

**BEFORE THE PUBLIC UTILITIES COMMISSION OF
THE STATE OF CALIFORNIA**

**Order Instituting Rulemaking on the Commission's)
Own Motion into Addressing The Commission's) R.11-11-008
Water Action Plan Objective of Setting Rates that)
Balance Investment, Conservation, and) (Filed November 10, 2011)
Affordability For the Multi-District Water Utilities)
of: California-American Water Company (U210W),)
California Water Service Company (U60W), Del)
Oro Water Company, Inc. (U61W), Golden State)
Water Company (U133W), and San Gabriel)
Valley Water Company (U337W).)**

**REPLY COMMENTS OF
THE NATIONAL CONSUMER LAW CENTER AND
THE UTILITY REFORM NETWORK**

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I. INTRODUCTION

In this proceeding, the Commission has determined to review the sixth objective of its Water Action Plan -- the issue of “setting rates that balance investment, conservation, and affordability, with a focus on multi-district water utilities.”¹ On March 1, 2012, the National Consumer Law Center (NCLC) and The Utility Reform Network (TURN) and the other parties submitted Comments on eight questions raised by the Commission, primarily discussing the feasibility of consolidation and/or a high cost fund.²

In initial Comments, NCLC and TURN demonstrated that the current assistance programs for water customers are limited and inadequate in addressing these goals.³ The Division of Ratepayer Advocates (DRA) similarly noted that in regard to current mechanisms to balance investment, conservation and affordability, it “is concerned that balance is shifting away from affordab[ilit]y in recent cases.”⁴ As explained in NCLC and TURN’s initial Comments, additional measures, particularly a high cost fund, appear promising for increasing affordability of water service to high cost areas.⁵ All parties commenting on the high cost fund, except one,

¹ Order Instituting Rulemaking (OIR) at 2.

² Comments were jointly filed by The National Consumer Law Center and The Utility Reform Network. Comments were also filed by the Division of Ratepayer Advocates (DRA), the Natural Resources Defense Council (NRDC), California-American Water Company (CalAm), California Water Service Company (Cal Water), Del Oro Water Company (Del Oro Water), Golden State Water Company (GSWC), and San Gabriel Valley Water Company (San Gabriel).

³ The need for customer assistance is supported, for example, by the growing percentage of customers enrolled in the utilities’ LIRA and customer assistance programs each year. Enrollment in San Gabriel’s California Alternative Rates for Water program has increased from 20.6% in 2009 to 23.8% in 2010 and 28.2% in 2011. San Gabriel Response to NCLC/TURN Data Request Set I-1e.

⁴ DRA Comments at 12.

⁵ Although it appears that more emphasis should be placed on affordability in maintaining a fair balance of interests, we note that the high cost mechanism proposed by NCLC/TURN would also address conservation, and likely would include investment in many cases.

acknowledge that there are possible advantages to its implementation. Some prefer an intracompany administered fund rather than an intercompany fund. At this early point of investigation, however, there is insufficient basis for eliminating an intercompany high cost fund from consideration and NCLC and TURN urge the Commission to find that each reasonable option for increasing affordability of water service to customers should remain open for the parties and Commission to further evaluate and consider.

Several parties also urged the Commission to update its methodology for district consolidation as a possible mechanism to address affordability. However, as predicted by NCLC and TURN, opening comments make it clear that consolidation efforts must be analyzed carefully and not undertaken lightly. Further, parties must be clear in the use of their terms and policy goals for consolidation must be explicit. As discussed below, consolidation can be another tool in the affordability toolkit, but further discussions are necessary to address various parties' concerns.

NCLC and TURN now jointly submit Reply Comments in response to the comments filed by other parties.

II. REPLY COMMENTS

A. Section 701.10 of the California Public Utility Code Does Not Prohibit the Use of Proposed Affordability Mechanisms

Commenting parties generally share NCLC and TURN's perspective that there is no insurmountable legal impediment to the implementation of the affordability mechanisms discussed in the OIR. While some parties noted the tension inherent in the policy goals of ensuring affordability while complying with the language in Section 701.10 regarding cost of

service and conservation goals, no party cited to Section 701.10 as an absolute bar to Commission action in this area.

1. Section 701.10 Does Not Prohibit a High Cost Fund

Commenting parties generally found no insurmountable legal barriers to establishment of a high cost fund. For example, Cal Water asserts that Section 701.10 necessarily should be read to allow some amount of cross-subsidization, and that there appears to be no blanket prohibition to the possibility of the Commission implementing a high cost fund.⁶ CalAm states that a high cost fund would not directly conflict with the California Public Utility Code, but notes that clarity is needed regarding what constitutes “unreasonable” rate differential between localities of classes of service, pursuant to Section 453(c).⁷ GSWC states that the purposes of Section 701.10 may be better met through policies applied at a region or company-wide basis,⁸ which suggests GSWC believes that a region or company-wide high cost fund could fulfill the requirements of Section 701.10. San Gabriel alone states the requirement of Section 701.10 to “minimize the long-term cost of service” could be read as a restriction on establishing a high cost fund.⁹ However, San Gabriel provides no support or explanation for this legal conclusion.

DRA comments that while the cost of providing water service in particular districts may not be accurately reflected in a high cost fund, Section 739.8 expressly authorizes such a fund if it provides rate relief to low-income customers.¹⁰ NCLC and TURN similarly noted that Section

⁶ Cal Water Comments at 13.

⁷ CalAm Comments at 8.

⁸ GSWC Comments at 12.

⁹ San Gabriel Comments at 7.

¹⁰ DRA Comments at 33.

739.8(c) enables the Commission to create programs for low income customers receiving assistance from a high cost fund where the true cost of service on their water bills separately lists service charge, surcharge, and credit.¹¹

Moreover, while Section 701.10(f) may be interpreted as requiring that water service rates be based on the cost of service, a high cost fund need not impact what rates are implemented, but may operate as a credit.¹² As a credit and not a rate applied to the bills of customers in high cost areas, the requirement of setting rates based on cost of service need not be disturbed. For example, Cal Water's Rate Support Fund is a type of high cost fund, already approved by the Commission and implemented by the water company that does not circumvent cost based ratesetting, but provides a credit, or subsidy to RSF customers.¹³

2. Section 701.10 Does Not Prohibit Consolidation

Several parties addressed the interpretation of Section 701.10 as it relates to both high cost fund and district consolidation in the same discussion. CalAm, San Gabriel, GSWC, and Cal Water find no legal barriers in Section 701.10 for either the high cost fund or consolidation policies, although, as discussed above, some utilities are more conservative in their interpretation of the statute than others.¹⁴

¹¹ See NCLC/TURN Comments at 23.

¹² NCLC/TURN Comments at 30.

¹³ Cal Water Comments at 2 (describing RSF as a subsidy); NCLC/TURN Comments at 25 (explaining RSF as an assistance fund with monies collected through a surcharge; Cal Water Tariff Schedule No. RSF, Revised Cal. P.U.C. Sheet No. 8595-W (applying surcharge to all non-LIRA customers and allocating it as a credit to certain districts).

¹⁴ Cal Am at 7-8, San Gabriel at 7 (decidedly more skeptical about any affordability mechanism complying with section 701.10); GSWC at 12 (calling Section 701.10 an "obstacle" for affordability programs, but noting that application of the policies on a company wide basis may properly balance competing objectives); Cal Water at 13 finding some cross subsidization is appropriate under the statute thereby allowing for limited district consolidation in the public interest.

However, DRA did specifically address district consolidation. As discussed above, a risk of relying on district consolidation to address affordability is that the lower rates for some customers in high cost areas will weaken the price signal provided to those customers to get them to conserve water. DRA suggests that by weakening the price signal, district consolidation may create “tension” between affordability and Section 701.10 (c) that requires the Commission provide “appropriate incentives” to conserve water.¹⁵ However, DRA acknowledges that determining whether a consolidation proposal is in the public interest is a complicated and multi-faceted analysis and that compliance with the statutory requirement to maintain incentives to conserve must be viewed in that context. Therefore, DRA and others acknowledge that consolidation could still satisfy Section 701-10(c) under the appropriate fact-specific analysis.¹⁶

Further, as discussed above related to High Cost Funds, DRA and NCLC and TURN also find that district consolidation satisfies Section 701.10(f), requiring rates to be based on the cost of service if certain criteria are met. Here again, both DRA and TURN and NCLC cite to the statutory support for low income program in Section 739.8 as support for district consolidation and to satisfy Section 701.10(f).¹⁷

B. Consolidation

Most parties acknowledged the important role that district consolidation can play to meet the objective to balance investment, conservation and affordability in the 2010 Water Action Plan. However, parties also urged the Commission to be judicious in its use of consolidation¹⁸

¹⁵ DRA at 29.

¹⁶ DRA at 30.

¹⁷ DRA at 32.

¹⁸ San Gabriel, at page 5 and 6, urged consolidation to only be done on a “case-by-case” basis and always voluntary and only in “the most exigent circumstances.” Cal Water cautions against “large-

and some proposed alternative consolidation plans that may meet their particular districts' needs. Further, almost all of the parties supported the current consolidation guidelines and found them to be useful and relevant.¹⁹ However, several parties agreed with NCLC and TURN that the guidelines should be revised or supplemented with additional considerations based on the Commission's two-decade old history applying the guidelines.

1. Policy Considerations for District Consolidation

While many parties were critical of consolidation policy because of concerns of cross subsidy and impacts on price signals, some utilities noted that consolidation of districts can be consistent with a Commission policy to set water rates to reflect cost of service to discrete areas as closely as possible. California American Water Company (CalAm) tries to bolster the argument for consolidation (and high cost funding) by suggesting that when discussing consolidation, policy makers should take care not to talk in terms of "subsidization."²⁰ CalAm correctly points out that in the electric and gas industries the Commission has determined cost of service and rates on a broader, service territory basis, even though costs to serve urban or rural areas in the state could also differ significantly.²¹

While NCLC and TURN cannot disagree with CalAm's point that the Commission has not adhered to a strict cost of service model for ratesetting in any industry it regulates, CalAm's suggestion that would hide a subsidy is problematic. While customer assistance benefits could be

scale" consolidation at page 6. NCLC and TURN, at page 16, state that consolidation should "not be undertaken lightly."

¹⁹ San Gabriel Comments at 5; Cal Water Comments at 6; NRDC Comments at 2. The exception is GSWC that urges the Commission to modify or eliminate the guidelines, although as discussed below, it neglects to propose specific modifications.

²⁰ Cal Am Comments at 2, note 1.

²¹ Cal Am Comments at 2, note 1.

called many different things (subsidy, credit, payment assistance to a particular area), charges that deviate from cost of service in a significant way, even if only to ensure safe and affordable drinking water to California consumers, must be transparent and clear in their implementation.²²

NCLC and TURN do agree with the point made by CalAm that different types of consolidation can be consistent with cost of service policies and methodologies if the Commission is willing to look at costs across a broader geographic unit or service level aggregation, as they have to implement affordability policies in other industries they regulate.

In contrast, DRA, points out that analogies to other Commission-regulated industries may not be appropriate due to the unique characteristics of water service whose costs are increasing over time and directly tied to considerations that policymakers cannot control, such as climate, geology, and topography.²³ Unlike telecommunications and electricity, the utilities can't simply increase the production line and make more water in areas where water is scarce. Therefore, if the analogy between industries is flawed, then the reliance on affordability measures from those industries also may be faulty.

NCLC and TURN agree with DRA's cautions about relying too heavily on policies from other industries, but note that adoption of models from other industries need not be "all or nothing." Both the lessons learned and benefits achieved from those long-standing affordability mechanisms should inform the discussion here.

San Gabriel Water Company (San Gabriel) claims that the "main beneficiaries" of district consolidation are "customers in small water districts, where high fixed costs must be spread over

²² NCLC/TURN Comments at 22-23; D.96-10-066 at 3 (citing AB3643).

²³ DRA Comments at 7.

a small customer base.”²⁴ Based on other parties’ opening comments, NCLC and TURN find this to be an over-simplification. While certain customers in small water districts may benefit from consolidation, the size of the districts is not nearly as relevant as the costs to serve in each district. Some districts may be small, but may have relatively low costs while larger districts (both in population or land area) may have extremely high costs. For example, Cal Water states that many of its lowest cost of service districts are in the San Joaquin Valley where farmworkers and low income customers are common, while its highest cost districts are in affluent and more densely populated cities in San Mateo and Los Angeles counties.²⁵ In that situation, the more populous and more affluent district could be the beneficiary of consolidation, perhaps at the expense of the low income customers in the more rural areas.²⁶ This is a small but important point when considering the impact, and unintended consequences, of consolidation proposals.

Golden State Water Company (GSWC) offers a unique perspective on consolidation because much of its service area has been consolidated into two main regions through “rate regionalization” but several additional districts in its Northern California territory have yet to be consolidated or regionalized.²⁷ GSWC is not satisfied with the rate regionalization process, “Thus while regionalized rates accomplish the goal of subsidizing high cost areas, such consolidation masks the true cost of water service, and so it counterproductive in promoting conservation.”²⁸ The Natural Resource Defense Council (NRDC) and DRA make similar claims

²⁴ San Gabriel Comments at 3.

²⁵ Cal Water Comments at 7.

²⁶ See DRA Comments at 17.

²⁷ GSWC Comments at 4.

²⁸ GSWC Comments at 5.

in the abstract.²⁹ NCLC and TURN agree that the risk of losing a proper price signal for conservation must be part of the Commission’s analysis for any conservation proposal.

However, using GSWC’s example it would be unsustainable to allow residents in Calipatria to pay the same high rates for water as the residents in Clearlake. There must be a balance to provide rate relief but maintain price signals by ensuring rates are not set too low.

2. Alternative Proposals to District Consolidation

CalAm and Cal Water both suggest a variation of district consolidation that would entail the consolidation only of certain cost categories among districts where, as CalAm describes it, the districts share “commonalities in infrastructure that have similar maintenance, engineering and operations practice.”³⁰ Both CalAm and Cal Water list similar examples of possible cost categories for consolidation, including meter reading, billing, call handling and some capital costs. Cal Water lists several additional categories including management expenses, legal fees and vehicle maintenance.³¹

Many costs for services provided by the parent company or affiliates of these utilities are already shared among each utility’s districts. However, both CalAm and Cal Water suggest different allocations for these district-specific costs than the allocation that the Commission currently uses to apportion shared corporate services. To evenly apportion these consolidated costs, CalAm proposes a “common charge for metered customers.” Cal Water also notes that

²⁹ NRDC Comments at 2; DRA Comments at 5.

³⁰ CalAm Comments at 5. Cal Water Comments at 7-10. San Gabriel also offers a similar proposal but with less detail. More closely related to Cal Water’s proposal, San Gabriel suggests that all costs could be consolidated except purchased water and power which presumably significantly vary among districts. San Gabriel at p. 6. In addition to the concerns with CalAm’s partial consolidation proposal, NCLC and TURN would be concerned that leaving a high-cost district to shoulder its own power and purchased water costs may not solve the problem making the consolidation of the other costs a wasted effort.

³¹ Cal Water Comments at 9-10.

cost consolidation should serve to spread the costs “evenly” to all customers in all districts, but does not suggest a mechanism.³²

At this early stage of the docket, NCLC and TURN are open to alternative proposals to traditional district consolidation/single tariff pricing. However, both utilities’ proposals raise several issues. First, would CalAm’s “common charge” be a flat rate or part of the volumetric rate? By CalAm’s description it sounds like it would be a flat rate, which would potentially impact price signals and the effectiveness of tiered rates. Second, prior to consolidation of the costs for rate design purposes, would the Commission first determine if the costs at issue were properly and reasonably incurred on a district by district basis? CalAm asserts that such a proposal “would not involve significant cost shifting” and Cal Water says the costs would be allocated “evenly” but neither of them elaborates or provides sufficient support for their vague assertions.³³ Third, utilities must have the burden to demonstrate that this cost consolidation would indeed promote economies of scale and that such economies of scale would result in lower rates to high cost areas. This is especially the case if the “supply costs” (which Cal Water describes to be purchased water, water treatment and power cost) -- arguably the largest cost drivers--would not be included in the consolidation. Finally, cost consolidation of only certain cost categories would likely make rate design more complicated instead of simplifying rate design, a key goal of rate consolidation.

CalAm also raises the possibility of Class A utilities purchasing smaller Class C and D utilities as a method of consolidation.³⁴ This Commission has had a long-standing policy to

³² CalAm Comments at 5; Cal Water at 8.

³³ CalAm Comments at 5; Cal Water at 8.

³⁴ CalAm Comments at 7; *See also*, San Gabriel Comments at 5,6.

encourage Class A utilities to purchase small systems. In both the 2005 and 2010 Water Action Plans, the Commission explicitly included reference to “incentivize large utilities to buy small ones” as a means toward accomplishing the objective to Maintain Highest Standards and an overall principle of Safe, High-Quality Water.³⁵

TURN and NCLC do not disagree that some small water companies may not have the resources to effectively provide water service to their customers. In some instances, company acquisitions could provide the means to upgrade those smaller systems and provide needed capital for on-going operations costs. Acquisitions and mergers are a form of consolidation and serve many of the same goals as consolidation within a single company. However, just as in the case of consolidation of districts within a company, the purchase of smaller water companies may not always be the right solution and any incentives applied to the transaction could be costly for customers of both utilities.

CalAm cites to additional land development as a benefit of consolidation and, in particular, the purchase of smaller independent systems.³⁶ Conversely, DRA cited to additional land development in areas with scarce or high cost water as one of the main *risks* of consolidation or high cost funding.³⁷ TURN and NCLC generally agree that land development in areas of scarce or high cost water is not a policy that this Commission should encourage through low water rates. However, reasonable and conservative consolidation proposals should not create those inefficient incentives for improper land development and growth.

GSWC urges the Commission to consider a very different proposal to allow the cost of

³⁵ 2010 Water Action Plan at 5, 9.

³⁶ CalAm Comments at 7.

³⁷ DRA Comments at 28-29. *See also*, Cal Water at p. 12-13 and GSWC Opening at p. 11 where these utilities also raise concerns about increased development in high cost areas.

all capital projects to be included in a General Office cost allocation methodology across all districts instead of on a district specific basis as it is today.³⁸ While GSWC points out the potential benefits of such a proposal, including “rate stability” and avoidance of rate shock, NCLC and TURN caution that such a proposal may just spread the negative effects of rate instability and rate shock across more GSWC ratepayers if it creates greater incentive for, and no check against, incurring additional and excessively large capital expenses that will simply impact more ratepayers. If the Commission is interested in further discussing this proposal, it should be included in workshops where there can be significantly more discussion and explanation of the implications of such a proposal.

San Gabriel raises concerns about the Rate Case Plan, but makes no proposals to tie its concerns into the scope of this docket.³⁹ NCLC and TURN agree that the transition to the rate case schedule set forth in the plan has not been smooth and often has resulted in ratepayers feeling overwhelmed by rate increases for their water. It is also correct that the consolidated rate cases have made it more challenging to take a detailed look at the specific costs and revenues for a single district. However, it is also valuable that with rate case consolidation, the Commission has a “big picture” as to the utility’s operations and revenues and can make adjustments in those figures while taking the total company into consideration. Related to the issues in this docket, these consolidated rate cases also allow the Commission to see the wide disparities in rates among the district as they create a rate design for all the districts. While the implementation of the rate case plan has been challenging, changes to the rate case plan do not appear to be within the specific scope of this docket.

³⁸ GSWC Comments at 13.

³⁹ San Gabriel Comments at 4.

3. 1992 Consolidation Guidelines

Opening comments included responses to the questions in the OIR that specifically asked about the Commission's current consolidation guidelines. NCLC and TURN suggested that the guidelines themselves were still relevant and included valid considerations for analysis of district consolidation proposals. However, additional criteria should be developed in light of changing demographics, conservation programs, and the considerable gap in affordability among districts within the same company.⁴⁰ San Gabriel was the only utility that suggested the guidelines required no change.⁴¹ Along with NCLC and TURN, several utilities suggested additional or changed criteria.

CalAm noted that the original policy goals of the guidelines were a straight forward matter of ensuring administrative efficiency and regulatory streamlining, but that over the years the Commission has applied the guidelines for much more substantive purposes, including rate affordability. It urged the Commission be clear on the exact goals of the guidelines at it considers a possible emphasis on consolidation.⁴² NCLC and TURN agree. CalAm, however, does not propose additional criteria or guidelines but, instead, provides a list of additional policy goals. Presumably, CalAm is suggesting that a consolidation proposal should be analyzed against these additional policy goals: smooth rate increases, increasing affordability, increasing economies of scale, facilitating greater public access to reliable water supplies and, most broadly, promoting the common good.⁴³ While NCLC and TURN agree with the inclusion of these policy goals,

⁴⁰ NCLC/TURN Comments at 18-19.

⁴¹ San Gabriel Comments at 5.

⁴² CalAm Comments at 3.

⁴³ CalAm Comments at 5.

providing actual criteria or guidelines to guide implementation is necessary to help the Commission come to workable solutions. A prioritization of these additional goals, and specific criteria to analyze consolidation proposals against them, are necessary to properly implement these goals and should be further discussed.

Cal Water, on the other hand, proposes specific additional criteria for the Commission to use in addition to the Guidelines to satisfy the Water Action Plan goals of balancing investment, conservation and affordability. Such considerations include socioeconomic status, district size, and current and future infrastructure needs.⁴⁴ TURN and NCLC also suggested that infrastructure needs should be considered as an additional criteria.⁴⁵ However, as discussed above, NCLC and TURN do not find that the size of the districts is indicative of the benefits of consolidation.

NRDC also suggests several revisions to the guidelines including the addition of several criteria related to average cost of wholesale purchased water, existing levels of water use and potential administrative cost savings.⁴⁶ NCLC and TURN note in Opening Comments that the Commission has looked at potential administrative cost savings in the past and agree that it should be looked at as part of the analysis. NCLC and TURN also agree with NRDC that, ideally, the potential districts should have similar levels of water use for the reasons stated by NRDC.

However, NCLC and TURN do not necessarily agree with NRDC that the districts should

⁴⁴ Cal Water Comments at 6; *See also* DRA Comments at 17, also recommending that average income level (socio economic) should be part of the analysis so that larger, but low income, districts do not subsidize high income but higher cost districts.

⁴⁵ NCLC/TURN Comments at 19.

⁴⁶ NRDC Comments at 3. *See also*, DRA Comments at 15, 16 wherein DRA suggests average water use and reduction in administrative costs should be two of only a few additional criteria for the guidelines.

have similar costs of water. Purchased water is a huge cost driver for many districts and may be a factor in declaring a certain district “high cost.” If NRDC is saying that districts should only be candidates for consolidation if they have similar purchased water costs, that would suggest that in many cases high-cost districts would be attempting to consolidate with other high-cost districts, thereby defeating the purpose of consolidation. NCLC and TURN agree with NRDC (and DRA and others) that maintaining a price signal for conservation is important.⁴⁷ However, similarity of purchased water costs should not be a major consideration in consolidation analysis.

GSWC encourages the Commission “to consider modifications to or elimination of these guidelines as needed to meet the goals of the OIR.”⁴⁸ It notes that the Commission itself has not strictly relied on the guidelines but instead has approved consolidation on other considerations, even where the guidelines may not have allowed consolidation.⁴⁹ In those instances, rate relief became the predominant policy goal, with other considerations or concerns about consolidation moving to the background. GSWC encourages continued flexibility so that consolidation proposals do not need to meet all four of the criteria to be adopted. However, GSWC also suggests emphasis on the operational element of the guidelines above all others so that consolidation would be allowed if districts were operated in a similar manner including similar billing systems or management structure.⁵⁰ While TURN and NCLC agree that operational similarities would make consolidation logistically easier, many other considerations must be

⁴⁷ NRDC Comments at 2,4; DRA Comments at 8.

⁴⁸ GSWC Comments at 9.

⁴⁹ GSWC Comments at p. 6. *See also*, DRA Comments at 14, acknowledging that the Guidelines “do not limit the Commission’s ability to review any [consolidation] proposal on a case-by-case basis” beyond the Guidelines themselves.

⁵⁰ GSWC Comments at 9.

taken into account, including those proposed in NCLC and TURN Opening Comments.⁵¹

Even though San Gabriel states that it sees a need to revise the guidelines, it makes the point that one of the main “hurdles” for consolidation (as well as high cost funding) is “ratepayer acceptance” and urges the Commission to look at ratepayer attitudes when analyzing a proposal for consolidation.⁵² NCLC and TURN agree that the implementation of any mechanism that would change a customers’ rate must be done with sufficient consumer education and proper messaging. Indeed, as discussed in NCLC and TURN’s Opening Comments, one of the many criteria used by the Commission in previous cases to evaluate consolidation proposals, in addition to its 1996 guidelines, is “customer preference.” NCLC and TURN urge that the Commission continue to incorporate this criteria into its analysis.⁵³

As ratepayer advocates, NCLC and TURN urge the Commission to listen to and address ratepayer concerns and opinions in its decision-making process. However, NCLC represents that interests of low-income consumers and TURN has a responsibility to advocate for all ratepayers, not just the majority of the ratepayers in a particular district. Further, this Commission has a responsibility to develop policies that look at the impacts to all ratepayer groups, not just the loudest groups. The most vulnerable ratepayers that may live in rural areas or be low income may not have the loudest voices because their special needs may not be met by policies that tend to protect the majority. Therefore, while the Commission must be sensitive to and take into account customer preference, loud voices complaining about having to “pay for someone else’s water” cannot alone serve to frustrate the broader policies contained in the Water Action Plan

⁵¹ NCLC/TURN Comments at 17-19.

⁵² San Gabriel Comments at 7.

⁵³ NCLC/TURN Comments at p. 18, citing to D.05-09-004 and D.08-05-018.

and set forth in statute.

As discussed above, parties generally agree with NCLC and TURN that the Commission's consolidation guidelines and current consolidation policies are useful and relevant to help address affordability in high cost areas. However, some changes to the guidelines are warranted to allow for consideration of additional factors and to capture the Commission's evolution of its consolidation analysis over the years.

C. Feasibility and Desirability of Implementing a High Cost Fund

A number of parties submitted comments in support of the Commission's consideration of a high cost fund. For the one party that prefers that it not be implemented, NCLC and TURN demonstrate that this opposition may be based on errors in assumptions. For parties preferring an intracompany fund to an intercompany fund, we show that this preference is inadequately explained and supported, and insufficient to warrant elimination of an intercompany high cost fund from consideration at this point. Additionally, we note that the proposal to adopt a high cost fund for the sole purpose of increasing company revenue is a misguided application of the fund, and contrary to the traditional purpose of a high cost fund and the objective of this docket to enhance affordability of water service to customers. NCLC and TURN address the concerns below.

Del Oro Water Company (Del Oro Water) states that its preference is to forgo the establishment of a high cost fund, because it believes that 5,600 of its customers in Northern California would end up subsidizing 2,500 customers in Southern California; however, Del Oro Water notes that it does not have resources to identify all high cost fund impacts, so it relies on the responses of the class A water utilities in this proceeding.⁵⁴ First, NCLC and TURN note that

⁵⁴ Del Oro Water at 2.

Del Oro Water's assumption of 5,600 customers subsidizing 2,500 may not be correct; the Commission has not yet defined the customer group(s) to receive assistance from a high cost fund. Further, making this conclusion in absence of information regarding amount of surcharge seems premature. Even if customers who pay into a high cost fund are not the direct recipients of the funding, they may be indirect beneficiaries and the amount of surcharge may be so small that it would be deemed reasonable and acceptable.⁵⁵

San Gabriel states that high cost funds within a single water utility should be specifically tailored and that extending high cost funds beyond the single utility should only be used in exigent circumstances.⁵⁶ However, San Gabriel does not elaborate upon or provide support for the reasoning behind this recommendation other than to state that ratepayers' acceptance may be the major obstacle of establishing a high cost fund.⁵⁷ As discussed above, NCLC and TURN acknowledge that ratepayer acceptance should be considered, however, in issuing an Order, the Commission's conclusions should rely instead on recommendations that are further developed and supported than this.

Cal Water notes that a high cost fund such as its Rate Support Fund (RSF) high cost fund, is preferable to a high cost fund modeled after California's telecommunications High Cost Fund A and B, which have been the subject of much contention.⁵⁸ While it notes the merits of using a high cost fund mechanism to increase affordability in very high cost areas, it states that its customers are concerned that the current RSF is insufficient in the context of high water bills in

⁵⁵ The Cal Water RSF is funded through a surcharge of \$0.010 per 100 cubic feet for all metered customers and a flat rate surcharge for flat rate customers. Cal Water Tariff Schedule No. RSF, Revised Cal. P.U.C. Sheet No. 8595-W; NCLC/TURN Comments at 25.

⁵⁶ San Gabriel Comments at 6.

⁵⁷ San Gabriel Comments at 7.

⁵⁸ Cal Water Comments at 4, 11.

RSF districts.⁵⁹ This concern supports the requests of NCLC and TURN, as well as DRA, that the Commission establish a schedule providing further opportunity for investigation and comment. Doing so will help lead to a final decision that ensures that the mechanisms adopted in this proceeding adequately address affordability issues for customers in California's high cost areas.⁶⁰

CalAm notes that there are numerous advantages of a high cost fund such as Cal Water's RSF that is funded by all customers. Such a fund can minimize significant, localized costs to customers while allowing necessary infrastructure investment.⁶¹ CalAm proposes that requirements of a high cost fund should include clear purpose and intent of the fund to guide implementation, along with customer notice, operation of the funding mechanism, avoidance of overly burdensome rates to customers contributing to the fund, and reporting requirements.⁶² NCLC and TURN do not disagree, but would add that further measures be put into place, so that there is tracking of data and expenditures to demonstrate reasonableness in administration and application of a high cost fund, and an increase in public accountability.⁶³

In commenting on the potential impacts of a high cost fund on development and conservation, however, CalAm appears to conflate the high cost fund with water system consolidation discussed above. CalAm states that costs of capital for acquiring smaller systems

⁵⁹ Cal Water Comments at 4-5.

⁶⁰ NCLC/TURN comments at 32-33.

⁶¹ CalAm Comments at 6. Note that Cal Water describes topography, distance from quality water supply, remoteness of area, small size of rural districts that lack economy of scale, and rate base required per customer are the characteristics that lead to high cost of service in its RSF districts. Cal Water Comments at 8.

⁶² CalAm Comments at 7.

⁶³ NCLC/TURN Comments at 22-24, 26.

could be spread over a larger customer base, making land development more attractive due to accelerated infrastructure investment.⁶⁴ As discussed above and further explained in our initial comments, however, acquisitions of systems are an issue of consolidation which is not necessarily tied to implementation of a high cost fund.⁶⁵ CalAm also suggests that a high cost fund could be applied to “undercollected balances” when consumer conservation means utilities collect revenues below their revenue requirement.⁶⁶ NCLC and TURN object to such application of a high cost fund. One of the main purposes of implementing a high cost fund in this proceeding is to address the issue of affordability.⁶⁷ Applying these funds to uncollectible or “undercollected balances” would be contrary to the public policy of a high cost fund in furthering customer affordability, and simply serve as a windfall to utilities and their shareholders.

GSWC states that a high cost fund could be implemented through a transparent surcharge to all applicable bills, but notes that the Commission should carefully define what constitutes a high cost area to avoid unintended consequences.⁶⁸ It urges the Commission to consider the socioeconomic status of an area when considering the price of water service in an area.⁶⁹ NCLC and TURN agree with the concept of transparency and that socioeconomic status of an area must

⁶⁴ CalAm Comments at 7.

⁶⁵ NCLC/TURN Comments at 13-14 (definition of consolidation includes acquisition of a system by another entity). *See also* Page S. Manning, et al., Consolidation Issues: Pros, Cons, Options and Perceptions (Mississippi State University Extension) at 6-8, available at: http://www.msucare.com/water/pubs/consolidation_issues.pdf.

⁶⁶ CalAm Comments at 7.

⁶⁷ Order Instituting Rulemaking at 1-2; NCLC/TURN Comments at 3-5, 24-25,27-28. *See also* GSWC Comments at 10 (a high cost fund can help ensure affordable rates in high cost areas with minimal impact on other areas).

⁶⁸ GSWC Comments at 9-10, 12.

⁶⁹ GSWC Comments at 12.

be considered along with the cost of service to that area in determining whether the area should benefit from allocations from a high cost fund.

DRA supports a high cost fund only if it is targeted to increase affordability for those most in need.⁷⁰ Like CalAm and Cal Water, it recommends that instead of an end-user surcharge on all Class A investor owned water companies which could become complex and raise issues of equity, the Commission should consider an intra-company high cost fund similar to the Cal Water's RSF, to increase affordability.⁷¹ NCLC and TURN agree that an intra-company high cost fund has potential to increase affordability. However, at this preliminary stage of investigation, NCLC and TURN also believe that it is too early to eliminate the inter-company high cost fund from consideration and that the problems associated with the inter-company telecommunications high cost fund in California need not be replicated in the context of the water industry. Rather, improvements to that model, based on learning and past experience, can be made in this proceeding.⁷² Additionally, an inter-company fund, while providing equal funding opportunities to both smaller and larger utilities, has the added benefit of making

⁷⁰ DRA Comments at 25. DRA also proposes workshops to discuss issues such as limiting eligibility in the high cost fund to districts where at least 50% of customers are at or below 200% of federal poverty guidelines and average residential water usage of 10 Ccfs or less. See DRA Comments at 25-26. NCLC and TURN agree with DRA's recommendation that workshops to discuss eligibility and other issues should be discussed in relation to a high cost fund. While it is true that establishing eligibility criteria for participation in a high cost fund could help target that assistance, see NCLC/TURN Comments at 27, NCLC and TURN additionally recommend that before firm income and consumption eligibility criteria are established, that the Commission and parties should have an opportunity to determine whether these criteria would sufficiently cover customers in all areas where affordable water service is a problem.

⁷¹ DRA Comments at 24-25.

⁷² NCLC/TURN Comments at 22-24 (explaining criticisms of California's telecommunications high cost funds), 26 (accountability measures and review for reasonableness should be implemented in a water high cost fund).

available a larger pool of funding to smaller utilities than would be possible under an intra-company high cost fund.⁷³

NRDC states that a High Cost fund, if implemented, should be focused on essential indoor water use and include a strong price signal to encourage water conservation at higher consumption levels.⁷⁴ While NCLC and TURN do not necessarily disagree with this concept, we strongly caution that the Commission should not lose sight of the danger in weighing the conservation signal issue too heavily if, in reality, people already cannot afford even the basic amount of water necessary for consumption.⁷⁵

III. CONCLUSION

NCLC and TURN respectfully request that the Commission consider the Reply Comments above, in resolving the water affordability issues in this proceeding. Currently, available assistance to make water service affordable for California customers is inadequate, and more is needed. The Commission should develop a detailed proposal in light of this proceeding,

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⁷³ NCLC/TURN Comments at 26-27.

⁷⁴ NRDC Comments at 4.

⁷⁵ See NCLC/TURN Comments at 5 (pointing to example of increasing water service disconnections of low-income customers for nonpayment); DRA Comments at 2 (“Water rates should be low enough so that low-income customers will not have to forgo other essential services, (food, energy, medical care, etc.) to pay their water bills”).

and adopt a schedule for workshops, comments on guidelines for consolidation and determining all of the ways that a consolidation and/or a high cost fund can be successfully implemented for California's water customers.⁷⁶

Respectfully Submitted,

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⁷⁶ See NCLC/TURN Comments at 32; DRA Comments at 34.