

WATER/RSK/SNR/MRB/jlj

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

DIVISION OF WATER & AUDITS  
Water & Sewer Advisory Branch

RESOLUTION W-4672  
February 14, 2008

R E S O L U T I O N

**(RES. W-4672), GOLDEN STATE WATER COMPANY, INC. (GSWC).  
COMMISSION REVIEW OF DIVISION OF WATER AND AUDITS (Division)  
DISPOSITION OF ADVICE LETTER 1241-W. ORDER APPROVING NEW WATER  
SERVICE CONTRACT WITH CALIPATRIA STATE PRISON AND AUTHORIZING  
RECOVERY OF REVENUE SHORTFALL FROM THE EFFECTIVE DATE OF THIS  
RESOLUTION.**

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**SUMMARY**

This Resolution reviews the recent rejection of Advice Letter 1241-W by the Division, approves the New Agreement between GSWC and Calipatria State Prison (Prison) and authorizes recovery of revenue shortfalls occurring after the effective date of this Resolution.

**BACKGROUND**

GSWC has been providing the Prison with water under a contract. The existing contract, which went into effect on September 21, 1990, provides the Prison with water at a 60% discount below the rates for other customers in the Calipatria-Niland service area. The Prison uses 40% of the water in the service area.

GSWC filed Advice Letter (AL) No. 1206-W on January 5, 2006, to withdraw water service under contract to the Prison and provide service to the Prison under current tariff rates. The Office of the Secretary, California Department of Corrections and Rehabilitation (CDCR), filed a protest to the advice letter on January 26, 2006. Decision (D.) 06-01-025 of January 12, 2006, in Application 05-02-004, a General Rate Case for GSWC Water Region III, directed GSWC to use the Advice Letter process to change its rates for the Prison.

D.06-01-025 adopts fixed capital overhead allocation amounts rather than a percentage approach and it adopts a 10-basis point adjustment to GSWC's return on equity due to instances of management shortcomings. The Decision also requires SCWC to assume for test year and escalation year analysis that the Prison takes service at the otherwise applicable Region III tariff rate, even though the Prison will continue to pay the previously-negotiated contract rate, unless and until the Commission approves a different rate for the Prison; and the GSWC shareholders are responsible for the revenue shortfall recoveries. On February 16, 2006, GSWC applied for rehearing of D.06-01-025. On November 9, 2006, in D.06-11-020, the Commission granted a

limited rehearing of D.06-01-025. The Decision denied rehearing of D.06-01-025 as it related to rate treatment of the Prison.

Res. W-4601 of June 15, 2006, suspended GSWC's AL No. 1206-W for 60 days and required that GSWC attempt to resolve its rate dispute by negotiation. If the dispute were resolved by negotiation, GSWC was to substitute the new agreement for the existing one or establish a tariff for Service to Prison at the renegotiated rates; and GSWC could modify existing rates to make up for any shortfall in the revenue requirement prospectively.

In Res. W-4601, GSWC was directed that if resolution by negotiation did not occur within 60 days after the effective date of Res. W-4601, GSWC was to file an application to establish cost-based tariffed rates for service to the Prison. The filing was to address the direct costs of serving the prison and a fair allocation of the non-direct costs of service.

On June 21, 2006, GSWC in AL 1213 established the Calipatria Prison Memorandum Account (CPMA) to track the difference ("shortfalls") between revenues under Calipatria-Niland Region III tariff rates and the existing Prison rates.

On November 1, 2006, 139 days after the effective date of Res. W-4601, GSWC and the Prison executed a New Agreement. The New Agreement provides that either party may cancel the Agreement if the Commission 1) does not approve the entire Agreement without conditions or modifications which unacceptably affect either party, and 2) does not approve GSWC's rate-making treatment to fully recover any revenue shortfall pursuant to the prior Agreement and the revenues GSWC would have collected under GSWC's otherwise applicable tariff, each during the time period between June, 2006 and the Service Commencement Date, without conditions or modifications unacceptable to GSWC.

On December 15, 2006, GSWC filed AL 1206-WA, a supplement to AL 1206-W, seeking Commission approval of the New Agreement and ratemaking treatment for revenue shortfalls since January 19, 2006.

On January 19, 2007, the CPUC's Division of Ratepayer Advocates (DRA) protested AL 1206-WA.

On February 12, 2007, the Division rejected supplemental AL 1206-WA because it proposed to recover revenue shortfalls from January 19, 2006. This would be retroactive ratemaking. The rejection letter noted that GSWC could increase other tariff rates to compensate for the lower prison rates when the new rates for the prison take effect.

On March 20, 2007, GSWC filed AL 1241-W, seeking approval of the New Agreement and prospective rate-making treatment only for shortfalls. AL 1241-W also reserves the right to ask for future recovery of amounts in the CPMA.

On April 9, 2007, the DRA filed a protest of AL 1241-W. They note that Ordering Paragraph 5 of Res. W-4601-W says, "Pending resolution by negotiation, within no more than 60 days after

the effective date of this resolution, Golden State Water Company shall file an application to establish cost-based tariffed rates for service to the Calipatria State Prison.”

The DRA protest noted that the prior related AL 1206-WA was filed on December 15, 2006, four months past the Commission due date of August 15, 2006, without authorization for late-filing. AL 1241-W was filed nine months after August 15, also without authorization for late-filing. Further, AL 1241-W reserves the right to recover shortfalls occurring before Commission approval of the new Prison contract rates and the right to unilaterally cancel the New Agreement if the Commission denies such recovery.

DRA notes that GSWC proposes, based on Ordering Paragraph 4 of Res.W-4601, to implement a surcharge for the period April through December, 2007. However, Ordering Paragraph 4 only allows GSWC “to make up for any shortfall in the revenue requirement prospectively.” DRA also notes that the New Agreement allows GSWC to cancel the Agreement if the Commission does not allow GSWC to request recovery of shortfalls from June, 2006 onward. DRA views this as intentional disregard of W-4601’s prohibition of retroactive ratemaking.

DRA asks the Commission to impose penalties and fines under PU Code Sections 2107 and 2108 for GSWC’s continuing and repeated disregard of prior Commission decisions and resolutions, i.e., D.06-01-025, D.06-11-020, and Res. W-4601, and requests that the Commission order GSWC to file an application for new prison rates.

On April 20, 2007, GSWC replied to DRA, stating that: 1) a cost of service showing was not required, since they had signed a new contract with the Prison; 2) reserving the right to terminate does not contravene the Commission order to not engage in retroactive ratemaking; and 3) DRA’s assertion that GSWC should be required to file a formal application is legally and factually ungrounded.

On August 15, 2007, the Division rejected AL 1241-W, with prejudice and ordered GSWC to file an application.

On August 27, 2007, GSWC requested Commission review of the Division’s disposition of AL 1241-W.

## **DISCUSSION**

GSWC requests the Commission grant review of Division’s August 15 disposition of Advice Letter 1241-W, find that Division erred in rejecting the Advice Letter, and approve Advice Letter 1241-W. GSWC argues that Division’s August 15, 2007 rejection of AL 1241-W was in error because GSWC did negotiate and resolve issues related to new rates; that the rejection is inconsistent with direct orders from the Commission; that it exceeds the scope of Division’s authority; and that it contradicts Division’s prior disposition on the same issue.

GSWC quoted the Division’s letter rejecting AL 1241-W as saying ”the complex and material issues of fact and law pertaining to the new prison rates as mentioned in Commission D.06-01-025” GSWC correctly points out that D.06-01-025 did not mention ”issues of fact and law”.

However, Res. W-4601, Findings #4, says, “There are issues of fact and law that need to be resolved before the proper tariffed rates can be set for the Prison, unless these issues are resolved by negotiation”. The Resolution cites the need for a cost-of-service study covering all of GSWC’s direct and indirect costs to provide water service to Prison, providing that information to Prison, balancing the costs of providing service with the costs of Prison bypassing GSWC service, and negotiating with Prison based on that information.

On November 1, 2006, GSWC and Prison executed the New Agreement. This says the Existing Agreement will end and the New Agreement will begin upon Commission approval. The New Agreement was executed 139 days after the effective date of Res. W-4601, which required that after no more than 60 days, pending resolution by negotiation, GSWC must file an application to establish cost-based tariff rates for service to Prison.

GSWC says Ordering Paragraph 5 only applies if GSWC were filing an application to establish cost-based rates. We are not convinced. Ordering Paragraph 5 says GSWC *shall* file an application within 60 days, if a resolution by negotiation is not reached by then. GSWC did not comply. They notified Water Division staff by e-mail, 102 days after W-4601 was approved, that GSWC would not file a cost-based application.

GSWC argues that the statement in the February 13, 2007 letter rejecting AL 1206 WA the Division said, “While the new contract with Prison for the water service is acceptable, your proposed recovery of the revenue shortfall since January 19, 2006, is not.” constitutes complete acceptance of all parts of the contract.

GSWC also states that DRA’s April 9, 2007 letter protesting AL 1241-W “did not oppose the merits of the New Agreement or take issues with GSWC’s good-faith efforts to negotiate the New Agreement.”

In fact, DRA’s protest notes that the New Agreement was several months overdue; that an application for new Prison rates based on cost-of-service studies should have been filed 60 days after Res. W-4601; objects to the New Agreement’s section which would allow GSWC to unilaterally cancel the Agreement if the Commission does not allow collection of shortfalls back to June, 2006; and asks the Commission to impose fines and penalties for GSWC’s continued defiance of Commission orders.

GSWC argues that in rejecting the AL, Division exceeded its delegated “ministerial” authority.

On the issues we have determined as follows:

On the issue of the late-filed New Agreement and failure to file an application to establish cost-based tariff rates, the Commission will agree to accept the late filing of AL 1206-W and 1241-W and will not require an application to establish cost-based tariff rates. GSWC has resolved an issue of long standing with Prison. It is more important to have the issue resolved, although late, than to hold GSWC to the 60-day deadline.

The Commission believes Division's action was not in error since GSWC was not fully in accord with the requirements of D.06-01-025, D.06-11-020, and Res. W-4601. Division's action in rejecting Advice Letter 1241-W was technically correct. However, in weighing the gravity of the situation and considering the eventual resolving of the issue, we are inclined to pay more attention to the resolving of the issue than the technicality of the matter.

The Commission understands DRA's objection to the proposed contract clauses giving GSWC the right to cancel the contract, depending on future Commission actions concerning GSWC recovery of shortfalls. It would not be in the public interest for CPUC to let water company customers be hostage to such a contract, without safeguards. Therefore, the Commission intends to tie the benefits of Commission acceptance of AL 1241-W to GSWC continuation of this contract.

To that end, if the New Agreement is cancelled by GSWC, the terms of the existing contract which has been in effect since 1990 should be re-imposed; any increase in tariff rates to other Region III customers allowed by this Resolution should be rescinded; revenues from Prison should be shown as if they had been collected at the otherwise applicable Region III rates; and any shortfalls due to reimposition of the existing contract terms and the rescission of increases based on the New Agreement will again be at the expense of GSWC shareholders.

The Prison cannot be left without water service, and should not be obligated to pay the general tariff rate for water, if GSWC cancels the New Agreement. It would not be equitable to charge the Prison the general tariff rate because of the large amount of Calipatria plant in service they have paid for in the past. Further, the Prison is able to fund and construct its own water supply, and could presumably do so at less than the general tariff rate. If the Prison left the GSWC water system, the Calipatria District would use 40% less water and have a plant with significant excess capacity.

The Commission doesn't want the Prison to leave the GSWC water system, find its own source and make the rest of the district's customers bear the full operational cost of Calipatria's operating system. The potential revenue loss at shareholder expense if GSWC should cancel the New Agreement should provide an incentive for GSWC to maintain that agreement.

Under D.06-01-025, GSWC is entitled to recover revenue shortfalls from the effective date of this resolution. GSWC should recalculate the difference in revenues between the New Agreement and otherwise applicable Region III rates starting from the effective date of this Resolution.

GSWC asked that the Commission remove language from this Resolution prohibiting recovery of revenue shortfalls, saying recovery is not the issue in this proceeding. GSWC introduced this issue by the terms of their contract with Calipatria State Prison.

Decision 06-01-025 stated that until the Commission approves a different rate for the Prison, GSWC shareholders are responsible for the revenue shortfall recoveries. In D.06-11-020, the Commission denied rehearing of D.06-01-025 as it related to rate treatment of the Prison. The Commission will not revise those Decisions in this Resolution.

Amounts accumulated in the Calipatria Prison Memorandum Account before the effective date of this resolution represent revenue shortfalls for which GSWC shareholders are responsible, and will not be charged to ratepayers.

### **COMMENT**

Public Utilities Code Section 311(g) (1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Public Utilities Code Section 311 (g) (2) provides that this 30-day period may be waived or reduced upon stipulation of all parties in the proceeding.

The 30-day comment period for the draft resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments, and will be placed on the Commission's agenda no earlier than 30 days from the date of mailing of this resolution to the parties.

Comments were received from GSWC, DRA, and the City of Claremont. To the extent that changes were necessary, they have been incorporated therein.

### **FINDINGS OF FACT**

1. Decision 06-01-025, January 5, 2006, requires Golden State Water Company to assume for test year and escalation year analysis that Calipatria Prison takes service at the otherwise applicable Region III tariff rate, even though the prison will continue to pay the previously-negotiated contract rate, unless and until the Commission approves a different rate for the prison; and the Golden State Water Company shareholders are responsible for the revenue shortfall recoveries.
2. Resolution W-4601 suspended Advice Letter 1206-W for 60 days.
3. Resolution W-4601 directed Golden State Water Company to resolve its rates for the Calipatria State Prison by negotiation.
4. Resolution W-4601 required Golden State Water Company to negotiate a new contract with Calipatria State Prison or file an application to establish cost-based tariff rates for service to Calipatria State Prison.
5. Resolution W-4601 allows Golden State Water Company to modify existing rates to make up for any shortfall in the revenue requirement prospectively, if the rate controversy with Calipatria State Prison is resolved by negotiation.
6. Golden State Water Company executed a New Agreement with Calipatria State Prison which Golden State Water Company could cancel if the Commission does not allow Golden State Water Company to recover revenue shortfalls back to June, 2006.
7. Golden State Water Company was late in filing a New Agreement with the Commission.
8. Golden State Water Company was able to settle its issues with Calipatria State Prison, although they were late in settling and in filing the New Agreement with the Commission.

**THEREFORE IT IS ORDERED THAT:**

1. Golden State Water Company's Existing Agreement with Calipatria State Prison is suspended.
2. The provisions of Golden State Water Company's Advice Letter No. 1241-W are accepted. Golden State Water Company may file a compliance advice letter to make these provisions effective.
3. Golden State Water Company may modify existing rates to other customers to make up for any shortfall in the revenue requirement prospectively. Amounts accumulated in the Calipatria Prison Memorandum Account before the effective date of this resolution represent shortfalls for which Golden State Water Company shareholders are responsible, and will not be charged to ratepayers.
4. If Golden State Water Company cancels the New Agreement as allowed in that Agreement, rates in the existing contract in effect since 1990 shall be reinstated.
5. If Golden State Water Company cancels the New Agreement, any increase in tariff rates to other Region III customers to make up for tariff shortfall shall be rescinded.
6. If Golden State Water Company cancels the New Agreement, Golden State Water Company shareholders shall be responsible for revenue shortfalls due to reimposition of previous rates.
7. 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 February 14, 2008; the following commissioners voting favorably thereon:

/s/ PAUL CLANON

Paul Clanon  
Executive Director

MICHAEL R. PEEVEY  
President

DIAN M. GRUENEICH

JOHN A. BOHN

RACHELLE B. CHONG

TIMOTHY ALAN SIMON

Commissioners