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MAIL DATE
9/8/97

Decision 97-09-059 September 3, 1997

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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| In the Matter of Hillcrest Water Company for a 23.3% general rate increase in TY 1993 for service provided to 3000 flat-rate customers in and around Yuba City, and an additional increase of 1.7% for 1994 and 1995. | A.92-11-016 (Filed November 13, 1992) |
| Order Instituting Investigation Into the Rates, Charges, and Practices of Hillcrest Water Company | I.93-03-056 (Filed March 24, 1993) |

ORIGINAL

## ORDER DENYING REHEARING OF D.97-06-105

On July 16, 1997, Hillcrest Water Company (Hillcrest) filed an application for rehearing of our Decision (D.) 97-06-105 in the above-captioned consolidated proceeding. Upon review of the application, and all matters raised therein, we hereby deny rehearing. Hillcrest has not established legal error in our decision as is required by Cal. Pub. Util. Code Section 1732. On August 21, 1997, Hillcrest also filed a motion for a stay of D.97-06-105 pending the Commission's decision on the application for rehearing. With this order denying rehearing, the motion is moot.

In 1983, the Commission ordered Hillcrest to apply a ratepayer surcharge to the repayment of a loan obtained by the company under the Safe Drinking Water Bond Act (SDWBA), and maintain all surcharges collected in a separate, interest bearing account.[1]

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1 See D.83-07-004, 12 Cal.P.U.C.2d 1, 6-7. Among the findings and orders of this decision, Finding of Fact 7 stated: "The surcharges are to be used only to amortize the SDWBA loan. The surcharges should be separately identified on customers' bills and the monies collected should be deposited in an interest bearing account with the fiscal agent approved by DWR. Such deposits shall be made within five working days after collection. The interest earned on the deposits shall be used

In a subsequent investigation (I.93-03-056), which was consolidated with Hillcrest's 1992 rate case, A.92-11-016, the staff of the Commission found that although the company had made payments on the loan, it had actually collected sufficient funds from the ordered surcharges to have repaid the loan, but had not done so. Further, the staff auditors found that Hillcrest had not allocated all surcharge monies to the separate, interest bearing account. (See the Commission Staff Report, May 11, 1994, pp. 6-14.) In light of this information, in D. 95-01-038, the Commission approved a settlement agreement between Hillcrest and the Division of Ratepayer Advocates which required that Hillcrest complete repayment of the loan by January 1, 1996, and cease collecting the ratepayer surcharges.[2] However, after a hearing held in January 1997 in the consolidated investigation/rate case, the Commission determined that in violation of D.95-01-038, Hillcrest had not yet completed the loan repayment. In D.97-06-015, therefore, we ordered that Hillcrest's ratepayer charges be reduced for whatever period of time elapses from January 1, 1996, to the date Hillcrest completes repayment of the loan. We ordered the reduction of charges to ratepayers be achieved by reducing Hillcrest's rate of return to 5.375%, a 50% reduction.

In the application for rehearing, Hillcrest claims that it was not given notice and the opportunity to be heard on the issue of reducing its rate of return as a consequence of its violations of Commission orders, that the reduction is an inappropriate penalty, and that ratepayers will be adversely affected. We are not persuaded by Hillcrest's arguments, and do not find that they substantiate any legal error in D.97-06-105.

First, Hillcrest was provided adequate notice that the rates it charges its customers were at issue in this matter when the investigation was opened on March 24, 1993 for the purpose of examining the use of the revenue Hillcrest collected from the rate

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exclusively for the purpose of repayment of the SDWBA loan. Order No. 5 stated: "To assure repayment of the [SDWBA] loan, Hillcrest shall deposit all rate surcharge revenue collected, in an interest-bearing account. . . ."

2 See D.97-06-105, pp.2, 6-7.

surcharges, revenue which should have been applied to the repayment of the SDWBA loan. We ordered that the investigation (I.93-03-056) be consolidated with the 1992 general rate case, A.92-11-016. Further, in D.93-12-013, the Commission stated that it was thereby disposing of all issues in A.92-11-016 "with the exception of the establishment of the level of residential metered rates." (See Interim Opinion D.95-01-038, p. 1.)

The history of this matter demonstrates, therefore, that Hillcrest's obligation to repay the loan began with a 1983 rate order. Further, Hillcrest was reminded in the order instituting the investigation, I.93-03-056, and in D.95-01-038 that issues involving the ratepayer surcharge and Hillcrest's failure to repay the loan were being considered in a ratemaking forum. It is quite appropriate, therefore, that we issue a rate order as a consequence of Hillcrest's unlawful actions in failing to comply with Commission rate orders.

We see no basis, moreover, for Hillcrest to claim that because neither the staff nor the assigned Administrative Law Judge (ALJ) specifically invited Hillcrest to testify or offer evidence on the effect of its violations on ratepayers, Hillcrest was prevented from doing so. Hillcrest fails to cite any direction, order, or comment of the ALJ or Commission decision which prohibited Hillcrest from addressing the subject of the appropriate impact on customer rates of Hillcrest's ongoing violations of Commission orders. With a prehearing conference held September 5, 1996, a subsequent prehearing conference on October 17, 1996, an evidentiary hearing held January 22, 1997, the submission of briefs on February 28, 1997, and a settlement conference held March 11, 1997, Hillcrest had every chance over several months to address the consequences of its mishandling of ratepayer charges and the possibility that the Commission would make a justified adjustment of those charges. Hillcrest cannot reasonably or credibly claim that it was unaware its rates were not involved in this proceeding.

In short, Hillcrest had clear notice and ample opportunity to be heard on the subject of the appropriate rates to charge its customers in light of Hillcrest's violations of Commission orders and decisions.

Second, we find no rationale offered by Hillcrest to support its contention that reducing its rate of return, which is the effective means for reducing ratepayers charges, is inappropriate because such an order can only be made in a rate case. Hillcrest's argument is not only unsupported by any legal authority, it also is of no avail since, as we have discussed above, Hillcrest is here involved in a consolidated rate case and investigation.

Hillcrest also quarrels with our order because we described the reduction of Hillcrest's rate of return as a "penalty." Hillcrest attempts to distinguish our imposition of this penalty from the actions we took in the cases we cited as precedents: General Telephone Company of California (1980) 4 Cal.P.U.C.2d 428, 511 and Gibbs Ranch Water Company (1994) 56 Cal.P.U.C.2d 468, 480.

Hillcrest notes that the rate of return reduction in General Telephone was called an "incentive" to "improve service," not a "penalty". This semantic argument does not advance Hillcrest's position, however. It is no more convincing than an argument against calling a jail term a "punishment" rather than a "deterrent" against further unlawful behavior. We have, moreover, limited the rate of return reduction to endure only so long as Hillcrest remains in violation of the Commission's orders, from a starting date of January 1, 1996. Clearly, our order is designed to be an "incentive" to Hillcrest to repay the loan sooner rather than later. Labeling the rate of return reduction an "incentive" rather than a "penalty" would have no effect on the meaning or the impact of the order. Furthermore, Hillcrest cites no legal authority precluding our description of the order as a "penalty."

Hillcrest makes a similarly flawed semantic argument regarding Gibbs Ranch in which the Commission did not apply the term "penalty," but did reduce the company's rate of return because of "lack of management effectiveness." Since Hillcrest

insists, we will clarify that violations of regulatory orders epitomize management ineffectiveness because managers of a public utility are obliged to act lawfully. Thus, the reduction of Hillcrest's rate of return is also imposed because of lack of management effectiveness. We will also clarify that the reduction of Hillcrest's customer charge by a lowering of the rate of return was ordered because of the persistent and willful violation of Commission orders which have the force and effect of law. [3]

Hillcrest's arguments, therefore, regarding the use of the term "penalty" to describe the reduction in the rate of return are without any legal or rational support, and fail to demonstrate legal error in D.97-05-105.

Third, Hillcrest argues in the application for rehearing that reducing its rate of return will adversely affect ratepayers. We want to make it very clear that there is to be no adverse effect on ratepayers, and there is to be an immediate reduction in ratepayer charges resulting from the ordered reduction in Hillcrest's rate of return. Our rate orders are issued on the basis that they are just and reasonable, and provide sufficiently for the operations of the utility. We reject any claim, or implied warning, that the reduction of Hillcrest's rate of return to 5.375% will mean a reduced commitment to making any necessary re-investment in the utility. Hillcrest remains obligated by law to provide its customers with a vital public utility service that is safe and reliable. Hillcrest errs seriously in contemplating it has an excuse for doing anything less.

Consistent with our discussion herein, therefore, we deny rehearing of D.97-06-105. Hillcrest has not met its burden of demonstrating legal error. However, we will add to the findings of fact and conclusions of law to more completely reflect the record and to clarify our decision. We will add as a finding of fact that if circumstances warrant, Hillcrest and Daryl Morrison, president and sole shareholder of Hillcrest, can be subject to the additional penalties prescribed in Sections 2107, 2108 and 2110 of the

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[3] We further note that a rate of return reduction may be ordered pursuant to the Commission's ratemaking authority in addition to civil penalties and/or criminal misdemeanor penalties that may be imposed on both Hillcrest and Daryl Morrison, the company's president and sole shareholder. (See Sections 2105, 2107, 2108, and 2110 of the California Public Utilities Code, and Sections 17200 et seq. of the California Business and Professions Code.)

California Public Utilities Code, and subject to the penalties prescribed in Sections 17200 et seq. of the California Business and Professions Code in an action brought by the California Department of Justice or the county's District Attorney.[4] We will also modify Conclusion of Law No. 4 to read: "We conclude at this time that as a result of Hillcrest's and Morrison's violations of Commission orders and decisions, it is fair and just to reduce ratepayer charges through a reduction of Hillcrest's rate of return for a period of time equal to the time it is in violation of D.95-01-038, as described herein." Finally we will delete Ordering Paragraph 6, which closed the matter and substitute: "This docket shall remain open for further consideration of Hillcrest's compliance with the Commission's orders discussed herein and the present decision, and for further consideration of appropriate enforcement actions."

With respect to Hillcrest's motion for a stay of D.97-06-105, it is redundant under statutory procedure and mooted by the instant denial of the application for rehearing. Hillcrest's motion relies on Section 1733(a) of the California Public Utilities Code which provides:

> "Any application for a rehearing made 10 days or more before the effective date of the order as to which a rehearing is sought, shall be either granted or denied before the effective date, or the order shall stand suspended until the application is granted or denied; but, absent further order of the commission the order shall not stand so suspended for more than 60 days after the date of filing of the application, at which time the suspension shall lapse, the order shall become effective, and the application may be taken by the party making it to be denied." (See Hillcrest's Motion for Stay, p. 2. Emphasis added.)

Hillcrest's application for rehearing was filed 10 days before July 26, 1997, the effective date of D.97-06-105. Because a decision on the application was not reached before the effective date, Section 1733(a) was triggered and the decision was temporarily

[4] Appended to Hillcrest's application for rehearing is a declaration of Daryl Morrison dated July 14, 1997, which attests that

suspended. Hillcrest's motion is, therefore, redundant. Further, with our present decision denying rehearing, the orders in D.97-06-105 become immediately effective, and no grounds for a further stay are warranted or required.

**IT IS THEREFORE ORDERED** that:

1. The application for rehearing of D.97-06-105 is denied.

2. D. 97-06-105 shall be modified to include as Finding of Fact No. 17a: "If circumstances warrant, Hillcrest and Daryl Morrison, president and sole shareholder of Hillcrest, can be subject to the additional penalties prescribed in Sections 2107, 2108 and 2110 of the California Public Utilities Code, and subject to the penalties prescribed in Sections 17200 et seq. of the California Business and Professions Code in an action brought by the California Department of Justice or the county's District Attorney."

3. Conclusion of Law No.4 of D. 97-06-105 shall be modified to read: "We conclude at this time that as a result of Hillcrest's and Morrison's violations of Commission orders and decisions, it is fair and just to reduce ratepayer charges through a reduction of Hillcrest's rate of return for a period of time equal to the time it is in violation of D.95-01-038, as described herein."

4. Ordering Paragraph No. 6 of D.97-06-105 shall be deleted and replaced with: "This docket shall remain open for further consideration of Hillcrest's compliance with the Commission's orders discussed herein and the present decision, and for further consideration of appropriate enforcement actions."

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he is the president and sole shareholder of Hillcrest.

5. Hillcrest's motion for a stay of D.97-06-105 is denied as procedurally redundant and unwarranted.

This order is effective today.

Dated September 3, 1997, at San Francisco, California.

P. GREGORY CONLON
President
HENRY M. DUQUE
JOSIAH L. NEEPER
RICHARD A. BILAS
Commissioners

I dissent.
/s/ JESSIE J. KNIGHT, JR.
Commissioner