



ALJ/GT2/mef 5/27/2021

FILED

05/27/21
11:55 AM

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U338E) for Authority to Increase Rates for its Class C Catalina Water Utility and Recover Costs from Water and Electric Customers.

Application 20-10-018

**ADMINISTRATIVE LAW JUDGE'S RULING
ON LIMITED ISSUES BRIEFED**

Summary

This ruling directs Southern California Edison (SCE) to provide additional proposals for recovery of its costs in addition to those proposed in its application filed October 30, 2020, given the legal arguments and analysis presented in the limited briefing provided by the parties on Scoping Issue 2Bi, whether the Commission has authority to transfer recovery of SCE's Santa Catalina Island water utility (Catalina Water) service costs to SCE's electric utility customers who do not receive said water service.

1. Procedural Background

On October 30, 2020, SCE filed the instant application (Application) for approval of a Test Year 2022 General Rate Case (GRC) for Catalina Water. The Application seeks recovery of costs from Catalina Water customers and system-wide electric customers. The Application proposes to recover these costs via phased-in increases in Catalina Water customer rates, as well as collecting \$28.969 million from SCE's electric customers.

A prehearing conference (PHC) was held on January 7, 2021. On January 29, 2021, the Scoping Memo was issued and directed the parties to file, by March 5, 2021 and March 19, 2021, their respective Opening and Reply Briefs on Scoping Memo Issues 2Bi and 2Ci, as follows:

2Bi: Does the Commission have the authority to charge SCE's water utility service costs to SCE's electric utility customers who do not receive said water service?

2Ci: What cost recovery approaches should be considered other than SCE's proposal to recover water utility costs from Catalina Water customers and SCE's electric utility customers?

Parties subsequently filed briefing on these matters.

On March 30, 2021, Public Participation Hearings were held in this proceeding.

2. Discussion of Cross-Subsidy Issue

The Application seeks Commission authority to recover costs related to SCE's ownership and operation of Catalina Water, from 2022-2026. Most of these expenses are drought-related or capital expenditures. The Application proposes to recover these costs from Catalina Water ratepayers as well as SCE's mainland electric system customers.

The Utility Reform Network (TURN) and the Public Advocates Office (Cal Advocates), in their protests, question whether the Commission has the authority to approve such a proposal, where there is no obvious nexus between the mainland electric customers and the cross-subsidized costs they would be paying.¹

¹ TURN Protest at 2-3; Cal Advocates Protest at 2.

The Scoping Memo ordered briefing from the parties on issues 2Bi and 2Ci.

2.1. SCE Position

SCE, in its briefs, argues that the proposed cross-subsidy, whereby SCE's mainland electric customers would pay for the costs of the Catalina Water utility which does not serve them, is just and reasonable under Public Utilities (Pub. Util.) Code² (Code) Section 451, because the cross-subsidy, as proposed, is in the public interest and in turn is just and reasonable. Catalina's unique situation and compelling need for relief gives the Commission cause to approve the proposed cross-subsidy, which would be in the public interest.³

SCE notes that the Commission has previously recognized that the use of cross-subsidies with regards to utility costs necessarily requires a weighing of benefits and costs, in order to determine whether rate averaging is in the public interest.⁴ SCE then presents various subsidies the Commission has previously approved, across different industries and contexts, including subsidies across different geographical, customer, and income groups.⁵ SCE then argues that public policy supports the proposed cross-subsidy, as it will help maintain the water supply for Catalina Island residents, and that the small number of island residents cannot afford to shoulder all of the costs of the necessary infrastructure improvements needed on the island.⁶ Approval of the cross-subsidy could be

² All references to the code are to the California Public Utilities Code, unless otherwise specified.

³ SCE Limited Opening Brief at 2.

⁴ *Id.* at 3.

⁵ *Id.* at 4-5.

⁶ *Id.* at 5-6.

narrowly-tailored, and ensure Catalina Island residents have safe, affordable water available to them.⁷ Approval in such an instance would be reasonable, given the Commission's broad authority to interpret Code Section 451.⁸

Longstanding Commission precedent has established that utility charges must bear a nexus with the customers being charged them.⁹ SCE maintains that such a nexus exists between SCE mainland electric customers and the provision of water service to Catalina Island. SCE states that hundreds of thousands of its electric customers visit Catalina Island as tourists and utilize the water service.¹⁰ SCE states that non-visitors also benefit from the education, research, and conservation activities that occur on the island.¹¹ SCE claims that the cross-subsidy amount per customer (26 cents per month) is small compared to the benefits that its electric customers receive from Catalina Island.¹²

SCE also states that the cross-subsidy does not violate Code Section 453, which prevents utilities from setting rates that "make or grant any preference or advantage to any corporation or person or subject any corporation or person to any prejudice or disadvantage."¹³ SCE claims that Section 453 only prevents unjust and unreasonable discrimination, and that the Commission has interpreted that such treatment must draw an unfair line or strike an unfair balance between similarly situated entities, and there must be no rational basis

⁷ *Id.* at 6-7.

⁸ SCE Limited Reply Brief at 1-3.

⁹ 2008 Cal.PUC Lexis 162, 192 Decision ((D.) 08-04-054), *Order Instituting Rulemaking to establish the California Institute for Climate Solutions*.

¹⁰ SCE Limited Opening Brief at 8.

¹¹ *Id.* at 8-10.

¹² *Id.* at 7.

¹³ Code Section 453.

for the different treatment for those similarly situated.¹⁴ SCE argues that the circumstances of water procurement on Catalina Island present a rational basis for different treatment of the two customer classes, and thus the proposed cross-subsidy in this unique instance is not unjust and not unreasonable.¹⁵

SCE also notes that the Commission, in D.14-10-048, previously approved the same cross-subsidy in the previous Catalina Water application. In that proceeding, parties such as TURN and the predecessor to Cal Advocates jointly approved of a settlement agreement that instituted the cross-subsidy.

For the foregoing reasons, SCE believes the Commission has the authority to approve the proposed cross-subsidy. SCE also notes that the Commission should limit its analysis here to whether it has the authority to approve the cross-subsidy, leaving the factual determinations and analysis regarding whether it should approve it, as proposed, to later in the proceeding.¹⁶

2.2. TURN Position

TURN contends that the proposed cross-subsidy is unreasonable and violates statute and Commission precedent. Firstly, TURN states that the Commission lacks the authority to approve the proposed cross-subsidy. TURN disputes SCE's claim regarding the settlement agreement in D.14-10-048, the previous Catalina Water GRC decision. TURN notes that the settlement agreement, which approved the cross-subsidy, was envisioned to be a one-time event, and not to be used going forward. The Commission, in past precedent, has interpreted Code Section 451 to preclude the assignment of costs to ratepayers of other industries. In D.97-05-088, the Commission declined to

¹⁴ SCE Limited Opening Brief at 11, citing D.10-04-054 at 7.

¹⁵ *Id.* at 11-12.

¹⁶ SCE Limited Reply Brief at 3-4.

approve a Pacific Gas and Electric Company's (PG&E) proposal to have ratepayers pay for property taxes, noting that "[a] utility cannot charge ratepayers costs that are unrelated to the provision of any product or commodity or service, and the Commission cannot lawfully order such charges."¹⁷ TURN also argues that Code Section 453 prevents SCE from giving a clear "preference or advantage" and that the cross-subsidy proposal clearly gives Catalina Water customers such a preference.¹⁸ TURN also argues that the water utility should receive treatment similar to that of a SCE affiliate, since it provides no benefit to electric ratepayers, and that the Commission has determined that utility affiliate costs should be assigned to the utility affiliates rather than being collected in regulated rates. Otherwise, ratepayers would be subsidizing these affiliate operations, and such costs would violate the principle that utilities should "only pass costs onto the regulated utility that the utility should bear pursuant to cost causative principles."¹⁹ TURN also notes that there is no precedent for a cross-subsidy between customers of different utility services (here, water and electric) for which the customer bases do not overlap.²⁰ TURN also notes that costs have continued to increase for electric ratepayers, and that such ratepayers continue to face affordability challenges, just as Catalina Water ratepayers do.²¹

TURN also disputes SCE's claim that a nexus exists between the water utility costs and the mainland electric customers. TURN states that the water utility cannot be treated as a "high-cost district" within SCE's electric service

¹⁷ TURN Limited Opening Brief at 3, citing D.97-05-088.

¹⁸ TURN Limited Opening Brief at 3-4.

¹⁹ TURN Limited Opening Brief at 4, citing D.04-09-061 at 158.

²⁰ TURN Limited Reply Brief at 2-4.

²¹ TURN Limited Opening Brief at 8.

operations, because it involves a completely different industry. TURN alleges that the Commission has never allowed a multi-district cross-subsidy when multiple utility service types are involved, and has in fact taken measures to ensure that such a thing not occur.²² TURN continues by noting that the tourism and education nexuses presented by SCE should be ignored, as the large bulk of electric customers do not set foot on Catalina Island, and these arguments could apply to locations throughout SCE's service territory, not just Catalina Island.²³

TURN also argues that a greater nexus exists between the costs and SCE's shareholders, and that if anyone other than Catalina Water ratepayers should pay these water costs it should be SCE's shareholders. These shareholders should bear the loss, as part of the risk of owning shares, and the impact to them would be small.²⁴

2.3. Cal Advocates Position

Cal Advocates agrees with TURN that the proposed cross-subsidy is unlawful. Cal Advocates argues that the Commission's rate design principles have highlighted the need for cost-causation, meaning that costs shall be paid by the customers that cause them, and that cross-subsidies should be avoided, unless they support explicit state policy goals.²⁵ Cal Advocates notes that SCE has in other proceedings noted the importance of following the principle of cost-causation.²⁶ The cross-subsidy in this proceeding would violate the principle by spreading the cost of service to a completely different industry and

²² *Id.* at 5.

²³ *Id.* at 9-10; TURN Limited Reply Brief at 5-6.

²⁴ *Id.* at 7-8.

²⁵ Cal Advocates Limited Opening Brief at 4.

²⁶ *Id.*, citing Exhibit SCE-01 at 13, A.17-06-030.

customer group, most of whom have not benefitted from Catalina Water.²⁷

Cal Advocates notes that the arguments for a nexus between SCE electric customers and Catalina Water costs are weak, as the tourism estimates are estimates and the educational and conservational benefits apply to everyone, not just SCE customers.²⁸

Cal Advocates also notes that the Commission, in the last Catalina Water GRC, explicitly stated that adoption of the settlement with a cross-subsidy did not permit SCE to “presume in any subsequent application that the Commission would deem the outcome adopted [in D.14-10-048] to be presumed reasonable and it must, therefore, fully justify every request and ratemaking proposal without reference to, or reliance on, the adoption of the settlement.”²⁹

2.4. Catalina Parties Position

The City of Avalon, et al., (Catalina Parties)³⁰ contend that the Commission has the authority to permit the proposed cross-subsidy, given the broad authority granted by Code Section 451.³¹ The Catalina Parties state that the Commission must conduct a factual analysis of the situation in order to determine whether proposed rates are reasonable or adequate. In conducting such analysis, the Catalina Parties recommend that the Commission consider the unique geographical nature of Catalina Island, SCE’s operational situation for the water utility, the extremely burdensome costs that would be levied onto Catalina

²⁷ *Id.* at 4-7.

²⁸ Cal Advocates Limited Reply Brief at 3-4.

²⁹ Cal Advocates Limited Reply Brief at 4, citing D.14-10-048, at 10.

³⁰ The City of Avalon, Catalina Island Chamber of Commerce, Santa Catalina Island Company, Santa Catalina Island Conservancy, Guided Discoveries, and Hamilton Cove Homeowners Association are participating in this proceeding as “Catalina Parties.”

³¹ Catalina Limited Parties Opening Brief at 5-8.

Water customers, as well as the potential burden on SCE customers. The Catalina Parties state that the policy goal of “providing adequate service at reasonable rates”³² supports the subsidy in this instance, given the unique circumstances on Catalina Island. The Catalina Parties, in particular, place heavy emphasis on the fact that Catalina Water is a unique operation under the SCE electric umbrella and should be treated as such.³³ The Catalina Parties also claim that precedent cited by TURN and Cal Advocates are not persuasive, given that the circumstances are not analogous.³⁴

2.5. Discussion

After reviewing briefs and arguments presented by the parties, we decline at this time to make a definitive ruling on the Commission’s authority to order the proposed cross-subsidy in this proceeding. Both SCE and the Catalina Parties argue that the Commission has broad authority to interpret and implement the Pub. Util. Code, including Sections 451 and 453. Code Section 451 requires that rates be “just and reasonable,” and historically the analysis of this has emphasized cost-causation principles.³⁵ “Rate designs must comply with a wide variety of laws designed to protect consumers, ensure reliability...and ensure safety.”³⁶ In considering electric rate design proposals, the Commission has previously considered the fact that “electricity is a basic necessity” and that “all residents of the state should be able to afford essential electricity.”³⁷ In

³² D. 15-07-001 at 1.

³³ Catalina Parties Limited Reply Brief at 10-11.

³⁴ Catalina Parties Limited Reply Brief at 7-8.

³⁵ D. 15-07-001 at 2.

³⁶ *Id.* at 26.

³⁷ *Id.* at 27, citing to AB 327.

recognition of this fact, the rate design principles allow the Commission to consider “explicit state policy goals” in determining whether a cross-subsidy is appropriate.³⁸ In this proceeding, the California Water Code requires that the residents of Catalina Island have access to “safe, clean, affordable, and accessible water...”³⁹ There arguably exists an explicit state policy goal in support of the cross-subsidy, in so far as it would allow the residents of Catalina Island access to affordable water.

However, other Commission policy and precedents to date require SCE to present additional evidence and information in this proceeding to show that the proposed cross-subsidy is reasonable here. SCE recognizes that cost-causation is an issue in this proceeding, and to address this, SCE presents novel nexus arguments, focusing on the tourism, educational, and conservation benefits of Catalina Island to SCE electric ratepayers.⁴⁰ The rate design principles emphasize the importance of cost-causation, and although cross-subsidies that do not strictly follow cost-causation principles may be considered, it is required that such subsidies “appropriately” support state policy goals.⁴¹ SCE must show that the proposed cross-subsidy is appropriate – a potentially difficult task, given that SCE does not dispute TURN’s allegation that there is no historical example for the Commission approving a cross-subsidy where the utility service provided in one district is different than the utility service in the other district.⁴² SCE’s reliance on the decision in the prior GRC approving the cross-subsidy via motion

³⁸ D.15-07-001 at 28.

³⁹ California Water Code Section 106.3(a).

⁴⁰ SCE Limited Opening Brief at 7-10.

⁴¹ D.15-07-001 at 28.

⁴² SCE Limited Reply Brief at 8.

for adoption of a settlement is also unfounded, given that it did not discuss the legal issues surrounding the cross-subsidy⁴³ and the explicit language in that decision noting it should not be relied upon going forward.⁴⁴

Moreover, Commission's Rule 12.5 specifically provides that a decision adopting a settlement agreement "does not constitute approval of, or precedent regarding, any principle or issue in the proceeding or in any future proceeding" unless that decision "expressly provides otherwise." Here, the prior GRC decision adopting the settlement agreement does not provide any language explicitly or implicitly that the decision should have a precedential effect.

Although this ruling does not rule out the cross-subsidy proposal at this time, it emphasizes the significant barriers to its approval. Given the uncertainty surrounding SCE's proposal to recover Catalina Water costs from SCE's mainland electric customers, and the unaffordable rate increases for Catalina Water customers in the other proposal,⁴⁵ SCE should devise and propose one or more additional alternatives to provide additional cost recovery options/methods. The alternative proposal(s) should enhance the record and provide the Commission with a reasonable range of options and increase the likelihood of approval of this Application.

All parties in this proceeding were also ordered to provide comment in this briefing to address Scoping Memo Issue 2Ci on other potential rate recovery alternatives to the two proposed by SCE.

⁴³ TURN Limited Opening Brief at 5, noting the word "subsidy" is not mentioned in the decision.

⁴⁴ D.14-10-048 at 10.

⁴⁵ Supplemental Testimony filed by Southern California Edison SCE-08, served February 26, 2021, at 11-21; *Id.* at 5-6.

TURN suggested consideration of a number of options, focusing mainly on a surcharge to be added onto tourism boats to Catalina Island.⁴⁶ SCE does not see the tourism boat surcharge by itself as a viable option,⁴⁷ nor does it see the other options as viable.⁴⁸

SCE presents the option of consolidating Catalina Water costs and rates with SCE electric expenses and rate bases,⁴⁹ however such a solution would not avoid the legal and policy issues that exist with the cross-subsidy option. As the applicant, it is SCE's responsibility to present cost recovery proposals that are just and reasonable.

3. Conclusion

We decline at this time to make a finding on the Commission's authority to approve the proposed cross-subsidy rate recovery proposal. However, SCE is directed to explore other options for rate recovery. By August 05, 2021, SCE shall file and serve its proposal(s) for one or more additional alternatives to provide additional cost recovery options/methods.

IT IS SO RULED.

Dated May 27, 2021, at San Francisco, California.

/s/ GARRETT TOY
Garrett Toy
Administrative Law Judge

⁴⁶ TURN Limited Opening Brief at 14-17.

⁴⁷ SCE Limited Opening Brief at 16-17.

⁴⁸ SCE Limited Reply Brief at 9-10.

⁴⁹ SCE Limited Opening Brief at 15-16.