

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

WATER DIVISION
Water Advisory Branch

RESOLUTION NO. W-4276
July 12, 2001

R E S O L U T I O N

(RES. W-4276), ALL WATER AND SEWER SYSTEM UTILITIES.
ORDER AUTHORIZING A GENERATOR COST MEMORANDUM
ACCOUNT.

BY ADVICE LETTER NO. 326 FILED BY SAN JOSE WATER
COMPANY (SJWC) ON MAY 7, 2001.

SUMMARY

By its Advice Letter No. 326, SJWC requests memorandum account coverage for certain expenses associated with anticipated rolling blackouts. This resolution allows all water utilities to book the incremental costs needed to run backup generators (up to \$0.20 per kilo-watt hour) and extends such protection to sewer system utilities. It denies protection for the other costs.

BACKGROUND

In its advice letter San Jose lists the following costs impacts if a rolling blackout occurs:

- a. Additional groundwater production costs during on-peak demand to make up for any reductions in import water deliveries from the Santa Clara Valley Water District due to source water supply interruptions from the State and Federal water projects.
- b. Additional groundwater production costs to replace surface water supplies that will be held back to serve critical zones during blackouts.
- c. Additional groundwater production costs to make up shortfalls in storage resulting from previous day(s) blackouts. Sufficient storage must be maintained to sustain the system through the next day and to provide for minimum fire protection in each operating zone.

- d. Leasing costs for generators for back-up power.
- e. Fuel to run the production/booster station generators during blackouts.
- f. Additional maintenance required on the diesel generators due to the increased operation during blackouts.
- g. Loss of cost efficiency due to pumping during on peak hours. Distribution mix of sources of supply under energy blackouts will not yield optimal energy efficiency.
- h. Labor overtime costs associated with service restoration following blackouts.

It requests that it be allowed to book these costs to a memorandum account for later recovery.

The California Water Association (CWA) represents its member water companies before the legislature, and it has participated in Commission proceedings as a spokesperson for the regulated water industry. By letter dated May 21, 2001, CWA supports SJWC's request for memorandum account treatment and recommends that the Commission issue a resolution authorizing all water companies to establish Electric Power Shortage Memorandum Accounts (accounts).

NOTICE AND PROTESTS

Since this is not a request for a rate increase or diminishment of service quality, no public notice is required. Notice will be required when the utility applies for recovery of the net collections in the account.

The Commission's Office of Ratepayer Advocates (ORA) filed a timely protest to SJWC's advice letter on May 24, 2001 and a response to CWA's letter on May 30, 2001. The gravamen of the protest is that the filing does not meet the guidelines for the establishment of a memorandum account because SJWC has not shown that the expense is substantial. It also mentions, and in its response to CWA's letter expands on this, that operating and financial risks are addressed during a water company's general rate case (GRC). As a result of that process, the authorized return on equity includes provision for events such as electric power outages. ORA recommends that, if the Commission wishes to allow the costs that SJWC and CWA list to be booked to the memorandum account, it also require the utilities to accept a reduction in return on equity of some amount. It references Decision 91-10-041, October 23, 1991, where the Commission provided memorandum account protection for losses due to California's drought, but required a 20 basis point reduction in return on equity to compensate for the reduced risk.

In its response on May 31, 2001, SJWC notes that it is impossible to predict the impact of rolling blackouts and that SJWC is on PG & E's real-time pricing schedules. If SJWC has to pump during peak times, its cost would be over ten times the amount currently reflected in SJWC's rates. It likened this account to the Catastrophic Event Memorandum Account in Resolution E-3238, dated July 24, 1991, and pointed out that recovery of that account is guaranteed, subject to reasonableness review.

DISCUSSION

Over the years the Commission has provided memorandum account protection for many expense items incurred by water and sewer service utilities, some of the more recent include:

Company	Resolution No.	Date	Purpose
Citizens	W-4227	October 5, 2000	Cover costs to comply with fluoridation requirements
Central Camp	W-4225	September 21, 2000	Engineering and legal expenses related to new source of supply
California-American	W-4188	February 3, 2000	Emergency water conservation expenses

Memorandum accounts are appropriate when the following conditions exist:

- a. The expense is caused by an event of an exceptional nature that is not under the utility's control;
- b. The expense cannot have been reasonably foreseen in the utility's last GRC and will occur before the utility's next scheduled rate case;
- c. The expense is of a substantial nature in the amount of money involved; and
- d. The ratepayers will benefit by the memorandum account treatment.

Clearly, the possibility of rolling blackouts is an exceptional event and could not have been anticipated in the utilities' last GRCs. Although the extent is unknown, estimates of fifty days of rolling blackouts in calendar year 2001 have been promulgated. As the summer is traditionally the season of highest demand for water utilities, impacts due to rolling blackouts could be significant.

Customers would benefit from the utilities' efforts to mitigate the impacts of rolling blackouts because water systems, and sewer service systems also, rely on electricity to run pumps, treatment facilities and control systems that monitor and optimize the use of facilities. In the event of a power failure, some water systems can use existing storage to keep positive pressure in the pipelines. Other systems, which rely on pump pressure, will experience dewatering. Systems with storage can also experience dewatering if the demand exhausts the stored water. In addition to the inconvenience to the customer, dewatering constitutes a health threat since contaminants can enter the water system. Normally a dewatered system results in a boil water order until water tests indicate the system is clean.

Sewer systems also rely on pumps and control systems to operate their facilities. Lack of power can result in delays in operation, with potential backup in the sewer lines, and potential loss of decomposing bacteria. One Commission-regulated sewer utility, Watertek, lost much of its composting bacteria due to a rolling blackout last winter. It estimated that it will take over 90 days to fully recover its processing capability. It is in the customer's interest that these detrimental impacts be avoided.

But the points ORA makes in its protest, as to whether memorandum account protection is necessary, and, if it is, whether there should be some contribution on the utilities' part, deserve addressing. California uses future test year rate of return ratemaking for water and sewer system utilities. Many costs can change between the time rates are set and the time events occur. In this case neither San Jose nor CWA has provided an estimate of the dollars involved, or compared that estimate to authorized revenues. Additionally, neither entity has claimed that, in the absence of memorandum account protection, any water company would be disadvantaged in actually doing its best to mitigate the deleterious effects of rolling blackouts. Without a showing that the memorandum account is needed to provide an incentive to improve service to the customers, this is just a request for cost-protection. Such protection may be incompatible with California's regulatory policy and, if so, should be denied.

Water Division staff is presently contacting all Commission regulated water and sewer service utilities to determine their vulnerability to rolling blackouts. While many of these utilities took action to provide back up generators and develop emergency action plans prior to and in 1999, as a result of the Y2K and Loma Prieta earthquake concerns, some systems could still be affected by rolling blackouts; however, there is no reason to believe that tracking costs in a memorandum account would reduce those impacts. Since tracking these costs will not provide improved service, these costs should be denied memorandum account protection, except one such cost discussed below.

SJWC's item e requests memorandum account protection for fuel used to power backup generators. Since 1978 this Commission has allowed water and sewer system utilities to offset changes in electricity and natural gas expenses (some water pumps use natural gas for power), as well as purchased water costs and groundwater extraction charges (pump taxes). Allowing water and sewer system utilities to book their incremental cost for diesel or other generator fuel, over the cost of electricity or natural gas, would be consistent with this policy.

Also, on June 7, 2001, the Commission approved Decision 01-06-009 authorizing a Rolling Blackout Reduction Program for San Diego Gas and Electric Company. This program adopts an energy payment of \$0.20/kWh to certain owners of backup generators to help cover the fuel and maintenance cost of running these generators during blackouts. In light of this policy, allowing water and sewer systems to book \$0.20 per kWh would be appropriate as well.

On the other hand, if the utility were earning more than its authorized rate of return in the calendar year in which the expenses were incurred, it would be unfair (and unnecessary) to allow recovery of these expenses from ratepayers. As with all additional charges booked to memorandum accounts, if the utility is already over-earning, ratepayers should not be required to provide even greater revenues to the utility. Thus it is reasonable that the utilities pass an earnings test. Fortunately we have already provided for such a test. During the three year rat cycle, water utilities must pass a Weather-normalized earnings test before the second test year or attrition year rates can be approved. This test is appropriate in this situation also.

As to ORA's protest, staff believes that not allowing recovery of any expenses other than incremental costs to provide electricity by backup generators meets the concerns expressed by ORA. Staff does not recommend a reduction in return on equity in return for this memorandum account, because protecting utilities from variations in purchased power was the policy when the general rate cases were processed and the resulting reduction of risk was included in the determination of rate of return.

Staff recommends that all water and sewer system utilities be authorized to book to a Generator Cost Memorandum Account the incremental costs of diesel or other fuel over purchased electricity or natural gas, as appropriate, and the extra cost of maintenance for the operation of backup generators to power pumps or office or shop space up to a maximum of \$0.20 per kWh generated. Class B, C and D utilities may request recovery by advice letter. Class A utilities shall request recovery in their next general rate proceeding. Staff will audit the account and recommend disposition, as the public interest requires.

In the Southern California Water Co. Headquarters case, Decision 92-03-094 (March 31, 1992) 43 Cal. P.U.C. 2d 600, this Commission clearly stated that memorandum account tracking could only occur prospectively:

“It is a well established tenet of the Commission that ratemaking is done on a prospective basis. The Commission’s practice is not to authorize increased utility rates to account for previously incurred expenses, unless, before the utility incurs those expenses, the Commission has authorized the utility to book those expenses into a memorandum account or balancing account for possible future recovery in rates. This practice is consistent with the rule against retroactive ratemaking.” (Emphasis in original.)

Therefore, we will only allow the tracking of expenses incurred after the establishment of this memorandum account. Because rolling blackouts may occur at any time, this resolution should be effective today.

FINDINGS

Allowing all water and sewer system utilities to establish a Generator Cost Memorandum Account as described in this resolution is in the public interest. All other coverage requested in the advice letter should be denied. Because a generation shortfall could occur at any time, this resolution should be effective today.

THEREFORE IT IS ORDERED that:

1. From the effective date of this order and until December 31, 2001, all water and sewer system utilities are authorized to book the incremental expenses for fuel and maintenance for providing power during rolling blackouts, with an upper limit of \$0.20 per kWh generated, to a Generator Cost Memorandum Account.
2. Utilities utilizing the account may file for recovery by advice letter or in a general rate proceeding, depending on size.
3. Class A utilities must file a weather normalized means test listing adopted, recorded and weather-normalized adjusted, for the calendar year in which these expenses were incurred. Class B, C, and D utilities and sewer system utilities may also file these documents or their annual report for the year. If these documents indicate that a utility was earning more than its last authorized rate

of return, recovery shall be denied.

4. 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 July 12, 2001; the following Commissioners voting favorably thereon:

WESLEY M. FRANKLIN
Executive Director

LORETTA M. LYNCH
President

HENRY M. DUQUE
RICHARD A. BILAS
CARL W. WOOD
GEOFFREY F. BROWN

Commissioners