer to expenses caused by events of an exceptional nature that is not under Suburban's control that will occur between general rate cases and which were unforeseeable. The expense of Suburban's participation in both its Holding Company Application and the Affiliate Transaction Rulemaking will occur after its latest rate case filed in A.08-01-044 and before its next schedule rate case filing in January 2011.

Were these proceedings foreseeable and are they exceptional?
Though these two proceedings may have not been foreseeable in the particular timeframe they are occurring, they should have been foreseeable generally given our past action on approving holding company structure and devising affiliate transaction rules for utilities in general and the water utility industry in particular. Suburban has been operating under a holding company structure without Commission authorization for over 30 years. With regard to affiliate transaction rules, five of the nine Class A water utilities have Commission authorized rules in place. In Suburban's last general rate case, holding company and affiliate transaction issues were both contested issues.

[3] Recently, in D.08-03-020, the Commission used the four-prong test in addressing memorandum account treatment for California Water Services (mimeo at p. 18).

The foreseeable issue is a close call in our minds. If this were the only issue with these Advice Letters, we would likely authorize their approval. However, we have other concerns with establishing these memorandum accounts as discussed below. Further, given our past attention to both holding company and affiliate transaction issues for Suburban as recently as our decision in Suburban's most recent general rate case, D.09-03-007, it is difficult for us to categorize the expense of participating in these proceedings as exceptional in nature.

Is the expense of Suburban's participation in these proceedings under its control?
There is no requirement that Suburban participate in the Rulemaking to establish standard rules for affiliate transactions for the water utility industry. Suburban's participation is permissive and clearly under its control.

In D.09-03-007 we ordered Suburban to file an application to establish a holding company, an organizational structure it has been operating under since 1976. Participation is this proceeding is clearly mandatory. As the moving party, much of the cost of its participation is under Suburban's control. Further, by removing affiliate transaction rules to the Rulemaking, this should reduce both the contentiousness and the costs outside Suburban's control of participating in this proceeding.

Is the expense of a substantial nature?
The third prong of the test requires a showing that the expense to be tracked in the memorandum account is of a substantial nature in the amount of money involved. Suburban argues its participation "is expected to be substantial due to the complexity of the issues, and possible intervenors."[4] However, Suburban's showing is devoid of any evidence to satisfy this prong. We do not view the modest cost of processing a routine holding company application as requiring the establishment of a memorandum account. Similarly, the cost of participating in an industry-wide Rulemaking with eight other like-minded utilities where the Commission already has several guidelines in place should not place a heavy financial burden on Suburban's participation.

Is there a ratepayer benefit by the memorandum account treatment?
Suburban argues that "the ratepayers will benefit by memorandum account treatment because these necessary costs will be normalized and spread over a reasonable period of time."[5] The benefits of a holding company structure inure primarily to the benefit of Suburban's parent company and other affiliates. Similarly, Suburban's participation in

[4] Advice Letter Nos. 262-W and 263-W at p.2.
[5] Ibid., p. 2.

the Affiliate Transaction Rulemaking is primarily for the benefit of its parent company and other affiliates. In neither proceeding has Suburban shown that ratepayer interest is the focus of its participation. As such, we do not find a ratepayer benefit associated with establishing memorandum accounts to track expenses for efforts primarily directed for the benefit of Suburban's parent company or other affiliates.

Conclusion

Suburban's showing on the need to establish memorandum accounts for its participation in its Holding Company Application and the Affiliate Transaction Rulemaking fails to satisfy three of the four prongs necessary for establishing memorandum accounts. Beyond the fact that these expenses will be incurred between rate cases, Suburban has failed to provide convincing evidence that would satisfy the remaining three prongs required to establish memorandum accounts. As such, Advice Letters Nos. 262-W and 263-W must be rejected as inconsistent with our direction and criteria for establishing memorandum accounts.

NOTICE

In compliance with Section 4 of General Order 96-B, a copy of Advice Letters Nos. 262-W and 263-W were mailed to all interested and affected parties as listed in Attachment A to the Advice Letters.

COMMENTS ON DRAFT RESOLUTION

This is a contested matter. Pursuant to Public Utilities Code under § 311(g) (1), the draft resolution was mailed for a 30-day period of public review and comment on June 9, 2009. Comments were received from _____ and reply comments from _____.

FINDINGS

1. Suburban Water Systems requests authority to establish memorandum accounts to track the cost of its participation in its Holding Company Application and the Affiliate Transaction Rulemaking.

2. Suburban Water Systems filed Advice Letters Nos. 262-W and 263-W as Tier 2 filings.

3. Pursuant to Decision 08-02-036, Advice Letters Nos. 262-W and 263-W are Tier 3 filings requiring Commission resolution.

4. The Division of Water and Audits suspended Advice Letters Nos. 262-W and 263-W on May 8, 2009.

5. On May 14, 2009, the Division of Ratepayer Advocates filed timely protests to Advice Letters Nos. 262-W and 263-W.

6. The Commission has a four-prong test for determining if a memorandum account is appropriate for tracking specific expenses. The four-prong test is outlined in Resolution W-4276 and Decision 08-03-020.

7. The expenses Suburban Water Systems will incur in its Holding Company Application and the Affiliate Transaction Rulemaking will occur after its most recent general rate case and before its next scheduled general rate case.

8. Suburban Water Systems' participation in its Holding Company Application and the Affiliate Transaction Rulemaking are standard regulatory proceedings where the cost of participation is wholly under Suburban Water Systems' control for the Affiliate Transaction Rulemaking and partially under its control for its Holding Company Application.

9. Holding company and affiliate transaction issues are commonly-addressed regulatory issues. For Suburban Water Systems, both of these issues were addressed in its most recent general rate case, Decision 09-03-007.

10. Suburban Water Systems' has not shown that its participation in its Holding Company Application and the Affiliate Transaction Rulemaking is an event of an exceptional nature.

11. Suburban Water Systems has provided no evidence that its participation in its Holding Company Application and the Affiliate Transaction Rulemaking will result in an expense of a substantial nature in the amount of money involved.

12. Suburban Water Systems' participation in its Holding Company Application and the Affiliate Transaction Rulemaking is primarily for the benefit of its parent company and other affiliates.

13. Suburban Water Systems has not shown that ratepayers will benefit from the establishment of memorandum accounts to record expenses of its participation in its Holding Company Application and the Affiliate Transaction Rulemaking.

14. Suburban Water Systems has failed to satisfy three of the four prongs to determine if memorandum accounts are appropriate for tracking expenses associated with its participation in its Holding Company Application and the Affiliate Transaction Rulemaking.

15. This is a contested matter subject to the public notice comment provided for in Public Utilities Code § 311(g) (1).

16. Suburban Water Systems' Advice Letter Nos. 262-W and 263-W should be rejected as inconsistent with Commission direction and criteria for establishing memorandum accounts.

17. Tariff sheets 1207-W, 1208-W, 1209-W, 1210-W, and 1211-W attached to Advice Letters 262-W and 263-W should be rejected.

THEREFORE, IT IS ORDERED that:

1. Suburban Water Systems' Advice Letter Nos. 262-W and 262-W are rejected.

2. Suburban Water Systems' tariff sheets 1207-W and 1208-W attached to Advice Letter No. 262-W and tariff sheets 1209-W, 1210-W, and 1211-W attached to Advice Letter No. 263-W are rejected.

3. This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on July 9, 2009; the following Commissioners voting favorably thereon:

_____
PAUL CLANON
Executive Director

CERTIFICATE OF SERVICE

I certify that I have by mail this day served a true copy of draft Resolution W-4768 on all parties in these filings or their attorneys as shown on the attached list.

Dated June 9, 2009, at San Francisco, California.

/s/ Josie L. Jones
JOSIE L. JONES

Parties should notify the Division of Water and Audits, Public Utilities Commission, 505 Van Ness Avenue, Room 3106, San Francisco, CA 94102, of any change of address to insure that they continue to receive documents. You must indicate the Resolution number of the service list on which your name appears.

384653

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