

Investigation of South Duchesne Culinary Water, Inc.'s Compliance with Applicable Administrative Rules and Tariff

DOCKET NO. 18-2372-01  
ORDER TO FILE A GENERAL RATE CASE

ISSUED: February 20, 2020

## **1. BACKGROUND**

### **a. The September Order.**

On September 4, 2019, the Public Service Commission (PSC) issued an order in Docket No. 18-2372-01 (“September Order”), addressing numerous allegations that South Duchesne Culinary Water Inc. (SDCW) violated applicable provisions of administrative rule and tariff. The September Order found SDCW had committed no new violations with respect to numerous allegations the Division of Public Utilities (DPU) had raised “save for SDCW’s [alleged] failure to charge its owners and their development company the rates and fees the utility charged similarly situated customers.” (Order at 12.) On this issue, the PSC reserved making final findings and conclusions pending additional information and evidence.

#### **i. The PSC’s Findings Regarding Alleged Water Quality Violation.**

Because the DPU has submitted information that raises new concerns about SDCW’s water quality (*see infra* at 7-8), the PSC summarizes briefly here its findings and conclusions relating to an alleged water quality violation the PSC addressed in the September Order.

Among the violations the PSC declined to find in the September Order was the DPU’s contention SDCW had violated Utah Admin. Code R746-330-2 [hereafter “PSC’s Water Quality Rule”], which provides in pertinent part that water must be “free from disease-producing organisms and injurious chemical or physical substances” under the standards of the Utah

Drinking Water Board. The DPU introduced an administrative order and letter from the Department of Environmental Quality, Division of Drinking Water (“DDW”), showing that SDCW’s water system was in a “Not Approved” status owing to SDCW’s failure to maintain the required pressure (20 psi) in its system and its failure to comply with specific notice requirements.

Emphasizing that “SDCW’s issues with DDW [were] significant and must be redressed to the DDW’s satisfaction,” the PSC saw “little to be gained through the PSC’s duplicative enforcement of matters within the DDW’s purview.”<sup>1</sup> (September Order at 9.) The PSC noted the record showed SDCW had entered into a corrective action plan with DDW and that the “PSC is not well poised to interpret or apply regulations within the [DDW’s] purview.” (*Id.*) For its part, SDCW maintained that “at all times during the pendency of this matter, the sampling and testing of the SDCW water has met the purity standards required by the [S]tate, and SDCW has not violated [the PSC’s Water Quality Rule].” (*Id.*)

“The PSC conclude[d] that DDW’s enforcement actions, while certainly serious, [did] not raise allegations that SDCW’s water [was] disagreeable to ‘sight and smell’ or contain[ed]

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<sup>1</sup> The PSC noted the requirement to maintain the specified pressure arose out of a section of the administrative code subtitled “Minimum Water Pressure” within a subsection entitled “General Responsibilities of Public Water Systems.” Whereas the PSC’s Water Quality Rule relates exclusively to water that is disagreeable to sight and smell or contains injurious substances. In other words, the PSC understood another state agency to be charged with ensuring water companies’ systems comply with the laws’ technical specifications and engineering requirements. The PSC’s rule only applied in situations where a utility’s system produced water of insufficient quality.

‘disease-producing organisms’ or other ‘injurious chemical or physical substances.’” (*Id.*)

Accordingly, on the evidence presented, the PSC could not find SDCW had violated the PSC’s Water Quality Rule.

- ii. The PSC’s Directive to Provide Additional Information Concerning SDCW’s Failure to Charge Its Owners and Their Development Company.

As noted above, the PSC reserved making findings and conclusions in the September Order pertaining to SDCW’s alleged failure to charge its owners and their development company (collectively, the “Owners”) the rates applicable to any other similarly situated customer. The PSC observed “[o]n the facts presented, strong reasons exist to conclude SDCW has been, for many years, offering [the Owners] preferential, discriminatory service in violation of Utah Code Ann. § 54-3-8.” (*Id.* at 11.) However, SDCW argued the Owners had contributed financial resources that exceeded the amount of benefit they received as a result of not being charged in the manner of a similarly situated customer. (*Id.*) SDCW further argued it was “unaware of anything that would [not] allow that type of a quid pro quo to go on.” (*Id.*)

Noting that SDCW had “presented no documentation nor accounting to support [the existence of] such an arrangement,” the PSC nevertheless expressed interest in hearing additional evidence on the matter prior to making findings and conclusions. (*Id.*)

Consequently, the PSC ordered SDCW to file a report with the PSC by November 1, 2019, addressing (i) whether “SDCW’s failure to charge [the Owners] affect[ed] the rates SDCW charged its paying customers, and if so, what was the impact”; and (ii) whether “SDCW [is] adequately capitalized, and what effect, if any, has SDCW’s failure to charge [the Owners] had on SDCW’s finances.” (*Id.* at 12-13.) The Order directed SDCW to provide financial data and

explanations to support its conclusions. Finally, the Order directed the DPU to file a response to SDCW's report by December 6, 2019, including "what, if any, remedy it recommends the PSC institute to address any issues associated with SDCW's failure to charge [the Owners]." (*Id.* at 13.)

**b. SDCW'S Report.**

On October 31, 2019, SDCW filed its Report with the PSC ("SDCW's Report") as the September Order required.

SDCW represents its tariff was issued on August 14, 2003, establishing fees that "have never been increased." (SDCW's Report at 2.) SDCW's Report represents it selected its initial rates because they were equivalent to the rates the neighboring City of Duchesne charged at the time. (*Id.* at 3.) SDCW also represents it was "unaware of any documents from the 2003 time period that identify how its revenue requirement was originally estimated to establish the rates identified in the tariff." (*Id.*)

Generally, SDCW maintains the Owners contributed sums to SDCW in excess of the value they received from SDCW's failure to charge them otherwise applicable fees. SDCW includes estimates "of what the revenue requirement estimates might have looked like back in the 2003 time period" under numerous scenarios (varying based on the number of connected as opposed to standby lots).<sup>2</sup> (*Id.* at 4.)

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<sup>2</sup> SDCW represents the developer initially intended to develop 900 lots that could be connected to SDCW's water system. (SDCW's Report at 4.) However, owing to financial difficulties stemming, at least in part, from issues with the Utah State Tax Commission, the developer sold off much of the land and reduced the potential number of lots to 607. (*Id.* at 5.)

SDCW represents its “collections are sufficient to operate and maintain the water system [but] they are not currently generating a material return to the owners of the utility.” (*Id.* at 6.)

With respect to SDCW’s capitalization, SDCW represents it “is unaware of any standard for what constitutes ‘adequate capitalization.’” (*Id.*) SDCW “believes it is revenue adequate and has attempted to maintain a reserve balance equal to about two months of operating expenses.” (*Id.*)

**c. The DPU’s Recommendation to Reinstate Suspended Portion of Penalty and to Order SDCW to File a General Rate Case in 2020.**

After requesting and receiving an extension to file a response, the DPU filed its Comments on SDCW’s Report on December 13, 2019 (“DPU’s Recommendation”), noting inadequacies in SDCW’s Report and a lack of corroborating documents. The DPU recommended the PSC reinstate the suspended portion of the penalty (“Suspended Penalty”) the PSC ordered in the consolidated order it issued on February 13, 2018 in two prior dockets.<sup>3</sup> The DPU further recommended the PSC order SDCW to file a general rate case in 2020.

As a preliminary matter, the DPU notes that many regulated water companies “are subsidized by the developer whose development is supported by the water company” and that

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<sup>3</sup> On February 13, 2018, the PSC issued a consolidated order in *Formal Complaint of Tanya and Nick Olsen*, Docket No. 17-2372-01 and *Formal Complaint of Shane Houskeeper*, Docket No. 17-2372-02 (collectively, the “Complaint Dockets”), imposing a penalty of \$20,250 in connection with SDCW’s violation of numerous regulations and tariff provisions. On April 3, 2018, the PSC issued a Consolidated Order on Petition for Redetermination suspending 70 percent of the \$20,250 penalty, but providing “[i]f the PSC finds, in an order following an adjudicative process, an additional violation in [the next three years], the PSC [would] lift the penalty’s partial suspension and impose the full penalty in addition to any penalty associated with the new violation.”

such “subsidies, as well as all initial infrastructure paid for by the developer, are properly recorded as Contribution in Aid of Construction (CIAC).” (DPU’s Recommendation at 2.) The DPU asserts generally such “assets are donated by the developer to the water company free and clear of any obligation to the water company,” noting it “can be in a developer’s best interest to subsidize the water company.”<sup>4</sup> (*Id.*)

Further, the DPU notes that while SDCW’s Report states the Owners “estimate that they contributed more than \$31,000 each year,” SDCW’s Report contains no documentation to support these estimates.

- i. The DPU Argues SDCW’s Failure to Charge the Owners Had a Significant Negative Impact on Customers, Expressing Concerns about SDCW’s Capitalization and Financial Viability, and Recommending the PSC Order SDCW to File a General Rate Case.

Though the DPU “acknowledges that the rates [SDCW] charged [its] paying customers have stayed the same throughout SDCW’s business tenure,” the DPU believes SDCW’s failure to charge the Owners has had a significant negative impact on SDCW’s finances. The DPU explains that SDCW has taken on significant debt, potentially owing to inadequate revenues that in turn stem from its failure to charge the Owners. The DPU alleges SDCW’s accounting records are so inadequate, it cannot discern whether any of the debt stems from the Owners’ alleged subsidies or other obligations. However, the DPU argues “[r]egardless of the source of the debt, the proper collection of water bills from the [Owners] can and should reduce this debt.” (*Id.* at 5.)

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<sup>4</sup> For example, the DPU offers that developer subsidization may keep water rates low and thereby encourage “sale of lots based, in part, on cheap water rates.” (DPU’s Recommendation at 2.)

Without divulging information submitted in the confidential version of the DPU's Recommendation, the DPU represents "[i]t appears that SDCW is not adequately capitalized and SDCW's failure to charge [the Owners] has [had] a negative effect on SDCW's finances." (DPU's Recommendation at 9.) According to the DPU, SDCW "has negative equity, no cash, no reserves for the replacement of infrastructure when the time comes, and [a significant] debt." (*Id.* at 10.)

The DPU asserts that even "[u]sing the current population of customers," SDCW "is not earning enough to pay all operating costs, pay taxes, and provide a reserve to recover the original cost for infrastructure replacement." (*Id.* at 9.) The DPU argues the "likely result [will be] more under-spending or increasing rates, or both." (*Id.*)

The DPU "recommends the [PSC] order SDCW to file a general rate case during the calendar year 2020 to determine what the rates should be for SDCW to be a viable water company for its customers, and to define the amount of owner/developer contributions, if any." (*Id.* at 10.)

- ii. The DPU Raises New Evidence Relating to SDCW's Water Quality Issues and Recommends the PSC Reinstate the Suspended Penalty.

The DPU's Recommendation contains additional allegations pertaining to SDCW's violation of the PSC's Water Quality Rule. Specifically, the DPU represents it has been in communication with a representative of DDW who has provided documents pertaining to DDW's ongoing compliance efforts with respect to SDCW. Among the documents the DPU has obtained are several laboratory reports showing coliform bacteria detected in samples drawn from SDCW's water system, which the DPU attached as a confidential exhibit to its filing. The

DPU also attached a “boil order” it asserts the DDW issued to SDCW on November 8, 2019, instructing customers to boil water before using it in order to kill bacteria and other organisms that may be in the water.

In light of this apparent violation and SDCW’s unlawful failure to charge the Owners, the DPU recommends the PSC reinstate the Suspended Penalty.

## **2. FINDINGS, CONCLUSIONS, AND ORDER**

The Legislature has granted the PSC general jurisdiction over and the power to regulate public utilities. *See* Utah Code Ann. § 54-4-1. While the PSC does not often compel general rate cases, the Legislature has expressly empowered us to investigate the rates that a public utility is charging and, after opportunity for hearing, establish new rates. Utah Code Ann. § 54-4-4(2). The PSC must initiate such a proceeding on a finding that the rates a utility charges are unjust, unreasonable, discriminatory, preferential, “otherwise in violation of any provisions of law” or “insufficient.” *Id.* at § 54-4-4(1)(a). Whenever the PSC makes such a finding, the PSC “shall: determine the just, reasonable, or sufficient rates” and “fix” the rates accordingly. *Id.* at § 54-4-4(1)(b).<sup>5</sup>

### **a. The PSC Orders SDCW to File a General Rate Case on or before Thursday, October 1, 2020.**

Based on the entirety of the record in this docket, including the hearing the PSC held on July 18, 2019 and the parties’ filings prior to and subsequent to the hearing, the PSC finds and

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<sup>5</sup> Similarly, the Legislature has empowered the PSC, at its discretion, to “investigate ... one or more rates ... or practices of any public utility” and to “establish, after hearing, new rates ... [or] practices ... in lieu of them.” Utah Code Ann. § 54-4-4(2). This is consistent with the PSC’s relatively broad authority to conduct investigations under Utah Code Ann. § 54-4-2.



concludes SDCW's practice of failing to charge the Owners is preferential and discriminatory. Although the record remains unclear as to precisely how detrimental SDCW's preferential treatment was to the utility and its customers, the information the DPU presented strongly suggests the practice led to SDCW's under-collection of revenues, potentially causing it to incur otherwise avoidable debt and to be undercapitalized. These conditions could have significant rate impacts for customers and raise concerns about the viability and reliability of the service SDCW provides them.

Additionally, the PSC finds SDCW's rates, which have no discernible relationship to its revenue requirement and appear to provide an inadequate revenue stream, are unreasonable and likely insufficient. SDCW flatly states it selected the rates simply because they matched those of the City of Duchesne in 2003. We conclude a utility charging rates based solely on a neighboring municipal utility's benchmark from approximately 17 years ago is unreasonable. Moreover, based on the DPU's best estimates with currently available information, the DPU asserts SDCW "is not earning enough to pay all operating costs, pay taxes, and provide a reserve to recover the original cost for infrastructure replacement." (DPU's Recommendation at 9.)

In light of these findings, the PSC concludes a general rate case is necessary to establish rates that are just and reasonable and will support reliable and stable operation of the utility. The PSC directs SDCW to file a general rate case on or before **Thursday, October 1, 2020**. SDCW shall include in the filing all information necessary to constitute a complete filing pursuant to Utah Admin. Code R746-700-50 and R746-700-51. In so doing, SDCW shall comply with Utah Admin. Code R746-700-1 and R746-700-10, though SDCW need not file a notice of intent under R746-700-1(B).

The PSC is mindful that SDCW is a small, family-owned company and that preparation of rate case materials is cumbersome. The PSC encourages SDCW to retain whatever expertise it requires, including but not necessarily limited to a qualified accountant, to assist in the filing's preparation. The PSC also encourages the DPU to provide guidance to the extent SDCW seeks its assistance.

**b. The PSC Will Hear Additional Evidence and Make Findings and Conclusions Regarding SDCW's Alleged Violation of the PSC's Water Quality Rule, the Appropriate Penalty for SDCW's Charging Preferential Rates, and Reinstatement of the Suspended Penalty in the General Rate Case.**

The DPU's Recommendation introduces new and concerning information relating to SDCW's alleged violation of the PSC's Water Quality Rule, but SDCW has not had an opportunity to rebut or address it. SDCW must be given an opportunity to be heard on the new allegations and evidence. Additionally, as the DDW is currently taking corrective action to address the issue, the PSC concludes the most efficient course is for the PSC to examine these allegations in conjunction with the general rate case the PSC has ordered SDCW to file in this order.

At this juncture, the record clearly shows that SDCW failed, for many years, to charge the Owners rates applicable to any other similarly situated customer. Accordingly, the PSC finds and concludes SDCW violated Utah Code Ann. § 54-3-8, which prohibits utilities from charging preferential rates. However, the PSC finds the record is inadequate for the PSC to determine the appropriate penalty. The PSC sought additional information from the parties on this issue in its September Order, prompting the DPU to recommend a general rate case. At present, the record remains uncertain and undeveloped on the ramifications of SDCW's violation. We conclude the

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PSC will be better able to assess an appropriate penalty for SDCW's violation of § 54-3-8 with the benefit of a full record in the general rate case.

With respect to the DPU's recommendation that the PSC reinstate the Suspended Penalty, we similarly conclude this is a determination we will be better positioned to make at the conclusion of the general rate case. For now, the public interest is best served by SDCW committing all of its available resources to resolving its water quality problems and preparing an accurate and thorough filing for the rate case.

DATED at Salt Lake City, Utah, February 20, 2020.

/s/ Michael J. Hammer  
Presiding Officer

Approved and Confirmed February 20, 2020, as the Order of the Public Service Commission of Utah.

/s/ Thad LeVar, Chair

/s/ David R. Clark, Commissioner

/s/ Jordan A. White, Commissioner

Attest:

/s/ Gary L. Widerburg  
PSC Secretary  
DW#312169

Notice of Opportunity for Agency Review or Rehearing

Pursuant to Utah Code Ann. §§ 63G-4-301 and 54-7-15, a party may seek agency review or rehearing of this written order by filing a request for review or rehearing with the PSC within 30 days after the issuance of the order. Responses to a request for agency review or rehearing must be filed within 15 days of the filing of the request for review or rehearing. If the PSC fails to grant a request for review or rehearing within 20 days after the filing of a request for review or rehearing, it is deemed denied. Judicial review of the PSC's final agency action may be obtained by filing a Petition for Review with the Utah Supreme Court within 30 days after final agency action. Any Petition for Review must comply with the requirements of Utah Code Ann. §§ 63G-4-401, 63G-4-403, and the Utah Rules of Appellate Procedure.

CERTIFICATE OF SERVICE

I CERTIFY that on February 20, 2020, a true and correct copy of the foregoing was served upon the following as indicated below:

By Email:

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