

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA



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Application of California-American Water Company (U210W) for Authorization to Increase its Revenues for Water Service by \$55,771,300 or 18.71% in the year 2024, by \$19,565,300 or 5.50% in the year 2025, and by \$19,892,400 or 5.30% in the year 2026.

Application 22-07-001

**THE PUBLIC ADVOCATES OFFICE
REPLY BRIEF**

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I. INTRODUCTION

Pursuant to Rule 13.12 of the California Public Utilities Commission (Commission) Rules of Practice and Procedure (Rules) and the schedule established in the October 31, 2023 *Administrative Law Judge's Ruling Updating the Proceeding Schedule and Providing Direction Regarding Briefing*, the Public Advocates Office at the California Public Utilities Commission (Cal Advocates) submits this reply to the *Opening Brief of California American Water Company on non-WRAM Issues* (Cal Am Opening Brief on Non-WRAM issues).

II. DISCUSSION

A. The Commission Should Deny Cal Am's Special Request No. 4: Partial Consolidation of Transmission and Distribution Net Plant Costs.

In Rulemaking 12-06-013, the Commission recognized the principle of cost causation as “one of the underlying goals of the Commission’s rate making process.”¹ Under this principle, “costs should be borne by those customers who cause the utility to incur the expense.”² Special Request No. 4 would erode this principle by consolidating 50% of all California American Water’s (Cal Am) net plant Transmission and Distribution (T&D) assets into a central pool by 2025. Although consolidation sometimes helps facilitate a more equitable rate,³ applying cost-causation principles “achieves equity in rates by relating the costs imposed on the utility system to the customer responsible for those costs.”⁴ Consequently, the Commission should deviate from the principle of cost causation only when necessary to achieve rate equity.

In its opening brief, Cal Am admits that Special Request No. 4 would have little impact if granted because bill reduction experienced by customers now “will be negated

¹ Rulemaking (R.) 12-06-013, *Order Instituting Rulemaking on the Commission's Own Motion to Conduct a Comprehensive Examination of Investor-Owned Electric Utilities' Residential Rate Structures, the Transition to Time Varying and Dynamic Rates, and Other Statutory Obligations*, June 28, 2012, at 13.

² R.12-06-013, at 13.

³ For example, when the benefits of consolidation can be equally distributed such as in risk pooling.

⁴ R.12-06-013, quoting 26 CPUC 2d 392, D.87-12-066 (1987).

in the future when the T&D net cost pool increases.”⁵ Instead, Cal Am attempts to frame this shortcoming as a strength, arguing that Special Request No. 4 would “even out the costs associated with the replacement of T&D assets so that no individual customer feels the shock of a sudden increase in rates.”⁶ However, there is no evidence in the record that suggests rate shock is likely due to T&D asset replacement. On the contrary, the proposed consolidation is expected to have a bill impact of less than one percent for a majority of customer classes.⁷ Moreover, even if the customer bill impacts of consolidation were greater, Cal Am’s proposal would still be shortsighted. Consolidation may result in a short-term reduction to some customers’ bills, with all districts subsidizing each other. However, the costs and cross-subsidies would eventually stabilize, resulting in customers collectively paying the same costs. Thus, Special Request No. 4 would not achieve any meaningful benefits for customers.

Rather than benefiting customers, Special Request No. 4 would enable Cal Am to avoid alerting customers and the Commission to the full impact of expensive T&D projects. By distributing T&D project costs over a larger customer base, Cal Am would be able to recover these costs without drawing as much attention to bill increases. Indeed, the shock of a sudden rate increase that Cal Am wants to avoid serves a useful purpose: it calls for increased Commission scrutiny on costly expenditures. By eliminating or reducing these signals, consolidation can render customers more prone to paying excessive costs. Cal Am appears to anticipate excessive costs, stating that consolidation would help cover “the replacement of mains and services that only after installation are discovered to have long-term breakage and leakage issues.”⁸ Customers already pay the utility for its expertise in engineering and design to maximize the life of

⁵ *Opening Brief of California American Water Company on Disputed Non-Decoupling Issues* (Cal Am Opening Brief on Disputed Non-Decoupling Issues), at 6.

⁶ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 6.

⁷ *Public Advocates Office Prepared Testimony of Sari Ibrahim, Report on Contingency, Plant Retirement, Construction Work in Progress, Southern District and Corporate Plant Additions, and Special Request Number 4*, April 13, 2023, Exh. CALAD-SI-001, Attachment 3.

⁸ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 5.

infrastructure and services. Thus, the Commission should reject Special Request No. 4 to ensure Cal Am's accountability to customers and the Commission in prudent planning and development of T&D projects.

B. The Commission Should Deny Special Request No. 5: Acquisition Rate Base Normalization – Request to Deviate from Uniform System of Accounts.

Instead of following Standard Practice (SP) U-38-W for the Bellflower, East Pasadena, and Warring acquisitions, Cal Am proposes in Special Request No. 5 to book the acquisitions as gross plant with accumulated depreciation.² Under this methodology, acquired assets are “grossed up” so that post-acquisition plant, less depreciation reserve, would equal the authorized post-acquisition rate base.¹⁰ To ensure consistency in the accounting methodology for water system acquisitions of Cal Am and other water utilities, the Commission should require Cal Am to adhere to SP U-38-W.

In support of its request, Cal Am argues that its proposed accounting methodology would conform to Generally Accepted Accounting Principles (GAAP).¹¹ Cal Am correctly identifies GAAP as widely used by corporate and government entities, including the United States.¹² However, the validity of GAAP is not at issue. The significance in requiring Cal Am to adhere to SP U-38-W is in ensuring consistency of accounting methodology for water system acquisitions under the Commission's jurisdiction. As the Commission stated in D.16-11-006, the “purpose of the [uniform systems of accounting] is to have the water utilities provide financial transparency of their water operations on a consistent basis.”¹³ Essentially, Cal Am asserts that its individual interest in aligning with GAAP is greater than the Commission's interest in maintaining a consistent accounting methodology for regulated water utilities.¹⁴ Because

² *Direct Testimony of Stephen (Wes) Owens*, July 1, 2022, Exh. CALAM-SWO-001 at 52:14-16.

¹⁰ Exh. CALAM-SWO-001 at 52:20-22.

¹¹ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 8.

¹² Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 8.

¹³ D.16-11-006, at 38.

¹⁴ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 9-10.

other utilities follow SP U-38-W, Cal Am’s deviation from the standard practice would undermine the Commission’s ability to compare acquisitions and assess value. Requiring Cal Am to follow the standard practice ensures consistent accounting methodology across water utilities and enables the Commission to assess the value of acquired water systems. Cal Am claims that using different accounting methods would not result in any impact on customers, arguing that rate base is the same under either method, making the revenue impact the same. However, Cal Am also states that:

assuming the amortization period for UPAA [(utility plant acquisition adjustment)] is consistent with the remaining useful life of the associated assets, cost of service is not impacted, as there is no difference between depreciation expense and UPAA amortization.¹⁵

Cal Am’s assumption of consistency between the UPAA amortization period and remaining useful life of assets indicates that its requested deviation cannot ensure that there will be no revenue impacts. The Commission should avoid this risk entirely by denying Special Request No. 5 without prejudice. If Cal Am seeks to deviate from the rules and standard practices that are applicable to all Class A water utilities, it should proceed to do so in the correct forum: an industry-wide rulemaking or petition to change standard practice.¹⁶

C. The Commission Should Deny Special Request No. 6: Catastrophic Event Cost Normalization – Earthquake Insurance.

In Special Request No. 6, Cal Am asks to track earthquake insurance premiums in a catastrophic event memorandum account (CEMA). CEMA was authorized for “unforeseeable” expenses associated with disasters.¹⁷ As Cal Am admits, “the CEMA typically tracks costs incurred after a catastrophic event occurs...”¹⁸ This is exactly why tracking Cal Am’s proposed expenses in the CEMA is inappropriate: earthquake

¹⁵ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 8-9.

¹⁶ Standard Practice U-1-W, at 4.

¹⁷ Resolution E-3238, at 1.

¹⁸ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 11.

insurance premiums are foreseeable expenses that utilities incur before a disaster occurs.¹⁹ Utilities prepay earthquake insurance premiums to receive insurance for future earthquakes.²⁰ Utilities can reasonably forecast a budget for earthquake insurance premium expenses if they receive quotations from insurance companies.²¹ Therefore, Cal Am’s request is inconsistent with the purpose of the CEMA. Cal Advocates does not categorically oppose recovery of earthquake insurance premium expenses. Instead, Cal Advocates opposes Cal Am’s proposal in this GRC for two reasons: (1) Cal Am’s proposed earthquake insurance policy is unreasonable, as the costs would likely outweigh the benefits to ratepayers and (2) Cal Am’s request to track earthquake insurance premium expenses in the CEMA is inconsistent with the purpose of the CEMA.²²

Also, Cal Am and other utilities have means for recovering reasonable earthquake insurance premium expenses in the future. In the next GRC, Cal Am may propose a budget for earthquake insurance premium expenses as a component of the revenue requirement.²³ The Commission would then review this budget to determine whether it is just and reasonable. Furthermore, if Cal Am wishes to purchase an earthquake insurance policy before the next GRC, it can do so using shareholder funds.

D. The Commission Should Deny Special Request No. 9: Placer County Water Agency (PCWA) Capacity Cost Recovery.

In Special Request No. 9, Cal Am requests a deviation from Standard Practice U-27-W to enhance shareholder profits by increasing the interest rate

¹⁹ *Public Advocates Office Prepared Testimony of Isaac Gendler, Report on Depreciation, Earthquake Insurance, Customer Service, Wildfire, and Safety*, Updated on May 8, 2023, Exh. CALAD-CS-002, at 10:19-20.

²⁰ Exh. CALAD-CS-002, at 10:20 – 11:1.

²¹ Exh. CALAD-CS-002, at 11:1-3.

²² *Cal Advocates Opening Brief on Non-WRAM Issues*, at 7-9.

²³ In this GRC, the parties have settled all issues related to the revenue requirement. (*Joint Motion for Adoption of a Settlement Agreement Between California-American Water Company and Public Advocates Office in the General Rate Case*, July 1, 2022, at 4 (“Motion for Adoption of Settlement”).) The agreed-upon revenue requirement does not include any earthquake insurance premium expenses. (Motion for Adoption of Settlement.)

from the appropriate 90-day commercial paper rate to Cal Am’s authorized full rate of return for the PCWA Special Facilities Fee Memorandum Account. In its opening brief, Cal Am exaggerates the risk of recovery of costs tracked in the PCWA memo account. Cal Am incorrectly refers to costs paid to the memo account as “investments” and “capital expenditures.”²⁴ This memo account does not track investments or capital expenditures. Instead, it tracks “fees...associated with purchasing additional units of water...and water demand in excess of certain thresholds.”²⁵ Whereas *investments* and *capital expenditures* imply greater risk, Cal Am can reliably recover fees. To make recovery simple and reliable, Resolution W-5111 provides that Cal Am may file a Tier 2 advice letter to recover a shortfall when “under collection in the Special Facilities Fee Memorandum Account exceeds 2% of the gross operating revenue authorized.”²⁶ Additionally, Resolution W-5111 allows Cal Am to propose an equitable allocation for the cost amortization among customers who have exceeded their monthly demand targets.²⁷ Thus, the Commission should deny Special Request No. 9 because Cal Am can reliably recover the costs for these fees, as provided for in Resolution W-5111.

**E. The Commission Should Deny Special Request No. 13:
Chemical Cost Balancing Account.**

Cal Am states that a chemical cost balancing account is necessary because of the “extreme volatility in the chemicals market” and that this volatility “makes the cost of chemicals...extremely difficult to predict.”²⁸ However, all commodities are subject to price variations. Cal Am has not shown that chemicals prices are any more volatile than

²⁴ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 13, 15. Cal Am also provides examples of the Commission allowing a higher rate of return. (See *Id.*, fn. 70.) However, the examples provided are construction and capital projects, not fee recovery memo accounts like the one at issue for Special Request No. 9.

²⁵ Resolution W-5111, at 1.

²⁶ Resolution W-5111, at 9.

²⁷ Resolution W-5111, at 9.

²⁸ Cal Am Opening Brief on Disputed Non-Decoupling Issues, at 15-16.

the prices of other commodities that are included in the revenue requirement. No other Class A water utility has received authorization for a balancing account to track chemicals costs.²⁹

Further, the Commission should authorize memo and balancing accounts sparingly. The “ratemaking process should be transparent to decisionmakers and ratepayers and should encourage utilities to operate efficiently and within budget.”³⁰ Memo and balancing accounts “are alternative ratemaking mechanisms that are counter to both of these principles.”³¹ Although worthwhile in some instances, memo and balancing accounts undermine transparency and oversight efficiency. The Commission should strive to reduce the number of memo and balancing accounts, not authorize additional unnecessary memo accounts, and certainly not approve individual accounts in an individual utility’s general rate cases when the underlying expense affects all Class A Water utilities.³² Thus, the Commission should deny Special Request No. 13 to promote transparency and efficiency in the ratemaking process and because Cal Am has failed to prove that chemical costs are exceedingly volatile and unique to Cal Am’s position amongst all other Class A water utilities.

III. CONCLUSION

For the reasons stated above, Cal Advocates respectfully requests that the Commission:

²⁹ California Public Utilities Commission, “Report of Summary of Balancing Accounts for Class A and B Water Investor-Owned Utilities for the Six-Month Period Ending June 30, 2023,” Table 7, <https://www.cpuc.ca.gov/-/media/cpuc-website/divisions/water-division/reports/balancing-accounts/semiannualreportbalacct20230630v2.pdf>. Cal Advocates requests that the Commission take official notice of the information on this webpage as an official act of the executive branch of the State of California and as facts and propositions that are “not reasonably subject to dispute and are capable of immediate and accurate determination by resort to sources of reasonably indisputable accuracy,” pursuant to the Commission’s Rule 13.10 and Evidence Code section 452, subdivisions (c) and (h).

³⁰ Exh. CALAD-CS-001, at 5:10-11.

³¹ Exh. CALAD-CS-001, at 5:12-13.

³² Exh. CALAD-CS-001, at 5:17-18.

- Deny Cal Am’s request to consolidate water T&D net plant assets for all rate-making districts (Special Request No. 4);
- Deny Cal Am’s request to deviate from Standard Practice U-38-W (Special Request No. 5);
- Deny Cal Am's request to recover \$3.3 million per year in earthquake insurance premiums and to track its proposed earthquake insurance premium budget in the CEMA account (Special Request No. 6);
- Deny Cal Am’s request to deviate from Standard Practice U-27-W by increasing the interest rate from the appropriate 90-day commercial paper rate to Cal Am’s authorized full rate of return for the PCWA Special Facilities Fee Memorandum Account (Special Request No. 9); and
- Deny Cal Am’s request for a new balancing account to track chemical costs (Special Request No. 13).

Respectfully submitted,

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