

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the)
Commission's Own Motion to set rules)
and to provide guidelines for the)
Privatization and Excess Capacity)
as it Relates to Investor Owned)
Water Companies.)
_____)

ORIGINAL

FILED

PUBLIC UTILITIES COMMISSION
OCTOBER 22, 1997
SAN FRANCISCO OFFICE
R.97-10-049

ORDER INSTITUTING RULEMAKING

Introduction

In October of 1996 at our first Water Roundtable and again in mid-November at the Fall California Water Association Meeting, we expressed a keen interest in facilitating a greater understanding of the problems and the changes taking place in the water industry. Those problems and changes were (1) mergers and acquisitions, (2) privatization of, and use of excess capacity, which we are addressing in this OIR; and (3) alternative ratemaking procedures, such as cost of living increases, ratebase offsets and performance based regulation. We included these issues as an integral part of the Commission's first Business Plan. As a result, over the period from May, 1997 through August, 1997 our Water Division hosted three workshops to address these issues. Workshop reports have been written, distributed, and commented upon by the industry and interested parties on all but alternative ratemaking procedures, which is due to be distributed shortly. The workshop on Privatization and Excess Capacity was held on June 10 and 11, 1997, facilitated by the Water Division.

Workshop Results

The workshops were attended by almost all of our Class A water utilities, representatives of some of our smaller water companies, the California Water Association (CWA), representatives of the Commission's Office of Ratepayer Advocates, and the host Water Division. At times during the two days of the workshop, Commissioners Duque and Neepser and

their advisors attended. A workshop report on Privatization was mailed to all participants on August 7, 1997.

The workshop's participants agreed that the definition of privatization covered many related activities, and agreed that privatization was uniformly viable due to underutilized and excess capacity. The participants believed that privatization could result in "the maximum utilization of utility resources". The workshop report included the following examples:

1. the purchase of a non-investor owned public water system,
2. operation and maintenance of a public water system,
3. provision of billing services,
4. sales of reclaimed water,
5. use of power and energy purchase aggregation,
6. revenue from antennae or pole attachment agreement,
7. design and/or construction of municipal water systems, and
8. joint ownership/operation of municipal systems.

Allocation of Cost

We are now ready to ask the parties to comment on the following questions developed from the report, our roundtable of last October, and various discussions over the past year with the industry, the staff, and the Legislature. In addition, we invite parties to propose policies and findings consistent with their answers to our questions. We plan to have final rules or guidelines as soon as possible after the first of the year.

From our review of the report, no consensus appears to have been reached among the participants as to whether these endeavors are adequately covered by the Commission's uniform system of accounts, or whether these additional costs and revenues should be treated as "above-the-line" with all income/losses accruing to the ratepayer or "below-the-line" with the income/losses accruing to the shareholders. We also note from the report that the water companies who have already engaged in "privatization" have used multiple allocation methods. The participants, including the Commission's staff, did not reach agreement on whether incremental costs, or embedded costs, or a combination of the two was the appropriate method for allocation.

We believe that this OIR is the correct forum to provide rules and appropriate guidelines for regulated water utilities and staff governing the proper accounting and ratemaking for privatization and the use of underutilized and excess capacity. We have a series of questions of all the parties. Once we receive comments, we will prepare a proposed decision which will be served on all regulated water companies and on all interested parties, including the workshop's participants.

We would like the parties to address the following questions and propose policies and findings:

1. Do ratepayers benefit from the sale of excess capacity to others?
2. In what manner should a utility report any activity related or unrelated to providing water service? Should it be considered a regulated or non-regulated service?
3. Does the sale of excess capacity by a water company pose risk to ratepayers; and if so, how can ratepayers be protected?
4. Should the costs of such activities be based on fully allocated or incremental costs?
5. Should expenses associated with other than providing regulated water service follow the revenues, even when a loss occurs?
6. Should ratepayers of a regulated utility be required to make up for the losses of the non-regulated operations? Should they share in any profits?
7. Should any revenues and/or profit resulting from underutilized and excess capacity accrue to ratepayers or be shared between ratepayers and shareholders? If shared, in what proportion should we allocate?
8. Should the Commission encourage the water industry's participation in privatization and the use of underutilized and excess resources?
9. How can we differentiate between underutilized and excess capacity?
10. Can a water company have too much excess capacity, and how should that excess be treated for ratemaking purposes?

IT IS ORDERED that:

1. A rulemaking on the Commission's own motion is instituted to solicit comments and recommendations on our proposal for rules and guidelines for privatization and excess capacity as it relates to investor owned water companies.
2. All Class A water utilities subject to the Commission's jurisdiction, the California Water Association, the Water Division, and the Office of Ratepayer Advocates are made respondents to this proceeding. Other regulated water companies and interested parties are invited to respond to the questions set forth above.
3. An original and 7 copies of all comments shall be filed with the Commission's Docket Office at 505 Van Ness Avenue, San Francisco, California, 94102 within 30 days of the date of the issuance of this order. Two additional copies each shall be mailed to the Directors of the Water Division and the Office of Ratepayer Advocates. A copy of the comments should be mailed to all Class A water companies. Class A water companies shall serve each other and other interested parties. The Commission's Process Office shall compile and mail to all commenting parties a list of all parties who have filed comments. Each commenting party is required to serve its comments upon request.
4. Reply comments must be filed within 45 days of the date of the issuance of this order, as specified in Ordering Paragraph 3, above.
5. The Executive Director is directed to mail a copy of this order to all regulated water utilities, interested parties, and the workshop's participants.

This order is effective today.

Dated October 22, 1997, at San Francisco, California.

P. GREGORY CONLON

President

JESSIE J. KNIGHT, JR.

HENRY M. DUQUE

JOSIAH L. NEEPER

RICHARD A. BILAS

Commissioners