IN THE SUPREME COURT OF THE STATE OF IDAHO

UNITED WATER IDAHO INC.

Appellant,

v.

IDAHO PUBLIC UTILITIES COMMISSION

Respondent,

SUPREME COURT
DOCKET NO. 32431

IPUC CASE NO. UWI-W-04-04

Supw-05-01

OPENING BRIEF OF UNITED WATER IDAHO INC., APPELLANT

APPEAL FROM THE IDAHO PUBLIC UTILITIES COMMISSION
Paul Kjellander, President, Presiding

Dean J. Miller (ISB No. 1968)
McDevitt & Miller LLP
420 West Bannock
P.O. Box 2564
Boise, ID 83702
Telephone: (208) 343-7500
Fax: (208) 336-6912

Attorneys for Appellant
United Water Idaho Inc.

Lawrence D. Wasden,
Attorney General

Donovan E. Walker
Deputy Attorney General
472 W. Washington St.
Boise, ID 83702-5983

Weldon B. Stutzman
Deputy Attorney General
472 W. Washington St.
Boise, ID 83702-5983

Attorneys for Respondent
Idaho Public Utilities Commission

TABLE OF CONTENTS

TABLE OF CASES AND AUTHORITIES

Cases

Statutes

Constitutions

STATEMENT OF THE CASE

Nature of the Case

This is an appeal from Orders of the Idaho Public Utilities Commission, ("Respondent," "Commission") determining the rates United Water Idaho Inc., ("United Water," "Appellant") is permitted to charge to its customers. As an appellate remedy United Water requests that the Orders of the Commission be set aside and that the matter be remanded to the Commission with instructions to: 1) re-calculate United Water's rate base and prospectively implement new rates to allow an adequate return on rate base; 2) calculate and implement a rate surcharge in such amount and in such duration as is adequate to recover United Water's losses since entry of the Orders.

Course of Proceedings

On November 30, 2004 United Water filed an Application with the Commission for authority to increase its rates and charges for water service. (R. Vol. I, Pgs. 2-23.) On December 2, 2004 the Commission suspended United Water's proposed schedule of rates and charges for a period of thirty (30) days plus five (5) months pursuant to Idaho Code 61-622. (R. Vol. I. p. 24.) Public hearings were held on May 24-26, 2005. After post-hearing briefs were filed the Commission, on June 24, 2005 suspended the United Water's proposed rates and charges for an additional (60) sixty days. (R. Vol. II, p. 159.) On August 3, 2005 the Commission issued Final Order No. 29838. (R. Vol. I. p. 163.) United Water, on August 23, 2005, filed a timely Petition for Reconsideration. (R. Vol. II, p. 207.) On September 20, 2005 the Commission issued its Final Order on Reconsideration, No. 28971, denying, for the most part, relief requested in the Petition for Reconsideration. (R. Vol. II, p. 262). Thereafter, United Water filed a timely Notice of Appeal. (R. Vol. II. 281).

The effect of the Commission's Orders was to authorize an increase in rates of approximately 8.08%, in contrast to United Water's requested increase of approximately 18%.

Statement of Facts

A. *Ratemaking in General.*

To properly put in context the issues presented in this case, a general description of the rate making process is appropriate. The theory behind the ratemaking process is related to the concept of the "regulatory compact." The Wyoming Supreme Court recently summarized the concept as follows:

> "The 'regulatory compact' provides the fundamental basis for utility regulation. In general, the compact is a theoretical agreement between the utilities and the state in which, as a quid pro quo for being granted a monopoly in a geographic area for the provision of a particular good or service, the utility is subject to regulation by the state to ensure that it is prudently investing its revenues in order to provide the best and most efficient service possible to the consumer. In exchange, the utility is allowed to earn a fair rate of return on its rate base." *PacifiCorp v. Public Service Commission of Wyo.*, 103 P.3d 862, 871 (2004).

The utility's entitlement to a fair rate of return is a constitutional right.

> "Rates which are not sufficient to yield a reasonable rate of return on the value of property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment. This is so well settled by numerous jurisdictions of this court that citation of the cases is scarcely necessary." *Intermountain Gas Co. v. Idaho Public Utilities Commission*, 97 Idaho 113, 125, 540 P. 775, 787 (1975) (quoting *Bluefield Waterworks & Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923).

While the process of setting utility rates is thought by some to be arcane—even mysterious—the basic steps in the process are straightforward.[1] The first step in setting rates a utility may charge its customers is to determine the "rate base" which consists generally of

[1] This description of the rate making process is adapted from the Court's summary of rate making procedures in *Intermountain Gas Co. v. Idaho Public Utilities Commission,* 97 Idaho, 113, 116-117, 540 P.2d 775 (1975).

capital invested by the utility upon which the utility is entitled to earn a fair return.[2] The two major components of rate base are net utility plant and working capital. Net utility plant consists of water plant in service less accumulated depreciation and less capital provided by others.[3]

Next, a fair overall rate of return is determined, that is, the cost of capital expressed as a percentage, applied to the rate base to determine the income, or return, the utility is entitled to earn. In this case United Water and the Commission Staff stipulated that the fair rate of return was 8.375% which amount was accepted by the Commission. This percentage, which is a combination of the cost of debt and the cost of equity based on the utility's capital structure, is multiplied by the dollar amount of the approved rate base to produce an allowed operating income. Expressed as a formula, allowed operating income is:

Allowed Operating Income = rate of return * rate base.

This figure is then compared to the adjusted actual net operating income of the utility for a one-year test period. The test year is a projection of future revenues and expenses based on historical data. *Industrial Customers of Idaho Power v. Idaho Public Utilities Commission*, 134 Idaho 285, 291, 1 P.3d 786, 792 (2000). "The assumption underlying fixing of future rates on historical data is that for future years changes in the revenue, expense, and rate base will vary proportionately so that the utility will receive a fair rate of return."

The deficiency in the net operating income is calculated by subtracting the test period adjusted net operating income from the Commission's allowable net operating income, which results from the application of the Commission's determined fair rate of return to the Commission's determined rate base. Finally, the Commission calculates the additional revenue

---

[2] "A utility's 'rate base' represents the original cost minus depreciation of all property justifiably used by the utility in providing services to its customers." *Citizens Utilities Co. v. Idaho Public Utilities Commission* 99 Idaho 164, 579 P.2d 110 (1978).

[3] This includes contributions made by customers in aid of construction, advances in aid of construction and accumulated deferred income taxes.

the company must collect to generate this additional net operating income from the utility business after payment of income taxes. This final calculation represents the utility's "revenue deficiency", that is, the additional revenue the Commission allows the utility to obtain by raising its rates. The total amount the utility is permitted to recover from customers is known as the "revenue requirement."

The utility does not receive a guarantee that it will actually recover its revenue requirement or earn its allowed return, as this will depend on factors such as actual sales volumes, fluctuations in costs of service, and efficiency of management in operating the business during the period rates are in effect. As will be seen, however, the Commission is obligated to set rates that give the utility a reasonable opportunity to earn its allowed return. If plant in service is excluded from the rate base, then the allowed rate of return when applied to this lower rate base will produce a lower level of earnings. In other words, the utility will not have the opportunity to earn the allowed rate of return on its invested capital.

B. *Determination of Rate Base*

Each of the steps in the rate making process, described generally above, involve numerous sub-steps. As discussed more fully below, the issues involved in this case revolve around the determination of rate base. As noted, rate base is generally defined as capital invested in utility plant. The rate base is further refined by excluding from rate base investments in plant which are not used and useful in service to the public, *See* Idaho Code 61-502A. Also excluded are investments which the Commission determines to be imprudent or excessive in amount. *See e.g. Washington Water Power v. Idaho Public Utilities Commission,* 101 Idaho 567, 617 P.2d 1242 (1980). In this case, there were no challenges to United Water's plant in service either on imprudence or used and useful grounds.

Rate base is further adjusted by adding to rate base those investments made after the test period that are "known and measurable." "Test year data should be adjusted for known and measurable changes where the changes are shown to be reliable and certain. The Commission should include in the rate base all items which are proven with reasonable certainty to be justifiably used by the utility in providing services to its customers." *Utah Power v. Idaho Public Utilities Commission,* 102 Idaho 282, 629 P.2d 678 (1981).

There are two alternative methods which the Commission has used for calculating rate base during the test period. The first is the "year end" method, which measures the level of investment at the end of the (12) twelve-month test period. The other is the "13 month average" method which averages the sums of the monthly investment balances during the test period: plant additions in the first month are included at their full value, and the value of additions in each succeeding month is reduced by one-thirteenth, cumulatively. For a utility, such as United Water, that is experiencing customer growth and is making investments to serve that growth, the "year-end" method will, appropriately, produce a larger rate base than will the "13 month average" method which, in practical effect, centers the investment at the middle of the test year. Investments at the last month of the averaging period are included only at one-thirteenth of their value.

The choice of methods, and the periods chosen for the determination of rate base, can produce dramatically different results. Here, United Water, as it had in each of its prior rate cases during the past ten years, proposed a "year end" method based on plant in service at the end of the test year, July 31, 2004, with known and measurable additions after the test period, producing a total rate base of $137,584,397[4]. In other words, under the Company's proposal,

[4] United Water's final proposed rate base was $140,148,049. In its Final Order the Commission made accounting adjustments to rate base totaling deductions from rate base of $2,563,652. These are not disputed on appeal.

every dollar of capital invested by the Company and providing service to customers at the time of the new rates, would earn a return unless excluded from rate base as imprudent or not used and useful. The Commission, departing from the "year end" method it had approved in United Water's prior rate cases, suddenly switched to a "13 month average" method resulting in a final rate base of $126,824,685. (R. Vol. 11, p. 279, L. 11.) As will be discussed in more detail, approximately one half of the difference between the two rate base amounts is due to averaging the investment during the test year; the other one half is attributable to including post test year known and measurable investment at only 1/13 of its actual value. These investments, which are not alleged to be imprudent or not used and useful, are excluded from the rate base. In consequence, United Water is denied a return on rate base investment that is admittedly used and useful in service to the public, totaling $10,755,712 ($137,584,397 – $126,828,685). The revenue produced by rates calculated on a "13 month average" rate base will produce a return on investment of approximately 7.7%, far below the return of 8.375% found to be the reasonable rate of return. (Tr. Vol. VI. p. 1039, L. 1-14.)

ISSUES PRESENTED ON APPEAL

1. Whether the rates established by the Commission are sufficient to allow United Water a reasonable opportunity to earn its allowed rate of return.

2. Whether the Court may require that a rate surcharge be imposed to recover losses occasioned by an invalid Commission Order.

ARGUMENT

A. While the Standard of Review of IPUC Decisions is Deferential, Decisions of the Commission Are Not Unimpeachable Or Beyond Review.

Appellant acknowledges that the legislature intended to grant the Commission broad leeway in respect to setting public utility rates. Idaho Code 61-629 provides:

> The review on appeal shall not be extended further than to determine whether the commission has regularly pursued its authority, including a determination of whether the order appealed from violates any right of the appellant under the constitution of the United States or of the state of Idaho.

The Court, on numerous occasions has interpreted this section as creating a deferential standard of review. *See e.g. Page Data v. Idaho Public Utilities Commission,* __Idaho__ 2006 Opinion No. 34 (2006) and cases cited therein.

Nonetheless, the leeway granted the Commission is not unlimited. It is bounded in the first instance by the requirement that meaningful judicial review exist so as to prevent an agency, in the name of technical expertise, escaping public control. In the very first appeal of a Commission decision, the Court held that meaningful opportunity for judicial review saved the Public Utilities Law from being an unconstitutional delegation of legislative power to an unaccountable agency. In *Idaho Power Co. v. Bloomquist* 26 Idaho 222, 256, 141 Pac. 1083 (1914), the Court said:

> "It [the Court] may decide whether the orders of the board are unlawful or whether they violate a right of the petitioner under the constitution of the United States or the state of Idaho, and whether the evidence is sufficient to sustain the findings and conclusions of the commission. It will thus be seen that this court is given ample power to review the orders of the commission and to correct any mistakes that may have been made."

More recently the Court, in a similar vein, has observed that meaningful judicial review is necessary to ensure that "administrative expertise" does not become a "monster which rules with no practical limit on its discretion." *Washington Water Power v. Idaho Public Utilities Commission,* 101 Idaho 567, 576, 617 P.2d 1412 (1980).

Commission discretion is also bounded, for example, by the requirement that rates be non-discriminatory. *See* Idaho Code 61-315; *Building Contractors Ass'n, v. Idaho Public Utilities Commission,* 128 Idaho 534, 916 P.2d 1259 (1996).

A further limitation, particularly relevant to this appeal, is that the Commission must set rates that are sufficient to allow the utility the opportunity to earn its allowed return.

> "Whenever the commission...shall find...that the rates charged by any public utility are insufficient...the commission *shall* determine the just, reasonable or sufficient rates." Idaho Code 61-502. (emphasis added).

Rates that produce a rate of return less than the rate of return found by the Commission to be fair, just and reasonable are "insufficient" as a matter of law. *Idaho Power Company v. Idaho Public Utilities Commission*, 99 Idaho 374 582 P.2d 720 (1978); *See Also, Utah Power& Light Company v. Idaho Public Utilities Commission,* 102 Idaho 282, 629 P.2d 678 (1981).

Additionally, the Commission's findings and conclusions must be supported by substantial evidence. As the Court explained in *Hayden Pines Water Company v. Idaho Public Utilities Commission,* 111 Idaho 331, 723 P.2d 875 (1986):

> "In the recent case of *Idaho State Insurance Fund v. Hunnicutt,* 110 Idaho 257, 715 P.2d 927 (1985), this Court described the appropriate test for substantial competent evidence as follows:
>
> In *Local 1494 of the International Association of Firefighters v. City of Coeur d'Alene,* 99 Idaho 630, 586 P.2d 1346 (1978), this Court discussed the test for determining what constitutes substantial evidence for the purposes of judicial review of an administrative agency's action. We observed:
>
> The "substantial evidence rule" is said to be a "middle position" which precludes a *de novo* hearing but which nonetheless requires a serious review which goes beyond the mere ascertainment of procedural regularity. *Id.* at 633, 586 P.2d at 1349.
>
> Such a review requires more than a mere "scintilla" of evidence in support of the agency's determination, *id.* at 634, 586 P.2d at 1350, though "something less than the weight of the evidence." *Consolo v. FMC,* 383 U.S. 607, 620 [86 S.Ct. 1018, 1026, 16 L.Ed.2d 131] (1966). "Put simply," we wrote, "the substantial [competent] evidence rule requires a court to determine 'whether [the agency's] findings of fact are reasonable.' 4 Davis, Administrative Law Text § 29.01-02 at 525-530." *Local 1494, supra,* 99 Idaho at 634, 586 P.2d at 1350. . . .
>
> In deciding whether the agency's findings of fact were reasonable, reviewing courts should not "read only one side of the case and, if they find any evidence there," sustain the administrative action and ignore the record to the contrary." *Universal Camera [Corp. v. N.L.R.B.], supra,* 340 U.S. [474] at 481 [71 S.Ct. 456

This rule applies with particular force, when, as here, Commission findings have been challenged by petition for reconsideration:

> "Although in almost any rate case a requirement of findings so detailed that the same would proximate evidentiary findings would be unduly burdensome, we agree with Idaho Power that after the Commission's ruling is challenged on certain major items by the requisite petition for rehearing, then findings of fact based in substantially greater detail are required in order for this Court to properly conduct its appellate function." *Washington Water Power, supra; Boise Water, supra; Oregon Short Line, supra.* Moreover, the Commission must also set forth its reasoning in a rational manner." *Idaho Power Company v. Idaho Public Utilities Commission,* 108 Idaho 943, 703 P.2d 707 (1985.

Finally, when, as here, the commission changes regulatory methods it must provide a reasoned explanation for the change:

> "If, however, the IPUC decides a case in a manner contrary to prior IPUC rulings the Court will consider whether the IPUC has adequately explained the departure from prior rulings so that a reviewing court can determine that the decisions are not arbitrary and capricious." *Rosebud Enterprises v. Idaho Public Utilities Commission,* 129 Idaho 609, 917 P.2d 766 (1996).

B. The Effect of the Commission's Orders is to Unlawfully Deny United Water the Opportunity to Earn a Reasonable Return on Prudently Invested Capital

As established at hearing, the total of United Water's investment in rate base was $140,148,049 (Tr. Vol. VI. p. 855, L. 16.). No party contended that any part of the investment was imprudent or not used and useful in service to the public. As noted, the Commission made other adjustments, unrelated to the 13-month averaging, to rate base totaling $2,563,652 which are not contested on appeal. Accordingly, for purpose of this appeal, rate base is $137,584,397.

The Commission further found, based on the Stipulation between United Water and the Commission Staff, that a reasonable return on invested capital was 8.375%. (R. Vol. II, p. 164).

Accordingly, United Water's allowed return, or operating income, equals $11,522,693 ($ 137,584,397 x 8.375%).

Based, however, on the Commission approved rate base of $126,824,685 (R. Vol. II. p. 279 L. 11), the allowed return, is $10,621,567 (126,824,685 x 8.375%).

Allowed operating income of $10,621,567 produces a return on invested capital of 7.7% ($10,621,567 /$137,584,397). This produces an earnings deficiency of $901,126 ($11,522,693 – $10,621,567). Applying the Commission-approved gross-up factor for taxes of 1.683 the total revenue deficiency is $1,516,595.

It is thus a mathematical certainty that revenues allowed are insufficient to provide United Water the opportunity to earn the return of 8.375% which the Commission found to be the reasonable return on invested capital.

This court has held that rates which produce revenues that will not allow the utility the opportunity to earn the return found to be just and reasonable are insufficient within the meaning of Idaho Code 61-502. For example, in *Idaho Power Company v. Idaho Public Utilities Commission,* 99 Idaho 374, 582 P.2d 720 (1978), the Commission found that a rate of return of 8.23% was fair, just and reasonable. The Commission, however, improperly deducted certain items from rate base which had the effect of producing revenues sufficient to provide a return of only 8.09%. Because the return actually allowed was less than that found to be fair, just and reasonable, the Commission's order was set aside. "Orders based on findings by the IPUC that are not supported by the evidence must be set aside on appeal." 99 Idaho at 381.

A similar case is *Hayden Pines Water Company v. Idaho Public Utilities Commission,* 122 Idaho 356, 834 P.2d 873 (1992). There, the Commission required the utility to employ and accountant at an annual cost of $15,000, but did not allow corresponding revenue to cover the expense. Thus, by definition the allowed revenues would be insufficient to produce the allowed

return. On appeal, the Court set aside the Commission order, finding that the rates which produced the short-fall in revenues were unjust and unreasonable[5].

For other cases holding that while a utility is not guaranteed recovery of a particular rate of return but that rates must be sufficient to provide an opportunity to earn the allowed return, see *Utah Power & Light v. Idaho Public Utilities Commission,* 102 Idaho 282, 629 P.2d 678 (1981); *Citizens Utilities v. Idaho Public Utilities Commission,* 99 Idaho 164, 579 P2d 110 (1978); *Washington Water Power v. Idaho Public Utilities Commission,* 105 Idaho 276, 668 P.2d 1007 (1983).

C. Rates That Are Insufficient As A Matter of Statutory Law Are Confiscatory As A Matter of Constitutional Law.

As discussed above, the Commission is obligated by statute to set rates that are "sufficient" to allow the utility the opportunity to earn its allowed return on all prudently invested capital. Idaho Code 61-502.

Rates that are insufficient in the statutory sense suffer another potentially more serious defect—they are confiscatory in the constitutional sense. The rule is well established:

> "Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment. This is so well settled by numerous decisions of this court that citation of cases is scarcely necessary." *Bluefield Waterworks & Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679, 690, 67 L.Ed. 1176 (1923).

Rates that offend the Fourteenth Amendment to the United States Constitution are likewise prohibited by Art. 1, secs. 13 and 14 of the Idaho state constitution. *Capital Water Co. v. Public Utilities Commission of Idaho*, 44 Idaho 1, 262 P. 863 (1926); *Intermountain Gas Co. v. Idaho Public Utilities Commission*, 97 Idaho 113, 540 P.2d 775 (1975).

---

[5] *Hayden Pines* is discussed further in the next section of this brief, where it will be seen that the statutory concept of "insufficiently" is equivalent to the constitutional concept of confiscation.

In contrast to *Intermountain Gas*, the present case does not involve a claim that the rate of return allowed by the Commission was too low. The parties stipulated to the reasonable return. Rather, it involves a claim that the rates set will not produce revenues sufficient to allow an opportunity to earn the return found to be reasonable, because the stipulated rate of return was applied to a rate base which was arbitrarily reduced. The present case is similar to *Hayden Pines*, discussed above, in which the utility was forced to incur an expense without an allowance for corresponding revenue to cover the expense, making it impossible for the utility to earn its allowed return. This was found to be confiscatory:

> "Hayden asserts that it was an unconstitutional taking of Hayden's private property for the PUC to require Hayden to perform certain accounting functions without considering the cost of these accounting functions in reducing Hayden's rates. We agree.
>
> It was unjust and unreasonable for the PUC to direct Hayden to employ an accountant and then to refuse to consider the expense of doing so in determining Hayden's rates. Presnell testified that the expense would be $15,000 a year. The PUC acknowledged that no one disputed the accuracy of this estimate. The PUC just refused to consider the $15,000 expense until Hayden filed a new rate case, using a test year in which it had actually paid the accounting expense." 122 Idaho at 360.

D. If The End Result Of The Commission's Decision Is Unreasonable, Appellate Inquiry Is At Its End.

On several occasions the Court has observed that the focus of appellate review of rate making orders is on the end result, not on methods employed to reach the result.

> "Our purpose is not to analyze each step of the rate-setting process to determine whether the regulatory agency was correct in its decision, but to look at the overall effect of the rate fixed to determine whether the return to the utility is reasonable and just." *Agricultural Products Corporation v. Utah Power and Light,* 98 Idaho 23, 27, 557 P.2d 617 (1976); *See also, Intermountain Gas Co. v. Idaho Public Utilities Commission* 97 Idaho 113, 120, 540 P.2d 775 (1975).

The preceding sections of the brief establish that the end result is unreasonable because the rates established are insufficient to allow the opportunity to earn the allowed return. That should end the inquiry.

Nonetheless, there are cases where, notwithstanding the language of *Agricultural Products* and *Intermountain Gas*, the court has examined the methods employed to reach the end result. *See e.g. Idaho Power Company v. Idaho Public Utilities Commission, supra.* To the extent analysis of the underlying methods is thought necessary, United Water, in the following two sections of this brief demonstrates the fallacy of reasoning and insufficiency of evidence to support the end result.

E. Computation Of United Water's Test Year Rate Base Using a 13-Month Average Method Was Arbitrary And Not Supported By Evidence.

As previously discussed, United Water in this case proposed, and the Commission accepted, a twelve month test year ending July 31, 2004. (R. Vol. II, p. 165). United Water further proposed that its rate base be calculated as of the test year end, adjusted for known and measurable changes. This was consistent with the method approved by the Commission in each of United Water's preceding four rate cases, dating back to 1993. (Tr. Vol. VI. p. 1028 L. 1-5). In the 1993 case, the Commission explained the rationale for a year end rate base as follows:

> "A year-end test calculation of rate base for a utility experience rapid growth is, in this case, a more accurate reflection of that utility's investment in plant. In light of the foregoing and the absence of objection, we find a year-end calculation of rate base for Boise Water is fair, just and reasonable." (IPUC Order No. 25640, R. Vol. 1. p. 130).

Despite the long settled method of calculating rate base, and a solid rationale supporting it, the Commission suddenly changed to an average rate base calculation. United Water first had notice of the intended change upon receipt of Staff's pre-filed testimony only a few weeks before hearing. (Tr. Vol. VI. p. 967 L. 14). By averaging a test year that is already historical, only one-

thirteenth of projects in service in July 2004, over one year before the new rates became effective (August 25), are recovered under the new rates. Even projects placed in service in October 2003, almost two years before the rates became effective are not fully recovered under the Commission's averaging methodology.

United Water's Vice President succinctly explained the unfairness associated with the sudden change in methodology:

> "These water plant investments that are in service and providing benefits to customers will not be included in the earnings base, for no good reason other than a change in regulatory methodology. Twelve million dollars of investment actually made in plant that is used and useful is effectively vaporized in this case, simply by changing the ratemaking rules." (Tr. Vol. VI. p. 967 L. 6-11).

While the Commission is not rigidly bound by the doctrine of *stare decis*, when it changes regulatory course, it must provide a reasoned explanation for the change sufficient for the Court to determine that the change was not arbitrary. *Rosebud Enterprises v. Idaho Public Utilities Commission,* 129 Idaho 609, 917 P.2d 766 (1996). An agency action is arbitrary if it was done "...in disregard of the facts and circumstances presented or without adequate determining principles." *American Lung Association of Idaho v. State of Idaho, Department of Agriculture,* ___Idaho___, ___P.3rd___, 06.6. ISCR 261 (2006). An arbitrary act would occur "...if a ratemaking body were to make opportunistic changes in rate setting methodologies just to minimize return on capital investment in a utility enterprise." *Verizon Communications Inc., v. FCC* 535 U.S. 467, 152 Led.2d701,747 (2002).

The Commission's primary, ostensible, rationale for the change in regulatory methodology was to eliminate any mismatch between investment, revenue and expense. (Order on Reconsideration No. 29871, R. Vol. II. P. 264). This carried forward a concern expressed by the Commission in the preceding Idaho Power and Avista rate cases that investments made late

in the test year, or in the post-test year period, might have the effect of producing additional revenue or reducing operating expenses which, if unaccounted for, might result in rates which collected more than the utility's cost of service. In the Commission's Final Order in the Idaho Power case, the Commission advised utilities: "Generally speaking, the Commission expects all utilities to identify expense saving and revenue producing effects when proposing rate base adjustments for major plan additions." (Idaho Power Final Order No. 29505, R. Vol. I. P. 129).

Importantly, the Commission did not put utilities on notice that a 13 month average method must be employed or that it was the only solution to the perceived mismatch problem—it only advised utilities that some adjustment was required to take into account revenue increasing or expense reducing effects of late period investments.

United Water acknowledges in principle that a correct matching of investment revenue and expense is a legitimate regulatory goal—if properly done it provides an assurance that the resulting rates will be sufficient to produce the allowed return but will not produce revenues in excess of the utility's cost of service.

The question presented here is not the legitimacy of the regulatory goal but whether the change in methods to accomplish the goal is reasonably related to its achievement. *See Rosebud Enterprises, supra.* As demonstrated below, it is not.

In order to comply with the guidance provided in the *Idaho Power* and *Avista* orders, United Water added annualized customer growth revenue at current rates to the company's base revenues for all customers anticipated to be added to the entire system from the test year through May 31, 2005. This method matches the higher level of end of period May 31, 2005 revenues with the higher level of rate base as of the same date. (Tr. Vol. I. P. 19. L 1-23).

In contrast, the Commission failed to properly match the 13 month average rate base with corresponding revenues. The Commission used the same level of annualized revenues, those for the period ending May 31, 2005, that were contained in the United Water's filing. To be consistent with the 13-month average method, the May 31, 2005 annualized revenues should have been reduced back to the actual test year revenues centered at January 2004.

This method of treating investment and expense as adopted by the Commission was identical to that proposed by the Commission Staff. In rebuttal testimony, United Water's expert witness, Dr. Dennis Pesseau[6] demonstrated the fallacy of the staff approach, as ultimately adopted by the Commission:

> Q. Has, in fact, Staff failed to properly match its proposed thirteen-month expense and rate base estimates with corresponding revenues?
>
> A. Yes. This can be demonstrated by determining that Staff used essentially the same level of annualized revenues, those for the period ending May 31, 2005 that are contained in the Company's filing. In following its suggestion to use the thirteen-month average rate base, Staff should also have reduced the May 31, 2005 annualized revenues in the Company's filing back to the actual test year revenues centered at January, 2004. But Staff did not. The test year revenues used by Staff are actually the very same test year revenues developed by the Company for its end of period method, with one very small exception. On Company Exhibit 8, Page 2 of 2, proposed test year revenues are $31,534,832. To verify that Staff's case calculates annualized revenues identically to the end of period May 31, 2005 calculated by the Company, I refer to Staff Exhibit 126. On this Exhibit (column (6) line (12)) appears the same annualized revenue levels of $31,534,832. In other words, Staff mismatches rate base and expenses on a thirteen-month average basis, with a higher level of revenues calculated on a forward annualized period May 31, 2005. Thus there is a gross mismatch.
>
> Contrastingly, the Company's filing is consistent, in that it matches the higher level of end of period May 31, 2005 revenues with its end of period expenses and rate base. Staff on the other hand, mismatches these components by using the smaller than actual rate base, its thirteen month average, with the higher level of end of period revenues. This is a mismatch that eventually guarantees an under recovery of revenues

[6] Dr. Pesseau, an independent consultant, is a Ph.D economist who has conducted economic and financial studies for regulated industries for more than 30 years. (Tr. Vol. I. P. 289).

> sufficient to earn the allowed rate of return. (Tr. Vol. IV. P. 1301, L.31—P. 1032 L. 2).

While deference might ordinarily be due to Commission discretion in technical matters such as revenue matching, it does not require great technical expertise to comprehend the error of the Commission's chosen method. It "disregard[s] the facts and circumstances presented [and is] without adequate determining principles." *American Lung Association, supra.*

In addition to the matching rationale, the Commission offered other, secondary explanations for the switch in methodologies. They, too, are unpersuasive. In its Final Order No. 29838, the Commission offered two reasons for the change: that in the prior cases use of the year-end method was uncontested and that recent decisions by the Commission in other cases should have alerted United Water to the Commission's preference for an average methodology:

> "In the Company's rate cases since 1993, the year-end methodology was approved only because no party objected or proposed a different methodology. That history, along with United Water's review of the Commission's final Orders in the recent Idaho Power and Avista cases, provided the Company with adequate notice of the Commission's preference for the average rate base methodology." (Tr. Vol. II. p. 168).

The first reason—that use of the year end method in prior cases was uncontested—is not a reason at all. Whether or not use of a regulatory method is contested, the Commission is still obligated to independently determine that the rates produced by the method are fair, just and reasonable. Idaho Code 61-502.

Nor does the second articulated reason—recent use of an averaging methodology in other cases—offer reasoned support for the switch in methodologies. In the other cases, Idaho Power Case No. IPC-E-03-13 and Avista Case No. AVU-04-01[7] the utility in its initial filing proposed

[7] Final Order Nos. 29505 (IPCo) and 29602 (AVU) can be viewed at: http://www.puc.idaho.gov/internet/cases/elec/IPC/IPCE0313/ordnotc/20040525FINAL%20ORDER%20NO%2029505.PDF and

use of an average rate base, and had been using that approach in previous cases. Moreover, Order Numbers 29505 (IPCo) and 29602 (AVU) advised utilities that when proposing test year additions to rate base a corresponding revenue and expense matching adjustment should be made. Neither order declared that all utilities must use an average rate base method or that the average rate base method was the only or necessary solution to a perceived mismatching problem.

In its Final Order On Reconsideration, Order No. 29871, the Commission attempted to shore-up its rationale but, as will be seen, without success.

First, the Commission attempted to avoid the obvious problems with a switch in methodology by claiming it was not really a switch. "The Commission's rate base methodology in this case thus is not "departing from the year-end method" so much as it is returning United Water's rate cases to what had been established Commission practice." (Vol. II p. 264). Courts are suspicious of agencies that attempt to create a "Humpty Dumpty world" by turning the facts on their head. *See State of New York v. EPA,* ___F4th____ Slip Opinion, 03-1380 March 17, 2006 p. 14, (D. C. Cir. 2006).

Next, the Commission relied on decisions of this Court in *Utah Power & Light Company v. Idaho Public Utilities Commission,* 105 Idaho 822, 673 P.2d 422 (1983) and *Citizen's Utilities Company v. Idaho Public Utilities Commission*, 99 Idaho 164, 5792d 110 (1978), which, on the surface, approved use of a average methodology. *Utah Power* and *Citizens*, however, undermine the Commission's decision more than they shore it up. In both cases the Court found use of the average methodology, as it was applied, was permissible because it did not result in

---

http://www.puc.idaho.gov/internet/cases/elec/AVU/AVUE0401/ordnotc/20041008FINAL%20ORDER%20NO%2029602.PDF

impairment of the utility's ability to earn a reasonable return—which, as has been demonstrated, is precisely the defect of the averaging methodology as applied to United Water.

F. Including Post-Test Year Investment at 1/13 Of its Actual Value Was Arbitrary And Not Supported By Evidence

The second component of the Commission's averaging methodology was the treatment of investment that was made after the test year but that was known and measurable at the time of hearing. Post test year investment was treated as if it had been made in July, 2004, the last month of the test year which had the effect of including post test year investment at 1/13 of its actual value, resulting in $7,541,724 of investment in used and useful plant being excluded from rate base and the denial of a return on that investment as illustrated by this calculation:

Total Post Test Year Investment (excluding CWTP):	$8,170,201
Post Test Year Investment Allowed:	$ 628,477
Post Test Year Investment Excluded:	$7,541,724
Earnings Shortfall at 8.357%	$ 630,262
Incremental Tax Multiplier	1.683[8]
Revenue Requirement Deficiency:	$1,060,730

The Court has held that post-test year investment that is known and measurable should be included in rate base. In *Citizens Utilities v. Idaho Public Utilities Commission, supra,* the Court explained:

> "The Commission should include in the rate base all items which are proven with reasonable certainty to be justifiably used in providing services. There are two good reasons for including these items in the rate base; first, to avoid a rate base which does not adequately demonstrate real revenue needs and second, to reduce the necessity of a future application to adjust the rate base to represent additional investments. The decision of the Commission on this particular item is error. The cost of the billing machine should have been included in the rate base." 99 Idaho at 171. *See Also Utah Power v. Idaho Public Utilities Commission,* 107 Idaho 47, 685 P.2d 276 (1984); *Agricultural Products v. Utah Power & Light,* 98 Idaho 23, 557 P.2d 617 (1976).

[8] R. Exhibits Vol. II Staff Revised Exhibit 110, L. 19.

In neither its Final Order No. 29838 nor Final Order on Reconsideration No. 29871 did the Commission offer an explanation for disregarding the clear mandate of *Citizens Utilities*. In this case, the impact is even more egregious in that even plant in service during the historical test year is only included at a fraction of its cost.

To the extent the inclusion of post test year investment at 1/13 of its true cost is aimed at solving the problem of mismatched revenue and expense, it cannot conceivably be true that the revenue producing or expense reducing effects of the new investment are of such a magnitude that 92% of the investment should be disallowed. As with the treatment of test year investment, the treatment of post-test year investment adopted by the Commission was based on the Staff recommendation. Dr. Pesseau explained the error of the recommendation:

> Q. Is the end result of the Staff proposal out of proportion with the end result of adjustments recently made by the Commission in other cases to take into account revenue producing, expense reducing effects?
>
> A. Yes it is. In the recently concluded Avista rate case, the Commission, with some reluctance, employed a variant of a proxy approach developed in the preceding Idaho Power Company rate case. (*See* Order No. 29602, pgs 16-17). This resulted in approximately 12% of post test year investment being excluded. Without debating the merits of the adjustment methodology in *Avista* it is obvious that Staff's proposal in this case produces an end result totally disproportionate to the end result believed to be reasonable by the Commission in *Avista*. (R. Vol. VI. P. P. 1041 L. 1—11.)

Based on the foregoing discussion it is apparent that the Commission's change in rate base methodology was arbitrary. The objective observer is left with the abiding impression that it was "an opportunistic change in rate setting methodology just to minimize return on capital investment in a utility enterprise." *Verizon Communications v. FCC, supra.*

G. Remedy

As demonstrated above, the effect of the Commission's Orders is to unlawfully deny United Water the opportunity to earn its reasonable, allowed return. Therefore, United Water

seeks an order remanding the matter to the Commission with instructions to recalculate United Water's rate base in accordance with the Court's opinion and prospectively implement rates to permit recovery of the reasonable return on rate base. In addition, The Court should instruct the Commission to calculate and implement a rate surcharge in such amount and such duration as will recover United Water's losses from the date of Order No. 29871 through the entry of a new order.

1. The Supreme Court Has the Authority to Order a Surcharge.

It might initially be thought that the case of *Utah Power v. Idaho Public Utilities Commission,* 107 Idaho 47, 685 P.2d 276 (1984) is an impediment to a Court-mandated surcharge. There, the utility applied to the Commission for a surcharge to recover losses it suffered when a previous rate award was determined to be confiscatory by the Supreme Court. The Commission held it did not have authority to grant a surcharge, and on appeal the Court agreed.

Utah Power, however, did not consider the question presented here—whether as part of affording meaningful appellate relief the Court may mandate a surcharge. As will be seen, there is nothing in *Utah Power* that precludes this appellate relief.

The Supreme Court has the authority to order a surcharge for United Water to remedy the confiscatory loss resulting from the Commission's unconstitutional and invalid order. Pursuant to the Idaho Constitution, the Supreme Court has jurisdiction to review, upon appeal, any order of the public utilities commission. Idaho Constitution Article V, Section 9. In addition, "the legislature may provide conditions of appeal, scope of appeal, and procedure on appeal from orders of the public utilities commission." *Id.* However, the legislature lacks the authority to

completely eliminate the Court's authority to order a remedy.[9] Instead, the Idaho Constitution vests the Court with the authority to issue "all writs necessary or proper to the complete exercise of its appellate jurisdiction." Art. V, sec 9.

2. A Court-Ordered Surcharge Is Consistent with the *Utah Power* Decision.

Under current Idaho case law, the Comission lacks the authority to grant a surcharge to recover past losses caused by an invalid order which has been set aside on appeal. *See Utah Power & Light Co. v. Idaho Public Utilities Commission*, 107 Idaho 47, 685 P.2d 276 (1984) ("*Utah Power*"). However, this limitation in authority based on the Idaho Public Utilities Law does not apply to the Supreme Court.

In the *Utah Power* case, the Supreme Court had previously set aside a Commission order that resulted in an artificially low rate base. *Id.* at 278. Utah Power & Light (UP&L) then filed a petition for hearing with the Commission requesting that the Commission modify its previous order and grant UP&L a surcharge to cover the deficiency created by the order. *Id.* The Commission determined that it did not have the authority to implement such a surcharge stating, in part, "We are a regulatory Commission, not a court of law, and have no authority to award damages except as given to us by statute." *Id.*

On appeal, the Supreme Court affirmed the Commission's decision determining that the Commission lacked the authority to grant a surcharge to recover lost revenue resulting from an order later deemed invalid. The *Utah Power* decision rests on two rationales: (1) the surcharge was deemed retroactive ratemaking, which was considered outside the scope of the Commission's powers; (2) the stay and bond procedures set out in I.C. §§ 61-635 through 61-637

[9] Similarly, "the legislature [is] without the power to significantly limit or eliminate causes of action based on constitutional claims." *Osmunson v. State*, 135 Idaho 292, 295, 17 P.3d 236, 239 (2000) (citing *Olsen v. J.A. Freeman Co.*, 117 Idaho 706, 717-719, 791 P.2d 1285, 1296-1298 (1990)).

are the exclusive remedy for recovering from the Commission the revenues lost during appeal. As further demonstrated below, both rationales are based on the limited scope of the Commission's authority and, therefore, do not limit the remedies which may be prescribed by to the Court.

The so-called rule against retroactive ratemaking derives from two sources—one structural and one statutory. Neither, it will be demonstrated, is applicable to the judicial branch. The structural limitation on Commission authority is that, as an agency exercising legislative powers delegated to it by the legislature, the Commission may only act prospectively. *Id, at 107 Idaho 49.* This basis for the rule, obviously, is not a constraint on the judicial branch.

The statutory basis for the rule is that the Commission is bound by Idaho Code § 61-502 to act in a prospective manner only. Idaho Code § 61-502 provides that the Commission "shall determine the just, reasonable or sufficient rates ... to be *thereafter* observed." (Emphasis added). "[I]t does not give the PUC authority to prescribe surcharges or reductions to otherwise reasonable rates in order to make up past revenue shortfalls due to confiscatory rates." *Id.* at 107 Idaho 52. As with the first basis of the rule against retroactive ratemaking, this statutory constraint on the Commission is not a limitation on the power of the judiciary.

Courts of other jurisdictions that have considered the question have concluded that a judicially mandated rate adjustment resulting for statutorily authorized review of a Commission's order does not constitute retroactive rate making. *See: Pennwalt Corp v. Michigan Pub. Serv. Comm'n*, 311N.W.2d 423, 425, (Mich. Ct. App. 1981); *State* v. *Conservation Council of N.C.* 312 N.C. 59, 320 S.E.2d 679, 686 (1984); *Southwestern Bell v. Public Utilities of Texas* 615 S.W.2d (Tex. Civ. App. 1981); *Mountain States Tel. & Tel. v. Arizona Corp. Comm'n* 604 P.2d 1144 (Ariz. Ct. App. 1979); *Mountain States Tel. & Tel. v.*

Public Util Comm'n 502P2d 945, 949 (Colo. 1972); *Williams v. Washington Metro Area Transit Comm'n* 415 F.2d 922 (D.C. Cir. 1968) *(en banc); Southern California Edison v. Public Utilities Commission,* 144 Cal.Rptr.905 (Cal. 1978); *In re Commission Investigation into 1997 Earnings of U.S. West Communications, Inc.,* 127 N.M. 254 980 P.2d 37 (N.M. 1999).[10]

The second rationale in the *Utah Power* was that the stay and bond procedures are the exclusive means the Commission has to remedy an invalid Commission order. I.C. § 61-635 provides that an appeal from a Commission decision does not automatically stay operation of the Commission's order; however, during the pendency of the appeal, the Supreme Court may stay or suspend the operations of a Commission's order.[11] Pursuant to I.C. § 61-635, such an order requires at least three days notice, a hearing, and a finding that great or irreparable damage would otherwise result.[12] The order staying or suspending the Commission's order will not be effective until the appellant posts a bond pursuant to I.C. § 61-637 in an amount sufficient to cover the all damages resulting from the delay in enforcing the Commission decision.[13]

---

[10] Many of these cases involved the ability of the court to order refunds for rates found to be too high, not surcharges for rates that were too low, but the principle is the same.

[11] I.C. § 61-635 states:

> The pendency of an appeal shall not of itself stay or suspend the operation of the order of the commission, but during the pendency of such appeal, the Supreme Court may stay or suspend, in whole or in part, the operation of the commission's order.

[12] I.C. § 61-636 states:

> No order so staying or suspending an order or decision of the commission shall be made by the court otherwise than upon a three (3) days' notice and after hearing, and if the order or decision of the commission is suspended, the order suspending the same shall contain a specific finding based upon the evidence submitted to the court and identified by reference thereto, that great or irreparable damage would otherwise result to the petitioner and specifying the nature of the damage.

[13] I.C. § 61-637 states:

> In case the order or decision of the commission is stayed or suspended, the order of the court shall not become effective until a suspending bond shall first have been executed and filed with, and approved by the commission (or approved on review by the court), payable to the people of the state of Idaho, and sufficient in amount and security to insure

In determining that the stay and bond procedures were the exclusive means of obtaining relief from the Commission for an invalid Commission order, the *Utah Power* decision states, "the Public Utilities Law itself neither provides nor suggests any alternatives" to the stay and bond procedures and "[i]t has been firmly established that the PUC has no authority not given it by statute." *Id.* at 52, 685 P.2d 281.

As demonstrated above, the *Utah* Power decision rests on the concept that the Commission's authority is limited by statute. The difference between the instant case and the *Utah Power* decision is that United Water has not brought its proposed remedy to the Commission. Instead, United Water seeks a court-ordered remedy from the Supreme Court, and the Supreme Court is not limited by the statutory authority cited in support of the *Utah Power* decision.

3. If the Court Determines that *Utah Power* Bars a Surcharge, then the *Utah Power* Decision Should be Overturned.

If this Court should determine that the *Utah Power* decision somehow limits the Court's ability to fashion a remedy to address the interim harm caused United Water by the PUC's decision, then United Water respectfully requests that this court reevaluate and overturn the *Utah*

---

the prompt payment, by the party petitioning for the review, of all damages caused by the delay in the enforcement of the order or decision of the commission, and of all moneys which any person or corporation may be compelled to pay, pending the review proceedings, for transportation, transmission, product, commodity, or service in excess of the charges fixed by the order or decision of the commission, in case said order or decision is sustained. The court, in case it stays or suspends the order or decision of the commission in any matter affecting rates, fares, tolls, rentals, charges or classifications, shall also by order direct the public utility affected to pay into court, from time to time, there to be impounded until the final decision of the case or into some bank or trust company paying interest on deposits, under such conditions as the court may prescribe, all sums of money which it may collect from any corporation or person in excess of the sum such corporation or person would have been compelled to pay if the order or decision of the commission had not been stayed or suspended.

Power decision. This Court has recently articulated the standard to be applied when considering whether to overturn prior decisions as follows:

> When there is controlling precedent on questions of Idaho law "the rule of stare decisis dictates that we follow it, unless it is manifestly wrong, unless it has proven over time to be unjust or unwise, or unless overruling it is necessary to vindicate plain, obvious principles of law and remedy continued injustice." *Houghland Farms, Inc.* v. Johnson, 119 Idaho 72, 77, 803 P.2d 978, 983 (1990). While it is important that parties and their counsel have predictability regarding the law so that they may make informed decisions in the conduct of their affairs, when the judicial interpretation of a statute is manifestly wrong, stare decisis does not require that we continue an incorrect reading of the statute. "We have stated frequently that we will not follow prior incorrect decisions merely because the cases exist. The rule to stand by decided cases and to maintain former adjudications contemplates more than blindly following a former decision even if it is manifestly wrong." *Sherwood v. Carter*, 119 Idaho 246, 256, 805 P.2d 452, 462 (1991).

Greenough v. Farm Bureau Insurance, ___Idaho___, 2006 Opinion 20, February 27, 2006.

Applying this standard to the *Utah Power* decision, it is clear that the *Utah Power* decision should be overturned as it is manifestly wrong and overruling it is necessary to vindicate legal principles and remedy continued injustice.

a. The *Utah Power* Decision Rests on a Flawed Interpretation of Idaho's Public Utility Law.

The *Utah Power* decision was decided by a divided court. The vigorous dissents authored by Justices Shepard and Bakes persuasively argue that the majority misinterpreted the stay and bond procedures set forth in I.C. §§ 61-635 through 61-637. Justice Shepard wrote:

> The essence of the majority opinion is that, since Utah Power & Light did not follow procedural niceties which, for the first time in today's ruling, are deemed the exclusive avenue to avoid confiscation, the utility must suffer the loss. Even assuming that such argument is worthy of consideration in view of constitutional restraints, the majority's opinion is nevertheless seriously flawed. I.C. § 61-635 is, by its express language, permissive rather than mandatory, and despite the linguistic legerdemain of the majority, the word 'may' in that statute cannot somehow miraculously be turned into "must."

Utah Power, 107 Idaho at 58, 685 P.2d 287. Justice Bakes similarly described:

> The Court holds that if Utah Power & Light fails to post such a bond pending appeal, then even though the utility's property has been effectively confiscated there is no hope of recovery because of the failure to file such an appeal bond. By denying the utility a right to impose a surcharge, the majority makes the filing of a bond mandatory. This Court-imposed requirement of a mandatory bond pending appeal is ... contrary to the statute, which uses the permissive word 'may', not the mandatory word 'shall'....

Id. at 59, 685 P.2d 288.

The Court's conclusion that the stay and bond remedy is exclusive is not only inconsistent with the plain language of the statutory text, it also has the potential to lead to unconstitutional results. Because the Court's authority to grant the stay is optional, the Court could deny the stay, even though the order is later deemed invalid. If this invalid order set confiscatory rates, then the appellant has no remedy to address the constitutional deprivation. In addition to resting on a flawed interpretation of the stay and bond procedures, the majority decision in *Utah Power* is also based on a flawed analysis of the rule against retroactive ratemaking.

The rule against retroactive ratemaking, as indicated in the *Utah* Power decision, is based on the prospective nature of rates. *See, also, Popowsky v. Pennsylvania Public utility commission*, 642 A.2d 648, 651 (Pa.Cmwlth. 1994). "The rule against retroactive ratemaking prohibits a public utility commission from setting future rates to allow a utility to recoup past losses or to refund consumers excess utility profits." *Id.* One of the reasons for the rule against retroactive ratemaking is "the general principle that those customers who use power should pay for its production rather than requiring future ratepayers to pay for past use." *Id.* Another reason for the rule is consumer's right to rely on rates set by the commission. *Matanuska Elec. Ass'n, Inc. v. Chugach Elec. Ass'n, Inc.*, 53 P.3d 578, 583 (Alaska 2002).

Nonetheless, the rule against retroactive ratemaking does "not require that each and every act of the commission operate solely in futuro...." *Southern Cal. Edison v. Public Utilities Commission*, 144 Cal.Rptr. 905, 906 (Cal. 1978). Rather, the rule is "limited to the act of promulgating 'general rates.'" *Id.* Because a surcharge designed to recoup losses resulting from an invalid order does not result from or otherwise entail a general rate case, the rule against retroactive ratemaking does not apply. *See In re Commission Investigation into 1997 Earnings of U.S. West Communications, Inc.*, 127 N.M. 254, 980 P.2d 37 (N.M. 1999) (holding that Commission did not violate rule against retroactive ratemaking by ordering interim rate reduction to account for company's overearning).

As demonstrated above, the *Utah Power* decision is manifestly wrong. It is contrary to the plain language of the Public Utility Law and applies the rule against retroactive ratemaking in an inapproriate context. Moreover, as demonstrated below, the *Utah Power* decision leads to unconstitutional and unjust results.

b. The *Utah Power* Decision Leads to Unjust and Unconstitutional Results.

As described above, the *Utah Power* decision, based on an erroneous interpretation of the stay and bond procedures, leads to the possibility that a utility may be left without a remedy for constitutional injury. In addition, to the extent the decision is interpreted in a manner that would deprive the utility from seeking a court-ordered remedy, such as a surcharge, to recover the revenues wrongfully withheld, the decision sets forth an interpretation of Public Utility Law that violates due process and separation of powers principles.

Once the Court determines that a rate is confiscatory under the due process clause, the utility must have a guaranteed means of recovering the lost revenues associated with that

unconstitutional rate. Without a guaranteed remedy, the utility, and its shareholders, simply absorb the violation. Such a result cannot stand; the utility must be made whole.

In addition, to the extent the *Utah Power* decision is interpreted in a manner that would prevent the judiciary from fashioning a remedy to address constitutional violations, the decision violates principles of separation of powers.

As demonstrated above, the *Utah Power* decision is based on the limited statutory authority of the Commission. This statutory authority cannot be interpreted to limit the powers of this Court remedy the damage caused by an unconstitutional rate order. To do so would give the legislature unconstitutional authority over the judiciary.

The separation of powers principles is set forth in the Idaho Constitution, Article II § 1: "The powers of the government of this state are divided into three distinct departments, the legislative, executive and judicial; and no person or collection of persons charged with the exercise of powers properly belonging to one of these departments shall exercise any powers properly belonging to either of the others, except as in this constitution expressly directed or permitted." While the different branches of government serve as checks and balances of one another, they cannot usurp the unique functions of other branches.

The legislature, in exercising its authority to make laws, may limit the remedies available for statutory or common law violations. *Kirkland v. Blaine County Med. Ctr.*, 134 Idaho 464, 4 P.3d 1115 (2000). This authority is connected to the legislature's authority to limit or even eliminate statutory or common law rights of action. *Id.* However, "the legislature [is] without the power to significantly limit or eliminate causes of action based on constitutional claims." *Osmunson v. State*, 135 Idaho 292, 295, 17 P.3d 236, 239 (2000) (citing *Olsen v. J.A. Freeman Co.*, 117 Idaho 706, 717-719, 791 P.2d 1285, 1296-1298 (1990)). Thus, the legislature may not

limit the remedy available for constitutional wrongs. Determining constitutional rights and remedies is the unique province of the judiciary. Thus, the Public Utility Law cannot be read in a manner that would prevent United Water from recovering the revenues unlawfully withheld as a result of the confiscatory rates.

In conclusion, if this Court determines that the Commission has set rates unreasonably low, resulting in an unconstitutional confiscation of property, there must be a means to recover the revenues that have been deprived as a result of the Order. The Idaho Supreme Court has stated that the Commission lacks the authority to remedy the constitutional violation. Without recourse at the Commission, United Water now seeks a remedy addressing constitutional wrong from the Court. If the Court does not grant such a surcharge, the result will "give perpetual legal effect to an unlawful order, and ... unnecessarily and unwarrantedly penalize [the utility], its investors, and indeed its customers for the passage of time necessitated by appellate review of that unlawful order." *Potomac Elec. Power Co. v. Public Service Commission*, 380 A.2d at 149.

CONCLUSION

Based on the reasons and authority cited herein Appellants respectfully requests that Order Number 29871 be set aside and that the matter be remanded to the Commission with instructions to: 1) re-calculate United Water's rate base in accordance with the Court's opinion and prospectively implement rates to permit recovery of the reasonable return on rate base; 2) calculate and implement a rate surcharge in such amount and such duration was will recover United Water's losses from the date of Order No. 29871 through the entry of the new order described above.

DATED this 12 day of April, 2006.

Dean J. Miller

Attorneys for United Water Idaho, Inc.

CERTIFICATE OF SERVICE

Pursuant to I.A.R. 34(d) the undersigned certifies that two copies of the foregoing Opening Brief of United Water Idaho Inc., Appellant was served by hand-delivery upon:

Weldon B. Stutzman
Donovan E. Walter
Deputies Attorney General
472 W. Washington
Boise, Idaho 83702

This 17 day of April, 2006