

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

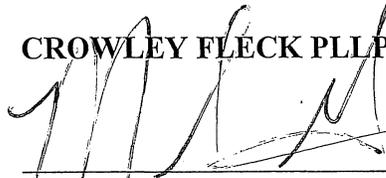
IN THE MATTER OF the Joint Application ) REGULATORY DIVISION  
of Liberty Utilities Co., Liberty WWH, Inc., )  
Western Water Holdings, LLC, and Mountain ) DOCKET NO. D2014.12.99  
Water Company for Approval of a Sale and )  
Transfer of Stock )

**Liberty Utilities Co. and Liberty WWH, Inc.'s Responses to  
Data Requests PSC-001 through PSC-027.**

Liberty Utilities Co. ("Liberty Utilities") and Liberty WWH, Inc. ("Liberty WWH" and collectively "Liberty"), by and through its undersigned counsel, hereby submits to the Montana Public Service Commission ("Commission") these responses to the first set of data requests from the Montana Public Service Commission.

Submitted this 17th day of February, 2015.

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**ATTORNEYS FOR LIBERTY UTILITIES CO.  
AND LIBERTY WWH, INC.**

PSC-001

Re: Organizational Chart

Witness: Unknown

- a. Please explain the indirect wholly-owned subsidiary relationship between Liberty Utilities and Algonquin including all companies.

**Response:** Algonquin Power & Utilities Corp. (“APUC”) is a publically traded, Canada corporation. APUC owns 100% of the issued and outstanding common shares of Liberty Utilities (Canada) Corp., a Canada corporation, which owns all of the issued and outstanding common shares of Liberty Utilities (America) Ventures, Inc., a Delaware corporation, which owns all of the issued and outstanding common shares of Liberty Utilities (America) Co., a Delaware corporation, which owns all of the issued and outstanding common shares of Liberty Utilities (America) Holdco Inc., a Delaware corporation, which owns all of the issued and outstanding shares of Liberty Utilities Co., a Delaware corporation, which owns the utility subsidiaries.

- b. Please provide the organizational chart for Algonquin through Liberty Utilities.

**Response:** See Liberty-Algonquin organizational chart attached as Attachment PSC-001 (LIB-A).

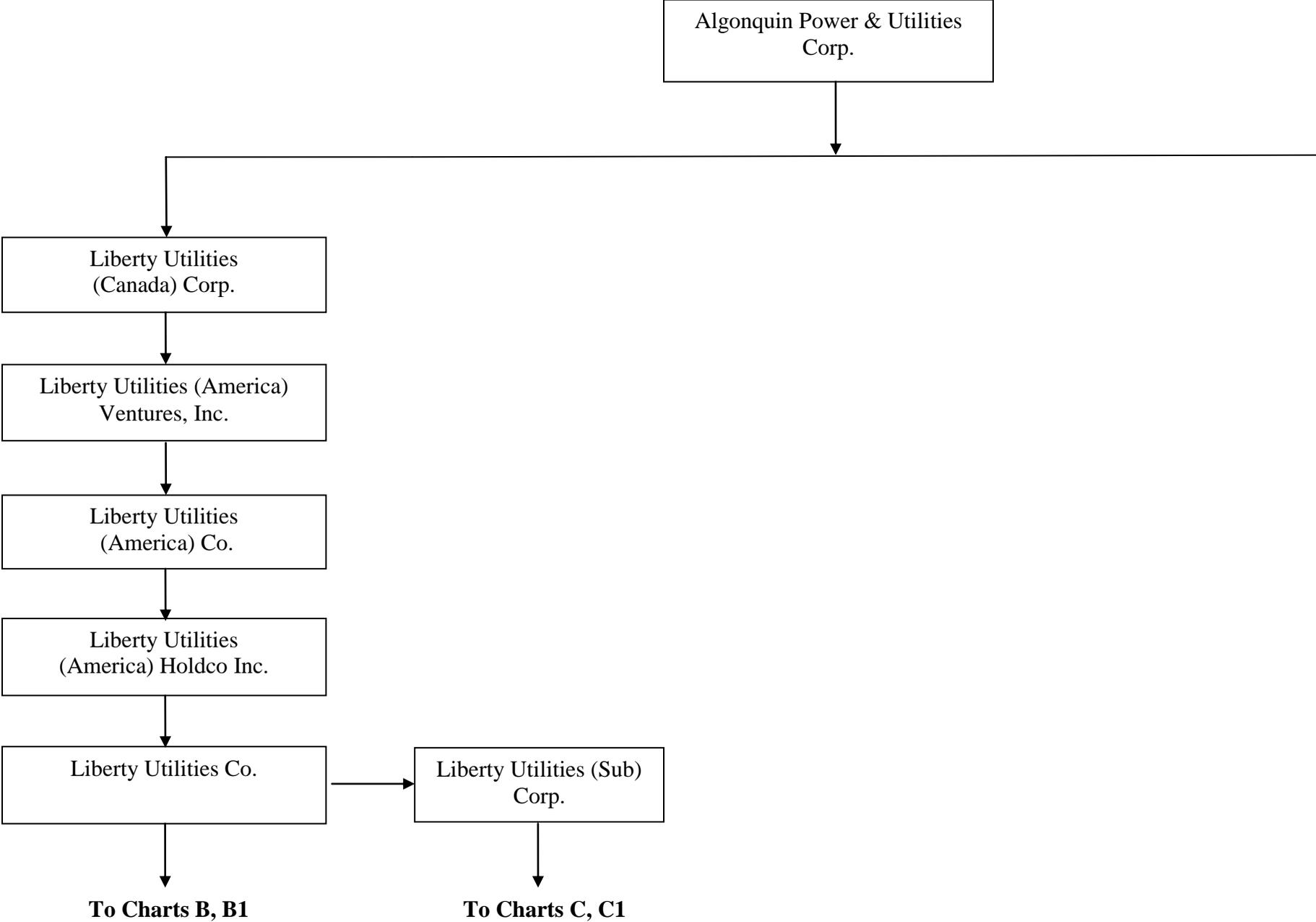
Response No. PSC-001  
Attachment PSC-001 (LIB-A)

**LIBERTY UTILITIES  
ORGANIZATION CHART  
AS OF FEBRUARY 4, 2015**

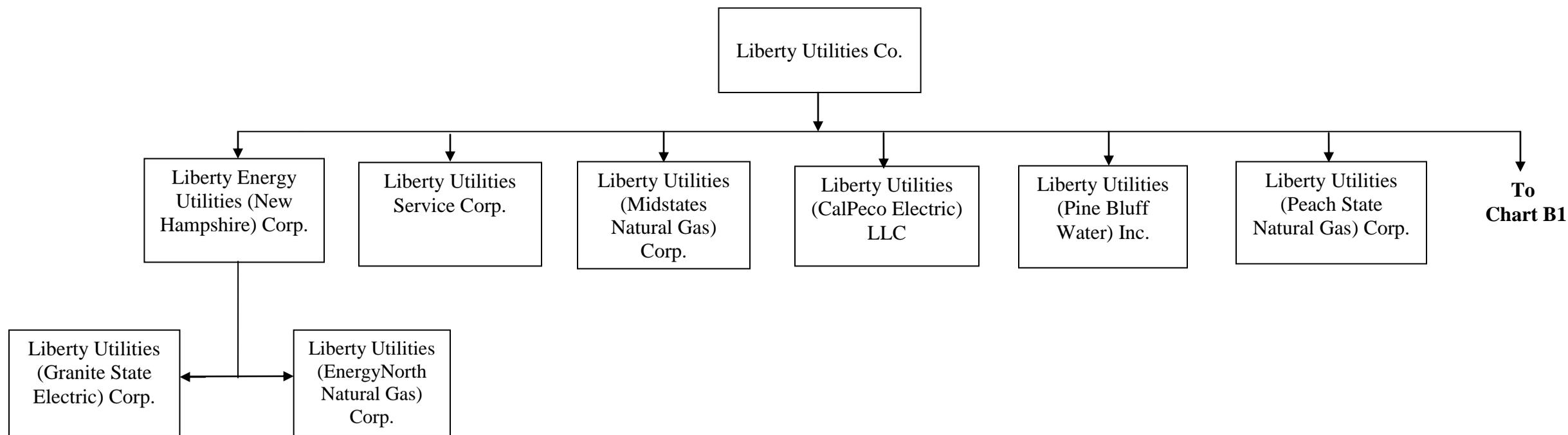
**KEY**

1. Corporation or LLC

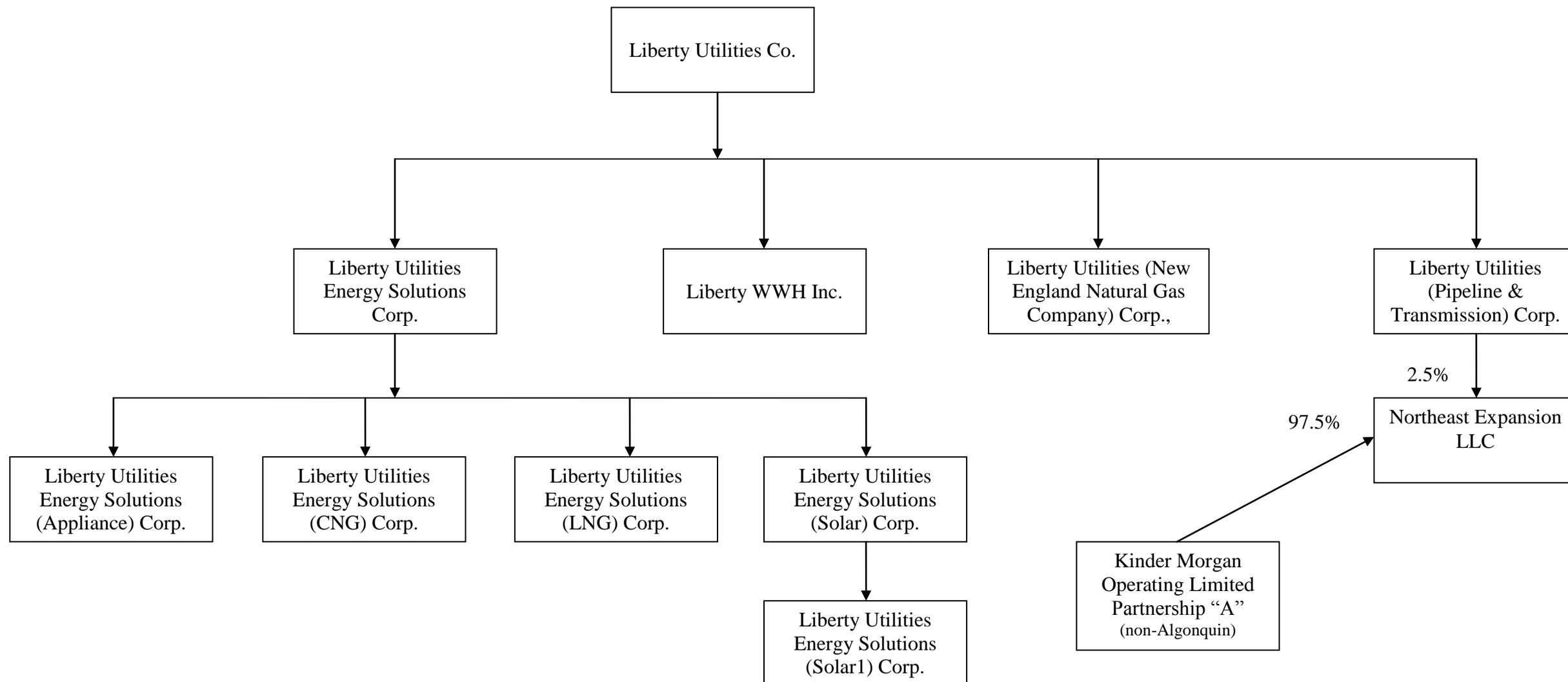
**Chart A**



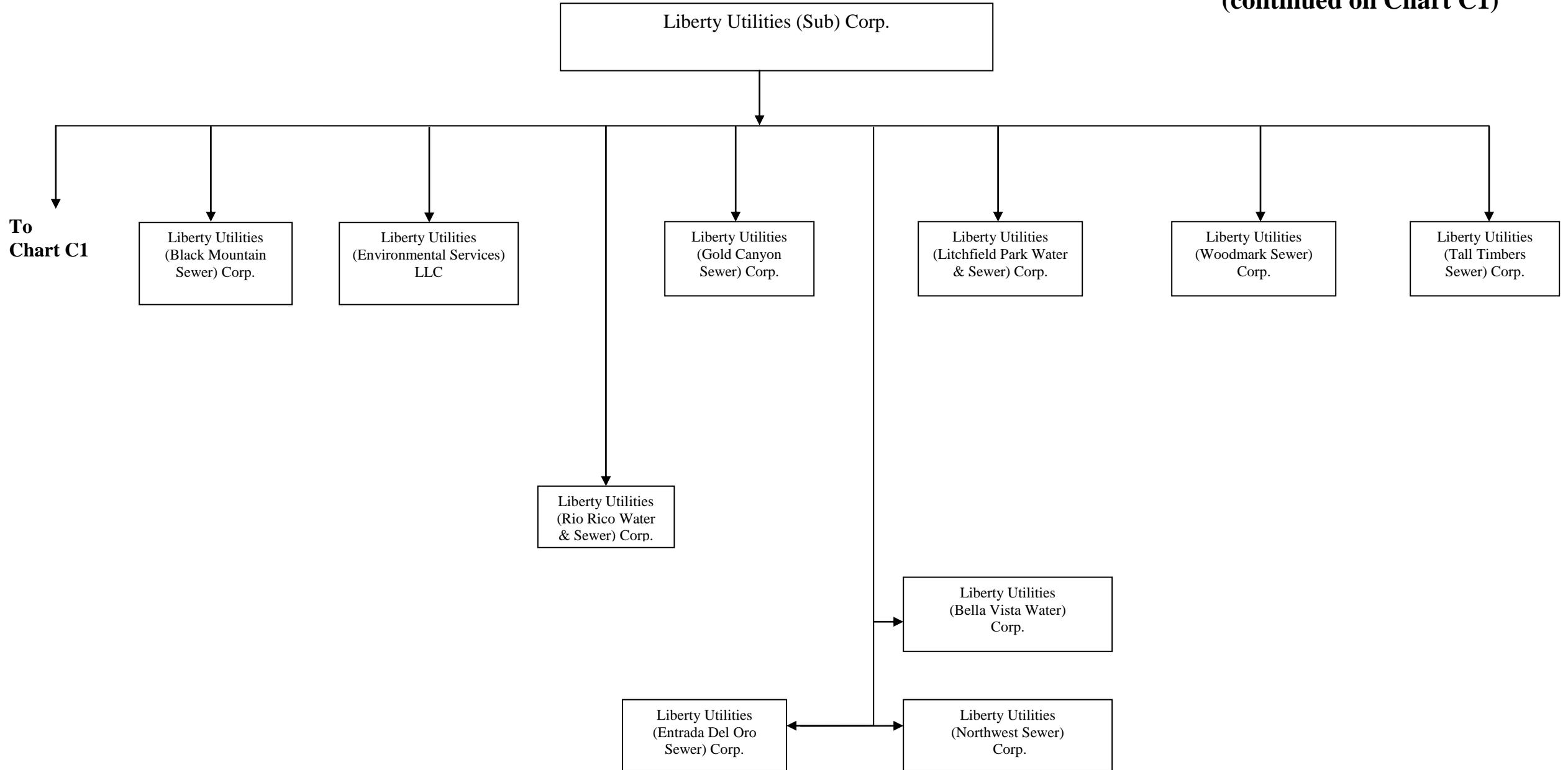
**Chart B**  
**(Continued on Chart B1)**



**Chart B1**

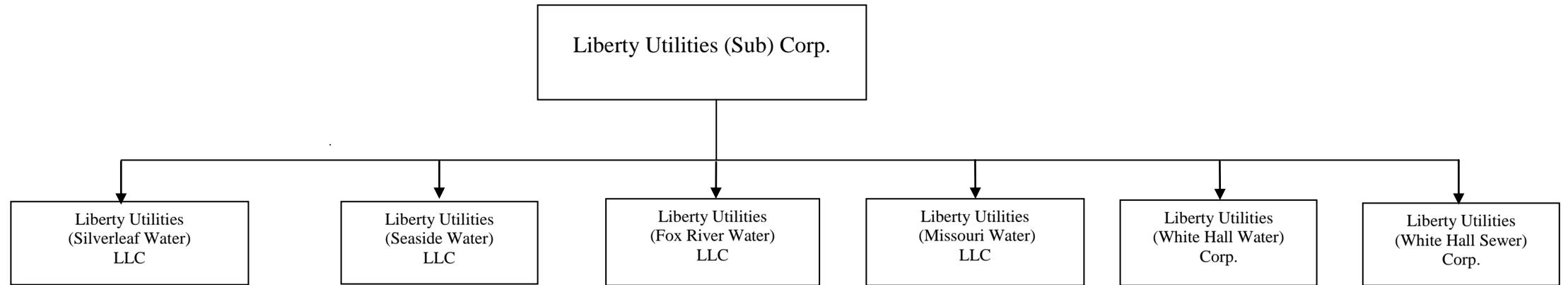


**Chart C**  
**(continued on Chart C1)**



**To  
Chart C1**

**Chart C1**



PSC-002

Regarding: Due Diligence

Witness: Unknown

- a. Please provide copies of all due diligence work papers, including but not limited to the offering valuation of Western Water Holdings in both paper and electronic formats with all formulas intact.

**Response:** Liberty objects to this request because it seeks information which is not relevant to this matter and is protected from disclosure as confidential and contains proprietary trade secrets. Liberty's due diligence work papers are not relevant because they have no impact on Mountain Water's consumers. The documents are not tied to the service consumers will receive, the operations of Mountain Water, or the rates consumers will pay. Moreover, Liberty's internal valuation will not affect Mountain Water's rates or the level of service, as stated in Liberty's application because Liberty does not intend to seek an acquisition adjustment to the existing rate base. Regardless of these considerations, all future rate changes will be subject to the Commission's review and approval. Accordingly, this request seeks information that has no bearing on the Commission's decision in this matter, and as such seeks information that is irrelevant and not reasonably calculated to lead to the discovery of admissible information.

The requested information is also protected from disclosure because it is proprietary and contains confidential trade secrets. Liberty's due diligence efforts, including any financial analyses of potential investments, are based upon years of research and investment at a substantial cost to Liberty Utilities. The underlying financial and other analyses and overall bid strategy and methodologies that Liberty implements in responding to solicitations relating to the sale of regulated utilities are proprietary and contain confidential trade secrets. Moreover, compelling winning bidders to disclose their successful strategy will necessarily have a chilling effect on the participation in the market of future offerings of utility assets. Disclosure of such information, even under seal, would be harmful to the business interests of Liberty, because both its seller and the City are parties who could obtain these materials, and the Commission cannot provide certainty that information produced, even under protective order, would not be subject to disclosure on challenge by a party or outside interested party.

- b. Please provide copies of all correspondence including electronic and phone logs between Liberty Utilities and Western Water regarding the sale and purchase of Western Water.

**Response:** Liberty objects to this request as overly broad and unduly burdensome, and to the extent it seeks information that is irrelevant and is not reasonably calculated to lead to the discovery of admissible information. The definitive Plan and Agreement of Merger was produced with the original Joint Application, and superseded all prior correspondence and negotiations. (Ex. B to Joint Application, Section 10.13, p. 51)

- c. Please provide copies of all presentations given to the directors of Western Water and to Liberty Utilities regarding the sale and purchase of Western Water.

**Response:** Liberty objects to this request because it seeks information which is not relevant to this matter and is protected from disclosure as confidential and contains proprietary trade secrets. Liberty's due diligence work papers are not relevant because they have no impact on Mountain Water's consumers. The documents are not tied to the service consumers will receive, the operations of Mountain Water, or the rates consumers will pay. Moreover, Liberty's internal valuation will not affect Mountain Water's rates or the level of service, as stated in Liberty's application because Liberty does not intend to seek an acquisition adjustment to the existing rate base. Regardless of these considerations, all future rate changes will be subject to the Commission's review and approval. Accordingly, this request seeks information that has no bearing on the Commission's decision in this matter, and as such seeks information that is irrelevant and not reasonably calculated to lead to the discovery of admissible information.

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- d. Please provide copies of all board minutes and notes where there was discussion of the sale and purchase of Western Water. If there were audio or video recordings, please provide those as well.

**Response:** Liberty objects to this request because it seeks information which is not relevant to this matter and information that is proprietary and contains confidential trade secrets. Liberty's internal presentations as requested are not relevant because they have no impact on the service consumers will receive, the operations of Mountain Water, or the rates consumers will pay. Moreover, Liberty does not intend to seek an acquisition adjustment to the existing rate base, and all future rate changes will be subject to the Commission's review and approval. Accordingly, this request seeks information that has no bearing on the Commission's decision in this matter, and as such seeks information that is irrelevant and not reasonably calculated to lead to the discovery of admissible information.

The requested information is also protected from disclosure because it is proprietary and contains confidential trade secrets. Liberty due diligence efforts, including its analyses of potential investments, are highly proprietary and based upon years of research and investment at a substantial cost to Liberty Utilities. The underlying financial and other analyses and overall bid strategy and methodologies that Liberty implements in responding to solicitations relating to the sale of regulated utilities are proprietary and contain confidential trade secrets. Moreover, compelling winning bidders to disclose their successful strategy will necessarily have a chilling effect on the participation in the market of future offerings of utility assets. Disclosure of such information, even under seal, would be harmful to the business interests of Liberty, because both the seller and the City are parties who could obtain these materials, and the Commission cannot provide certainty that information produced, even under protective order, would not be subject to disclosure on challenge by a party or outside interested party.

- e. Please provide all work papers that support the valuation of the offer presented to Western Water, including spreadsheets with formulas intact.

**Response:** Liberty objects to this request because it seeks information which is not relevant to this matter and is protected from disclosure as confidential and contains proprietary trade secrets. Liberty's due diligence work papers are not relevant because they have no impact on Mountain Water's consumers. The documents are not tied to the service consumers will receive, the operations of Mountain Water, or the rates consumers will pay. Moreover, Liberty's internal valuation will not affect Mountain Water's rates or the level of service, as stated in Liberty's application because Liberty does not intend to seek an acquisition adjustment to the existing rate base. Regardless of these considerations, all future rate changes will be subject to the Commission's review and approval. Accordingly, this request seeks information that has no bearing on the Commission's decision in this matter, and as such seeks information that is irrelevant and not reasonably calculated to lead to the discovery of admissible information.

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PSC-003

Regarding: Organizational Chart

Witness: Unknown

- a. Please provide the complete organizational chart for Liberty Utilities both prior to and after the proposed purchase and sale of Western Water showing all Liberty Utility subsidiaries.

**Response:** See attached Liberty-Algonquin organizational charts attached as Attachment PSC-001 (LIB-A) and Attachment PSC-003 (LIB-A).

- b. Please provide names and addresses of all subsidiaries of Liberty Utilities and the specific utility that each subsidiary provides.

**Response:**

<b>Name:</b>	<b>Address:</b>	<b>Specific Utility Service</b>
Liberty Energy Utilities (New Hampshire) Corp.	15 Buttrick Road Londonderry, NH 03053	n/a
Liberty Utilities Service Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities (Midstates Natural Gas) Corp.	2751 North High Street Jackson, MO 63755	Natural Gas service in Illinois, Iowa and Missouri
Liberty Utilities (CalPeco Electric) LLC	1125 Muscat Ave. Sanger, CA 93657	Electric service in California
Liberty Utilities (Pine Bluff Water) Inc.	1100 State Street P.O. Box 6070 Pine Bluff, AR 71611	Water distribution service in Arkansas
Liberty Utilities (Peach State Natural Gas) Corp.	2300 Victory Dr. Columbus, GA 31901-3455	Natural Gas service in Georgia
Liberty Utilities (Granite State Electric) Corp.	15 Buttrick Road Londonderry, NH 03053	Electric service in New Hampshire
Liberty Utilities (EnergyNorth Natural Gas) Corp.	15 Buttrick Road Londonderry, NH 03053	Natural Gas service in New Hampshire
Liberty Utilities Energy Solutions Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities Energy Solutions (Appliance ) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities Energy Solutions (CNG) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities Energy Solutions (LNG) Corp.	1212725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities Energy Solutions (Solar) Corp.	15 Buttrick Road Londonderry, NH 03053	n/a
Liberty Utilities Energy Solutions (Solar1) Corp.	15 Buttrick Road Londonderry, NH 03053	n/a
Liberty WWH Inc.	15 Buttrick Road Londonderry, NH 03053	n/a

<b>Name:</b>	<b>Address:</b>	<b>Specific Utility Service</b>
Liberty Utilities (New England Natural Gas Company) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Natural Gas service in Massachusetts
Liberty Utilities (Pipeline & Transmission) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities (Black Mountain Sewer) Corp.	112725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Sewer service in Arizona
Liberty Utilities (Environmental Services) LLC	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities (Gold Canyon Sewer) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Sewer service in Arizona
Liberty Utilities (Litchfield Park Water & Sewer) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Water and Sewer service in Arizona
Liberty Utilities (Woodmark Sewer) Corp.	16623 FM 2493 Tyler, TX 75703	Sewer service in Texas
Liberty Utilities (Tall Timbers Sewer) Corp.	16623 FM 2493 Tyler, TX 75703	Sewer Service in Texas
Liberty Utilities (Bella Vista Water) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Water distribution service in Arizona
Liberty Utilities (Entrada Del Oro Sewer) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Sewer service in Arizona
Liberty Utilities (Rio Rico Water & Sewer) Corp.	112725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	Water distribution and sewer service in Arizona
Liberty Utilities (Northwest Sewer) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities (Sub) Corp.	12725 W. Indian School Rd, Suite D-101 Avondale, AZ 85392	n/a
Liberty Utilities (Silverleaf Water) LLC	16623 FM 2493 Tyler, TX 75703	Water distribution service in Texas
Liberty Utilities (Seaside Water) LLC	16623 FM 2493 Tyler, TX 75703	Water distribution service in Texas
Liberty Utilities (Fox River Water) LLC	16623 FM 2493 Tyler, TX 75703	Water distribution service in Illinois
Liberty Utilities (Missouri Water) LLC	16623 FM 2493 Tyler, TX 75703	Water distribution service in Missouri
Liberty Utilities (White Hall Water) Corp.	101 Parkway Drive Whitehall, AR 71602	Water distribution service in Arkansas
Liberty Utilities (White Hall Sewer) Corp.	101 Parkway Drive Whitehall, AR 71602	Sewer service in Arkansas

c. Please provide the number of customers served by each utility.

**Response:** The table below indicates customers by utility as of December 31, 2014.

Utility	Type	Customers
Liberty Utilities (Calpeco Electric) LLC	Electric	48,900
Liberty Utilities (New England Gas Co.) Corp.	Natural Gas	54,426
Liberty Utilities (Peach State Natural Gas) Corp.	Natural Gas	56,270
Liberty Utilities (Pine Bluff Water) Inc.	Water	16,332
Liberty Utilities (Midstates Natural Gas) Corp.	Natural Gas	
-Missouri	Natural Gas	54,378
-Illinois	Natural Gas	22,038
-Iowa	Natural Gas	4,211
Liberty Utilities (Granite State Electric) Corp.	Electric	42,186
Liberty Utilities (EnergyNorth Natural Gas) Corp.	Natural Gas	87,199
Liberty Utilities (Black Mountain Sewer) Corp.	Wastewater	2,121
Liberty Utilities (Gold Canyon Sewer) Corp.	Wastewater	6,548
Liberty Utilities (Entrada Del Oro Sewer) Corp.	Wastewater	332
Liberty Utilities (Litchfield Park Water & Sewer) Corp.	Water & Wastewater	39,918
Liberty Utilities (Rio Rico Water & Sewer) Corp.	Water & Wastewater	8,454
Liberty Utilities (Bella Vista Water) Corp.	Water	9,908
Liberty Utilities (Missouri Water) LLC	Water	2,370
Liberty Utilities (Fox River Water) LLC	Water & Wastewater	439
Liberty Utilities (Silverleaf Water) LLC	Water & Wastewater	4,222
Liberty Utilities (Tall Timbers Sewer) Corp.	Wastewater	2,205
Liberty Utilities (Woodmark Sewer) Corp.	Wastewater	1,828
Liberty Utilities (Seaside Water) LLC	Water & Wastewater	468
Liberty Utilities (Whitehall Water) Corp.	Water	1,920
Liberty Utilities (Whitehall Sewer) Corp.	Wastewater	1,821
Total		468,494

d. Please provide name and addresses of the regulatory oversight body for each of the above utilities.

**Response:**

Utility	Commission / Address
Liberty Utilities (Calpeco Electric) LLC	California Public Service Commission 505 Van Ness Avenue San Francisco, CA 94102
Liberty Utilities (New England Natural Gas Company) Corp.	Massachusetts Department of Public Utilities One South Station Boston, MA 02110
Liberty Utilities (Peach State Natural Gas) Corp.	Georgia Public Service Commission 244 Washington St Atlanta, GA 30334-5701
Liberty Utilities (Pine Bluff Water) Inc.	Arkansas Public Service Commission 1000 Center Street PO Box 400 Little Rock, AR 72203-0400
Liberty Utilities (Midstates Natural Gas) Corp.	Illinois Commerce Commission 527 East Capitol Avenue Springfield, Illinois 62701
Liberty Utilities (Midstates Natural Gas) Corp.	Missouri Public Service Commission 200 Madison Street, PO Box 360 Jefferson City, MO 65102-0360
Liberty Utilities (Midstates Natural Gas) Corp.	Iowa Utilities Board 1375 East Court Avenue Des Moines, Iowa 50319
Liberty Utilities (Granite State Electric) Corp.	New Hampshire Public Service Commission 21 South Fruit Street, Suite 10, Concord, N.H. 03301-2429
Liberty Utilities (EnergyNorth Natural Gas) Corp.	New Hampshire Public Service Commission 21 South Fruit Street, Suite 10, Concord, N.H. 03301-2429
Liberty Utilities (Black Mountain Sewer) Corp.	Arizona Corporation Commission 1200 W. Washington Phoenix, AZ 85007-2996
Liberty Utilities (Gold Canyon Sewer) Corp.	Arizona Corporation Commission 1200 W. Washington Phoenix, AZ 85007-2996
Liberty Utilities (Litchfield Park Water & Sewer) Corp.	Arizona Corporation Commission 1200 W. Washington Phoenix, AZ 85007-2996
Liberty Utilities (Woodmark Sewer) Corp.	Public Utility Commission of Texas 1701 N. Congress Avenue PO Box 13326 Austin, TX 78711-3326

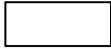
<b>Utility</b>	<b>Commission / Address</b>
Liberty Utilities (Tall Timbers Sewer) Corp.	Public Utility Commission of Texas 1701 N. Congress Avenue PO Box 13326 Austin, TX 78711-3326
Liberty Utilities (Bella Vista Water) Corp.	Arizona Corporation Commission 1200 W. Washington Phoenix, AZ 85007-2996
Liberty Utilities (Entrada Del Oro Sewer) Corp.	Arizona Corporation Commission 1200 W. Washington Phoenix, AZ 85007-2996
Liberty Utilities (Rio Rico Water & Sewer) Corp.	Arizona Corporation Commission 1200 W. Washington Phoenix, AZ 85007-2996
Liberty Utilities (Silverleaf Water) LLC	Public Utility Commission of Texas 1701 N. Congress Avenue PO Box 13326 Austin, TX 78711-3326
Liberty Utilities (Seaside Water) LLC	Public Utility Commission of Texas 1701 N. Congress Avenue PO Box 13326 Austin, TX 78711-3326
Liberty Utilities (Fox River Water) LLC	Unregulated due to small size
Liberty Utilities (Missouri Water) LLC	Missouri Public Service Commission 200 Madison Street, PO Box 360 Jefferson City, MO 65102-0360
Liberty Utilities (White Hall Water) Corp.	City of White Hall, 101 Parkway Dr. White Hall, AR 71612; Not regulated by the APSC
Liberty Utilities (White Hall Sewer) Corp.	City of White Hall, 101 Parkway Dr. White Hall, AR 71612; Not regulated by the APSC

Response No. PSC-003  
Attachment PSC-003 (LIB-A)

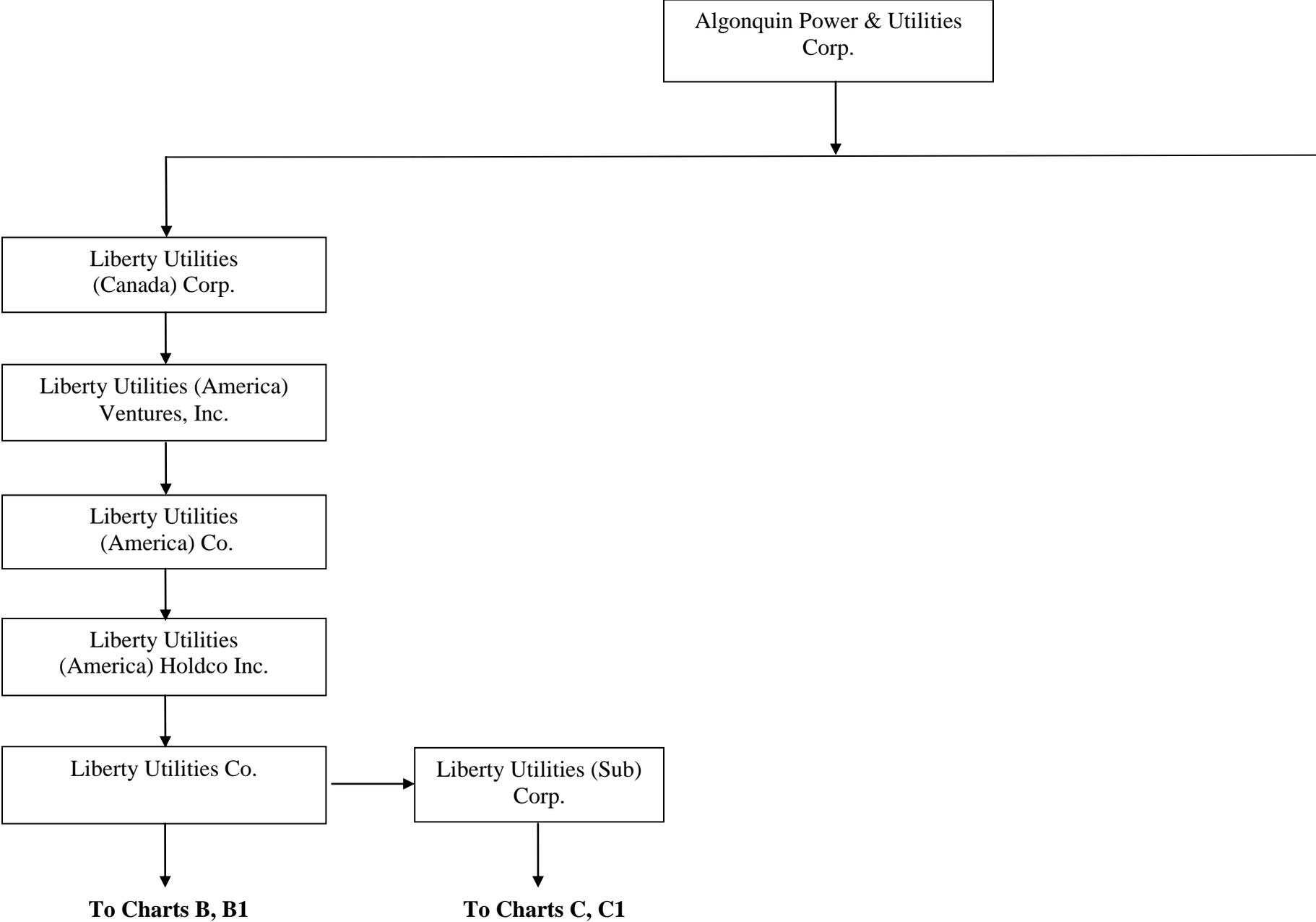
**LIBERTY UTILITIES  
ORGANIZATION CHART  
(After Park Water Acquisition)**

**KEY**

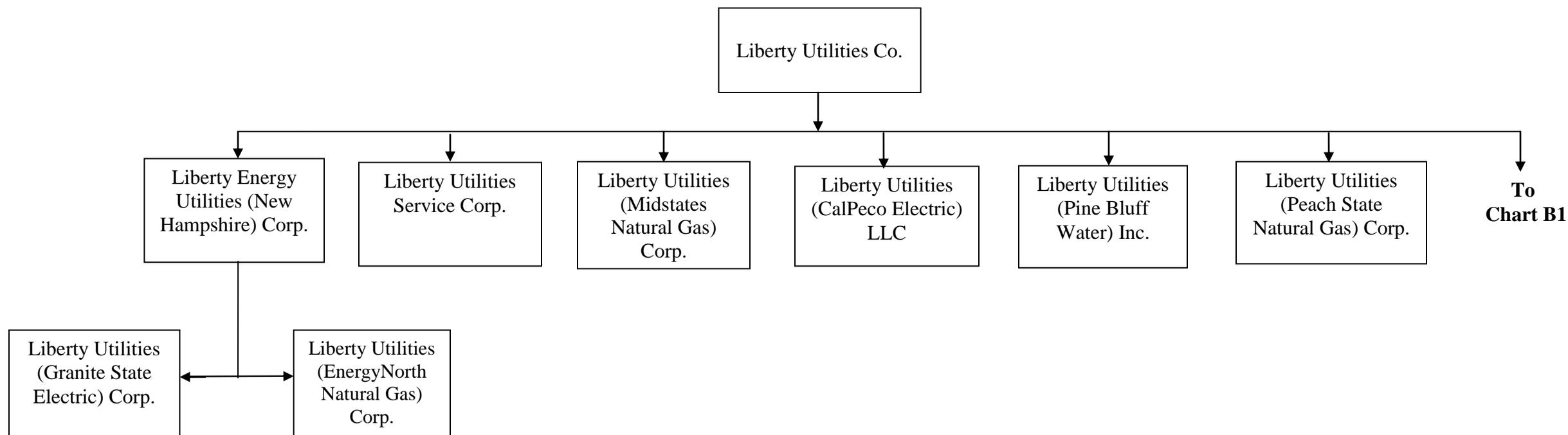
- 1. Corporation  
or LLC



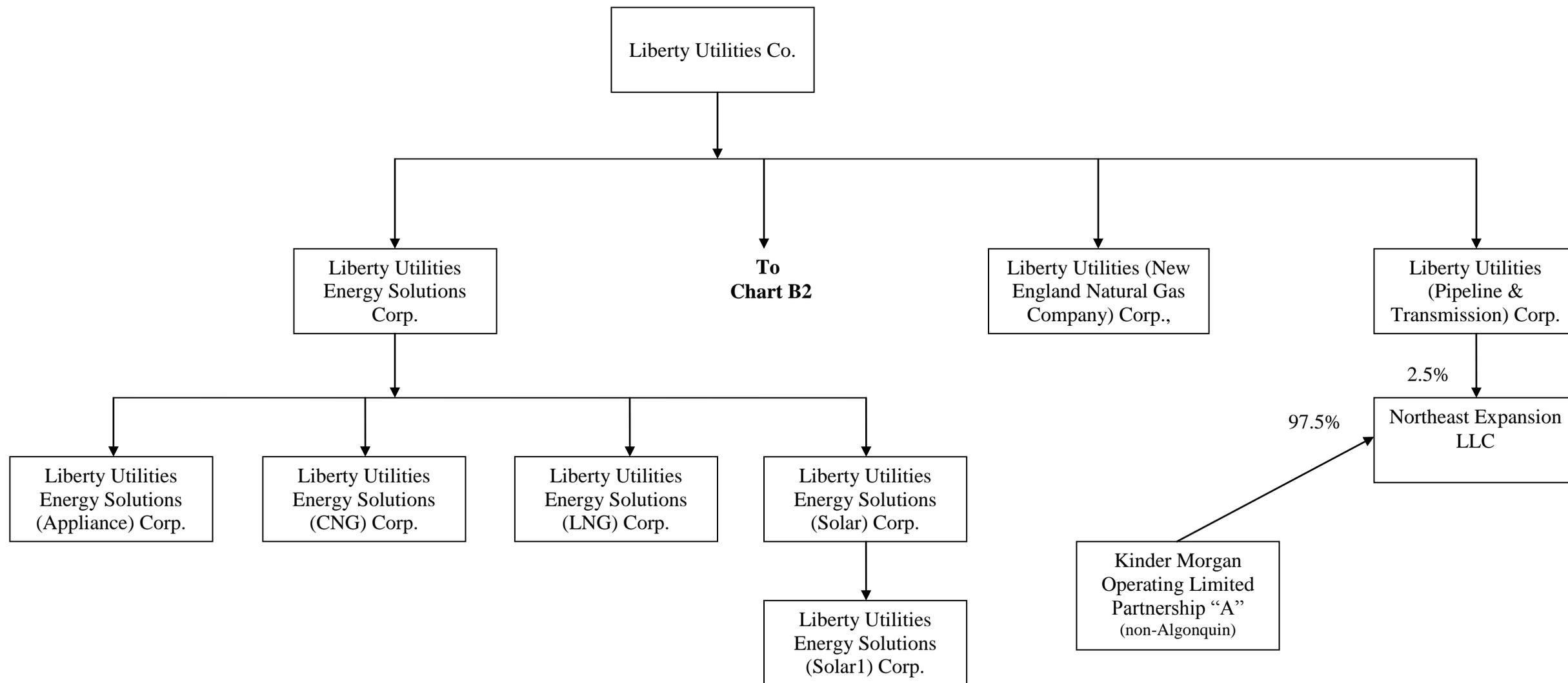
**Chart A**



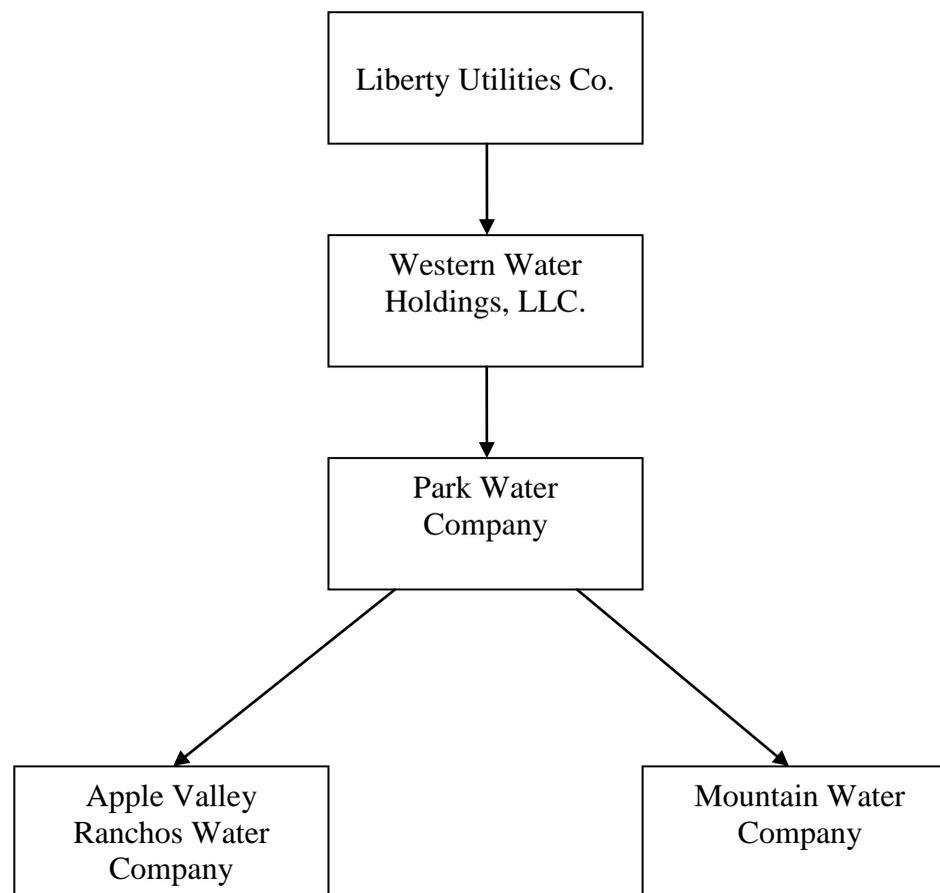
**Chart B**  
**(Continued on Chart B1)**



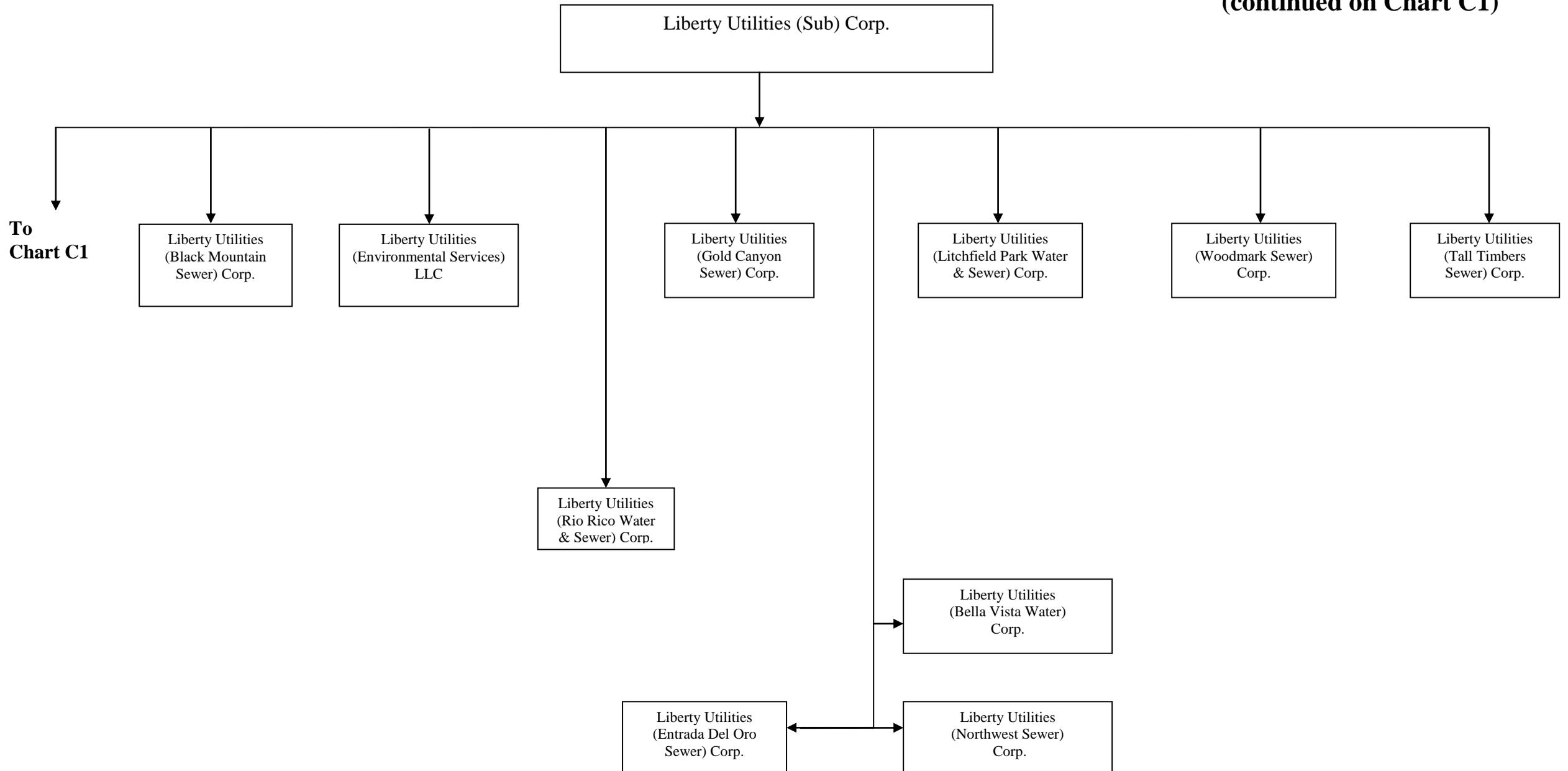
**Chart B1**



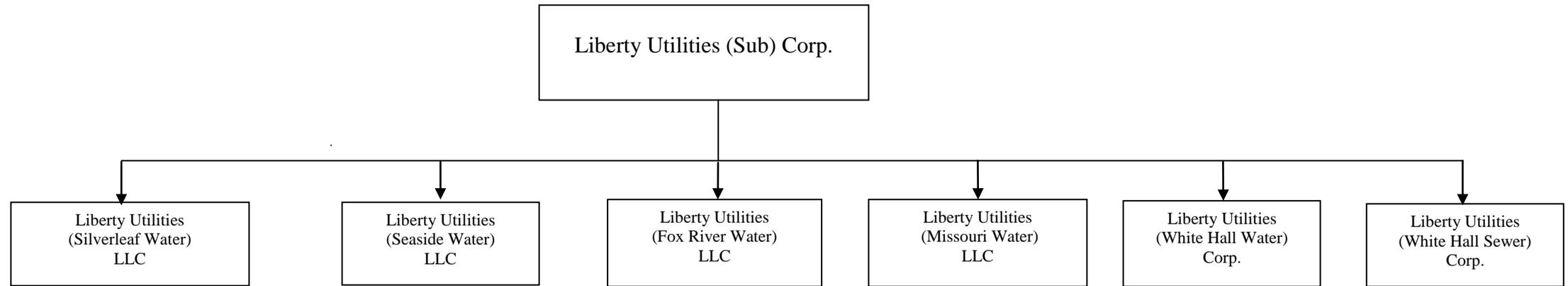
**Chart B2**



**Chart C**  
**(continued on Chart C1)**



**Chart C1**



PSC-004

Regarding: Ring Fencing  
Witness: Unknown

- a. Please provide copies of ring fencing provisions for each of the regulated subsidiaries of Liberty Utilities.

**Response:** At the outset, Liberty notes that the term “ring fencing” is not used uniformly within regulated industries. Indeed, there is a rather wide range of opinions among practitioners about what would be included within a definition of the term. The Company has assumed a broad definition of the term, such that “ring fencing provisions” for purposes of this response are defined as provisions that exist to protect customers from being adversely affected by actions taken by a regulated utility’s parent or affiliates. The following is a summary of what the Company believes to fall into this definition of “ring fencing provisions”, should they exist, across the States in which Liberty operates.

**Midstates:**

After reviewing the acquisition orders for the three Liberty natural gas utilities in Missouri, Illinois and Iowa, the only related provision is the following clause preventing Midstates from buying gas from affiliates without ICC (Illinois Commerce Commission) approval:

14. Liberty Energy Midstates is prohibited from purchasing or selling gas supply from an affiliated entity following the closing of the proposed transaction unless approval is petitioned for and granted by the Commission or unless such approval is not required under applicable law.

**Georgia:**

This section identifies “ring fencing provisions” that would apply to Liberty Utilities (Peach State Natural Gas) Corp in Georgia. The term “ring fencing provisions” does not appear within Georgia’s code or regulations applicable to utilities, and the Company is not aware of an order of the Georgia Public Service Commission (“GAPSC”) where the term has been used. Within the broad definition of the term as described above, the relevant provisions and practices in Georgia fall within two broad categories: (1) provisions that safeguard utility assets; and (2) provisions and practices that safeguard revenue requirements.

1. Protecting Utility Assets. Utility assets are safeguarded by the Commission having specific authority over the transfer of certificates of public convenience and necessity (O.C.G.A. §§ 46-4-28 et. seq. and Commission Rules 515-7-1-.09) and by granting authority over the issuance of stock by the regulated utility as well as issuance of long-term (defined as payable in a period greater than 12

months) bonds, notes or other evidences of debt (O.C.G.A. § 46-2-28 and Commission Rules 515-4-1-.01 et seq.).

2. Protecting Revenue Requirements. Revenue requirements are safeguarded by code provisions (O.C.G.A. § 46-2-26.4 and Commission Rule 515-3-1-.07) that specify the accounting procedures to be used by the Commission to establish rates to be charged by a gas utility.

With respect to shared costs (such as corporate overhead and shared services), utilities within the state that also have operations not subject to the Commission's jurisdiction (because such other operations are unregulated affiliates or divisions and/or because such other operations are affiliates or divisions regulated by jurisdictions other than Georgia) traditionally have utilized cost allocation manuals ("CAMs") that describe (a) the methodology used to allocate shared costs between regulated and unregulated operations and (b) the methodology used to allocate shared regulated costs among regulated operations. Changes to CAMs are made from time to time, and the changes are typically reviewed with Staff and interested parties at the time of such changes. Consequently, issues concerning internal cost allocations are typically resolved at the time of any such changes, and not raised in proceedings to establish new rates (except in the relatively rare situations of being raised by new intervenors that may not have participated in the discussions regarding CAM changes). Discussions regarding specific CAM elements typically center on associating cost causation with cost recovery. Nonetheless, overall reasonableness of CAMs tend to be assessed on a macro level (does it result in an overall fair and just share) rather than a micro level (could other factors provide a better nexus between cost causation and cost recovery for any particular set of costs).

The majority of all affiliate and shared costs are addressed by CAMs. With respect to services that are ancillary to core utility functions and that may be provided by third parties, the Staff has usually taken the position that the prices for such ancillary services should be established by the market. An illustration of the differences between an ancillary service and a core utility service can be found in gas supply services: services provided by a gas asset manager would be considered to be ancillary, whereas gas procurement would be a core utility service. Under this illustration, gas procurement would be governed by a CAM, but asset management services would not. For such ancillary services, most utilities typically issue requests for proposals. If affiliates are successful bidders, Staff and the Commission tend to be satisfied that the market value has been established. These practices have been established in a series of litigated dockets, and there is no single Commission rule that governs these practices (although language in orders often direct that such practices be perpetuated for the next rate or fuel cost cycle).

Finally, Liberty notes that pursuant to the Commission's general oversight authority, it has authorized its staff to review the books and records of parent and affiliate companies with respect to costs and charges associated with the regulated affiliate or

subsidiary. Protective orders are extended for confidential and trade secret materials that are examined.

### **New Hampshire**

In testimony before the Commission, Liberty agreed to a provision in the acquisition docket that Granite State would not procure power from a generation affiliate.

The New Hampshire Commission has rules pertaining to affiliate transactions. Those rules are available at: <http://www.puc.nh.gov/Regulatory/Rules/PUC2100.pdf>. In addition, the Company must file a compliance plan as required by the rules. That plan is a public document, and can be found on the NHPUC site [if necessary we can make this available. Do we want to attach it to a discovery response? I say no.]

Finally, there is a state law dealing with utility affiliates, located at: <http://www.gencourt.state.nh.us/rsa/html/xxxiv/366/366-mrg.htm>

### **Massachusetts**

The most-closely related rules in Massachusetts are found in 220 CMR: Department of Public Utilities 220 CMR 12.00: Standards of Conduct for Distribution Companies and Their Competitive Affiliates. These are rules for the interaction between the regulated and non-regulated affiliates. It primarily prevents a utility from providing a non-regulated affiliate any unfair competitive that would not be also made available to a non-affiliate. This rule is found attached as Attachment PSC-004 (LIB-A).

### **Arkansas**

The Arkansas Public Service Commission issued Order No. 7 in Docket 06-112-R, Affiliate Transaction Rules. Each year, Liberty Utilities (Pine Bluff Water) Inc. must file an annual affiliate report, containing relevant information and providing acknowledgement that it complies with all rules within the Arkansas Public Service Commission Affiliate Transaction Rules (Docket 06-112-R) Order.

The Order can be found here:  
[http://www.apscservices.info/pdf/06/06-112-r\\_59\\_1.pdf](http://www.apscservices.info/pdf/06/06-112-r_59_1.pdf)

### **California**

Attached is the California Public Utilities Commission (“CPUC”) decision and related appendix regarding affiliate transactions (see D.06-12-029) as Attachment PSC-004 (LIB-B). Although the decision only named three investor-owned utilities, Liberty Utilities agreed to follow this decision in the initial acquisition of the service territory from Sierra Pacific (see page 3 of D.10-10-027 Territory Transfer Appendices) attached as Attachment PSC-004 (LIB-C).

Currently, Liberty Utilities CalPeco does not have any affiliate agreements so therefore it does not file a compliance plan.

## **Arizona**

In Arizona, Liberty Utilities has six regulated utility subsidiaries: Liberty Utilities (Black Mountain Sewer) Corp., Liberty Utilities (Gold Canyon Sewer) Corp., Liberty Utilities (Litchfield Park Water & Sewer) Corp., Liberty Utilities (Bella Vista Water) Corp., and Liberty Utilities (Entrada Del Oro Sewer) Corp. Those entities are regulated by the Arizona Corporation Commission. Those entities are not subject to any ring fencing provisions established at the time of acquisition of those entities. In Arizona, Class A “investor-owned utilities” are subject to the Arizona Corporation Commission’s (“ACC”) Public Utility Holding Companies and Affiliated Interests Rules codified at A.A.C. R14-2-801 et seq. (“Arizona Rules”). Specifically, A.A.C. R14-2-804(A) provides that “a utility will not transact business with an affiliate unless the affiliate agrees to provide the Commission access to the books and records of the affiliate to the degree required to fully audit, examine or otherwise investigate transactions between the public utility and affiliates.” Further, under A.A.C. R14-2-805, Class A Arizona utilities are required to make an annual filing with the Arizona Corporation Commission each year relating to affiliate transactions, subject to review by the Commission and its Staff. Additionally, during rate cases before the Arizona Corporation Commission, affiliate transactions are closely scrutinized by the Commission and its Staff in review of those transactions, including review of affiliate transactions under the NARUC Guidelines for Cost Allocations and Affiliate Transactions.

## **Texas**

The relevant regulations for Texas are Chapter 24. Substantive Rules Applicable to Water and Sewer Service Providers, Subchapter B. Rates, Rate-Making, and Rates/Tariff Changes, §24.24-1 effective 9/1/14 (P 42190). More specifically, §24.24 Jurisdiction over Affiliated Interests identifies the Texas Public Utility Commission of Texas’ jurisdiction over affiliate interests. These are available at: <https://www.puc.texas.gov/agency/rulesnlaws/subrules/water/subchB/24.24.pdf>

Texas relies of several provisions in Texas Water Code to insure that a parent does not prohibit a subsidiary from providing continuous and adequate service to the public. Water Code 13.250(a) requires a retail public utility to provide continuous and adequate service. Section 13.002(2) allows the state to prosecute any affiliate for a violation of this duty. Section 13.411 affirms this right to prosecute a utility and an affiliate.

- b. If there are no ring fencing provisions in place for the regulated subsidiaries of Liberty Utilities, what safeguards are in place to prevent cross-subsidization from the regulated utilities to the non-regulated utilities? Please explain.

**Response:** To supplement the discussion provided in part a), Liberty provides its current version of the Cost Allocation Manual (“CAM”) as Attachment PSC-004 (LIB-D) to this response.

The Algonquin/Liberty CAM has been prepared in accordance and conformance with the NARUC Guidelines for Cost Allocations and Affiliate Transactions (“NARUC Guidelines”). More specifically, the founding principles of the Algonquin/Liberty CAM are to a) directly charge as much as possible to the entity that procures any specific service, and b) to ensure that inappropriate subsidization of unregulated activities by regulated activities, and vice versa, does not occur. For ease of reference, the NARUC Guidelines are included as Appendix 1 of the CAM.

Response No. PSC-004  
Attachment PSC-004 (LIB-A)

220 CMR 12.00: STANDARDS OF CONDUCT FOR DISTRIBUTION COMPANIES AND THEIR COMPETITIVE AFFILIATES

Section

- 12.01: Purpose and Scope
- 12.02: Definitions
- 12.03: General Standards of Conduct.
- 12.04: Pricing of Transactions Between Distribution Companies and Affiliates
- 12.05: Penalties

12.01: Purpose and Scope

- (1) Purpose. 220 CMR 12.00 sets forth the Standards of Conduct governing the relationship between a Distribution Company and its Affiliates transacting business in Massachusetts.
- (2) Scope. 220 CMR 12.00 applies to all Distribution Companies under the Department's jurisdiction. 220 CMR 12.00 does not supersede existing applicable law and regulations.

12.02: Definitions

Affiliate refers to any "affiliated company," as defined in M.G.L. c. 164, § 85, or any unit or division within a Distribution Company or its parent, or any separate legal entity either owned or subject to the common control of the Distribution Company or its parent.

Antitrust Laws are federal and state statutes, including the Sherman Act, 15 U.S.C. §§ 1 through 7, the Clayton Act, 15 U.S.C. §§ 12 through 27, and the Massachusetts Antitrust Act, M.G.L. c. 93, §§ 1 through 14A, and related judicial decisions.

Competitive Affiliate refers to any Affiliate that is engaged in the sale or marketing of products or services on a competitive basis.

Competitive Energy Affiliate refers to any Competitive Affiliate that is engaged in the sale or marketing of natural gas, electricity, or Energy-related Services on a competitive basis.

Competitive Non-energy Affiliate refers to any Competitive Affiliate that is engaged in the sale or marketing of products or service, other than natural gas, electricity, or Energy-related Services, on a competitive basis.

Department refers to the Department of Public Utilities.

Distribution Company refers to a natural gas local distribution company or Electric Company that provides distribution services under the Department's jurisdiction.

Electric Company is defined as in M.G.L. c. 164, § 1.

Employee refers to an officer, director, employee or agent who has specific knowledge of, or direct access to, information not otherwise available to Non-affiliated Energy Suppliers that could provide a Competitive Energy Affiliate with an undue advantage.

Energy-related Services are those services the costs of which have been recovered by Distribution Companies through rates approved by the Department.

Non-affiliated Energy Supplier refers to any entity, including aggregators, engaged in marketing, brokering or selling natural gas, electricity, or energy-related services to retail customers where such product or service is also provided by a Competitive Energy Affiliate.

Non-affiliated Supplier refers to any entity engaged in selling or marketing products or services where such product or service is also provided by a Competitive Affiliate.

12.03: General Standards of Conduct.

- (1) A Distribution Company shall apply tariff provisions in the same manner to the same or similarly situated entities if there is discretion in the application of the provision.
- (2) A Distribution Company shall strictly enforce tariff provisions for which there is no discretion in the application of the provision.
- (3) A Distribution Company shall not, through a tariff provision or otherwise, give its Competitive Affiliate or customers of its Competitive Affiliate preference over Non-affiliated Suppliers or their customers in matters relating to any product or service that is subject to a tariff on file with the Department.
- (4) If a Distribution Company provides its Competitive Energy Affiliate, or a customer of its Competitive Energy Affiliate, any product or service other than general and administrative support services, it shall make the same products or services available to all Non-affiliated Energy Suppliers or their customers on a non-discriminatory basis.
- (5) A Distribution Company shall not offer or sell electricity or natural gas commodity or capacity to its Competitive Affiliate without simultaneously posting the offering electronically on a source generally available to the market or otherwise making a sufficient offering to the market.
- (6)
  - (a) If a Distribution Company offers its Competitive Energy Affiliate, or a customer of its Competitive Energy Affiliate, a discount, rebate or fee waiver for any product or service, it shall make the same available on a non-discriminatory basis to all Non-affiliated Energy Suppliers or customers.
  - (b) If a Distribution Company offers a Competitive Affiliate, or a customer of a Competitive Affiliate, a discount, rebate or fee waiver for any product or service that is subject to a tariff on file with the Department, it shall make the same available to all Non-affiliated Suppliers and their customers simultaneously, to the extent technically possible, on a comparable basis.
- (7) A Distribution Company shall process all same or similar requests for any product, service, or information in the same manner and within the same period of time, consistent with the rules set forth in 220 CMR 12.03(6).
- (8) A Distribution Company shall not condition or tie the provision of any product, service, or rate agreement by the Distribution Company to the provision of any product or service by its Competitive Affiliate.
- (9) A Distribution Company shall not release any proprietary customer information to an Affiliate without the prior written authorization of the customer.
- (10) To the extent that a Distribution Company provides a Competitive Affiliate with information not readily available or generally known to any Non-affiliated Supplier, which information was obtained by the Distribution Company in the course of providing distribution service to its customers, the Distribution Company shall make that information available on a non-discriminatory basis to all Non-affiliated Suppliers transacting business in its service territory. 220 CMR 12.03(10) does not apply to customer-specific information obtained with proper authorization, information necessary to fulfill the provisions of a contract, or information relating to the provision of general and administrative support services.
- (11) A Distribution Company shall refrain from giving any appearance of speaking on behalf of its Competitive Affiliate in any and all contacts or communications with customers or potential customers. The Distribution Company shall not represent that any advantage accrues to customers or others in the use of the Distribution Company's services as a result of that customer or others dealing with the Competitive Affiliate.

12.03: continued

(12) The Distribution Company shall not engage in joint advertising or marketing programs of any sort with its Competitive Energy Affiliate, nor shall the Distribution Company directly promote or market any product or service offered by any Competitive Affiliate.

(13) Subject to 220 CMR 12.03(12), a Distribution Company may allow an Affiliate, including a Competitive Energy Affiliate, to identify itself, through the use of a name, logo, or both, as an Affiliate of the Distribution Company, provided that such use by a Competitive Energy Affiliate shall be accompanied by a disclaimer that shall state that no advantage accrues to customers or others in the use of the Distribution Company's services as a result of that customer or others dealing with the Competitive Energy Affiliate, and that the customer or others need not purchase any product or service from any Competitive Energy Affiliate in order to obtain services from the Distribution Company on a non-discriminatory basis. The disclaimer shall be written or spoken, or both, as may be appropriate given the context of the use of the name or logo.

(14) If a customer requests information about Energy Suppliers, the Distribution Company shall provide a current list of all Energy Suppliers operating on the system or registered with the Department, including its Energy-related Competitive Affiliate, but shall not promote its affiliate. The list of Energy Suppliers shall be in random sequence, and not in alphabetical order. The list shall be updated every 60 days to allow for a change in the random sequence.

(15) Employees of a Distribution Company shall not be shared with a Competitive Energy Affiliate, and shall be physically separated from those of the Competitive Energy Affiliate. The Distribution Company shall fully and transparently allocate costs for any shared facilities or general and administrative support services provided to any Competitive Affiliate.

(16) A Distribution Company and its Competitive Affiliate shall keep separate books of accounts and records which shall be subject to review by the Department in accordance with the provisions of M.G.L. c. 164, § 85.

(17) The Department may approve an exemption from the separation requirements of 220 CMR 12.03(15) upon a showing by the Distribution Company that shared employees or facilities would be in the best interests of the ratepayers and have minimal anticompetitive effect, and that the costs can be fully and accurately allocated between the Distribution Company and its Competitive Energy Affiliate. Such exemption shall be valid until such time that the Department determines that modification or removal of the exemption is necessary.

(18) A Distribution Company shall establish and file with the Department a dispute resolution procedure to address complaints alleging violations of 220 CMR 12.00. Such procedure shall designate a neutral person to conduct an investigation of the complaint; require that said person communicate the results of the investigation to the claimant in writing within 30 days after the complaint is received; and require that such communication describe any action taken and notify the complainant of his or her right to complain to the Department if not satisfied with the results of the investigation.

(19) A Distribution Company shall maintain a log of all new, resolved, and pending complaints alleging violations of 220 CMR 12.00. The log shall be subject to review by the Department and shall include the date each complaint was received; the complainant's name, address, and telephone number; a written description of the complaint; and the resolution of the complaint, or the reason why the complaint is still pending.

(20) Notwithstanding any other provisions in 220 CMR 12.00, in emergency circumstances, a Distribution Company shall take any actions necessary to ensure public safety and system reliability. A Distribution Company shall maintain a log of all such actions, subject to review by the Department.

12.04: Pricing of Transactions Between Distribution Companies and Affiliates

- (1) A Distribution Company may sell, lease, or otherwise transfer to an Affiliate, including a Competitive Affiliate, an asset, the cost of which has been reflected in the Distribution Company's rates for regulated service, provided that the price charged the Affiliate is the higher of the net book value or market value of the asset. The Department shall determine the market value of any such asset sold, leased, or otherwise transferred, based on the highest price that the asset could have reasonably realized after an open and competitive sale.
- (2) A Distribution Company may sell, lease, or otherwise transfer to an affiliate, including a Competitive Affiliate, assets other than those subject to 220 CMR 12.04(1), and may also provide services to an affiliate, including a Competitive Affiliate, provided that the price charged for such asset or service is equal to or greater than the Distribution Company's fully allocated cost to provide the asset or service.
- (3) An Affiliated Company may sell, lease, or otherwise transfer an asset to a Distribution Company, and may also provide services to a Distribution Company, provided that the price charged to the Distribution Company is no greater than the market value of the asset or service provided.
- (4) A Distribution Company must maintain a log of all transactions with Affiliated Companies made pursuant to 220 CMR 12.04(1) through (3). The log shall include the date of the transaction, the nature and quantity of the asset or service provided, the price charged, and an explanation of how the price was derived for purposes of compliance with 220 CMR 12.04. All log entries must be dated and made contemporaneously with relevant transactions. The log shall be kept up to date. The Distribution Company shall file a copy of the log with the Department no later than January 15th of each year, covering the previous year.

12.05: Penalties

- (1) Any Distribution Company or Affiliate that violates any provision of 220 CMR 12.05 shall be subject to a civil penalty not to exceed \$ 25,000 for each violation for each day that the violation persists; provided, however, that the maximum civil penalty shall not exceed \$ 1,000,000 for any related series of violations. Any such penalty shall be determined by the Department after a public hearing.
- (2) In determining the amount of any penalty assessed pursuant to 220 CMR 12.05(1), the Department will consider the following: the appropriateness of the penalty to the size of the business of the Distribution Company or Affiliate charged; the gravity of the violation; the good faith of the Distribution Company or Affiliate in attempting to achieve compliance after notification of a violation; and any other criteria deemed appropriate by the Department under the circumstances.
- (3) Nothing in 220 CMR 12.00 shall be construed to confer immunity from state and federal Antitrust Laws. A penalty assessed pursuant to 220 CMR 12.00 does not affect or preempt antitrust liability but rather is in addition to any antitrust liability that may apply to the activity.

REGULATORY AUTHORITY

220 CMR 12.00: M.G.L. c. 164, §§ 1, 1C, 1F, 76A, 76C, 85, 85A, 94A, 94B, 94C

**Response No. PSC-004**  
**Attachment PSC-004 (LIB-B)**

Decision 06-12-029 December 14, 2006

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

Order Instituting Rulemaking Concerning  
Relationship Between California Energy  
Utilities And Their Holding Companies  
And Non-Regulated Affiliates.

Rulemaking 05-10-030  
(Filed October 27, 2005)

**OPINION ADOPTING REVISIONS TO (1) THE AFFILIATE TRANSACTION  
RULES AND (2) GENERAL ORDER 77-L, AS APPLICABLE TO  
CALIFORNIA'S MAJOR ENERGY UTILITIES AND  
THEIR HOLDING COMPANIES**

**1. Summary**

Today's order amends the Commission's Affiliate Transaction Rules by adopting the Affiliate Transaction Rules Applicable to Large California Energy Utilities and amends General Order (GO) 77-L (which governs the reporting of compensation paid to executive officers and employees of regulated utilities), by adopting GO 77-M. The adopted amendments apply solely to Respondents, California's major energy utilities and their holding companies: Southern California Edison Company (Edison)/Edison International, Pacific Gas and Electric Company (PG&E)/PG&E Corporation, and Southern California Gas Company (SoCalGas) and San Diego Gas & Electric Company (SDG&E), both owned by Sempra Energy.

These amendments retain many of the proposals put forward by Commission staff but the Proposed Decision has been revised further under the direction of the assigned Commissioner. These revisions to the Affiliate

Transaction Rules have been designed to close existing loopholes in three main ways: (1) ensuring that key utility and holding company officers understand the Rules and their obligations under them; (2) providing greater security against the sharing within the corporate family, through improper conduits, of competitively-significant, confidential information; and (3) ensuring a utility's financial integrity is protected from the riskier market ventures of its unregulated affiliates and holding company parent. GO 77-M includes new provisions developed to yield a more complete and accurate picture of Respondents' compensation practices while protecting reasonable privacy interests.

The amendments to both Rules have required us to strike difficult balances between the public interest and the private interests of unregulated utility affiliates and the individuals employed within the holding company structure. Though we recognize these private interests, we have not lost sight of the reason these electric and natural gas utilities exist: to provide energy services in a safe, reliable and environmentally sustainable manner at the lowest reasonable cost.

## **2. Background and Procedural History**

Decision (D.) 06-06-062, which amended this Order Instituting Rulemaking (OIR or Rulemaking), discusses problems with the Commission's Affiliate Transaction Rules and with GO 77-L, as well as potential solutions. Following written comment and reply comment,<sup>1</sup> Commission staff released draft rule

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<sup>1</sup> At Respondents' request, the Administrative Law Judge (ALJ) extended the date for filing Comments from July 27 to August 8; she authorized the filing of Reply Comments on August 18. The following parties filed Comments: Consumer Federation of California (CFC), Division of Ratepayer Advocates (DRA), Respondents (jointly), Richard Robinson & Associates, Inc. (Robinson Associates), and the Greenlining

*Footnote continued on next page*

revisions on September 12, 2006<sup>2</sup> for further discussion at a public workshop held September 21, 2006. We have received additional written comment in the form of Pre-workshop and Post-workshop Statements.<sup>3</sup>

The Proposed Decision mailed on October 10, 2006. At the request of the assigned Commissioner, Oral Argument was held on October 18. Comments on the Proposed Decision were due on October 30, 2006 and Reply Comments were due on November 6.<sup>4</sup> By ruling on November 11, 2006, parties were asked to provide additional written comment by November 17, 2006.<sup>5</sup>

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Institute (Greenlining). The following parties filed Reply Comments: CFC, DRA, Greenlining, and Respondents (jointly). Greenlining requested and received leave from the ALJ to file a further Reply on August 23, 2006. Independent Energy Producers Association's (IEP) Comments were attached to its September 29, 2006 motion requesting party status. Because IEP was granted party status earlier in this Rulemaking, its motion is moot.

<sup>2</sup> See *Administrative Law Judge's Ruling Proposing Draft Rules for Workshop Discussion*, September 12, 2006 (September 12 ALJ Ruling).

<sup>3</sup> The following parties filed Pre-workshop Statements: CFC and Respondents (jointly). The following parties filed Post-workshop Statements: CFC, DRA, Greenlining, IEP, Respondents (jointly), Robinson Associates, and The Utility Reform Network (TURN).

<sup>4</sup> The following parties filed timely Comments: CFC, DRA, Greenlining, Respondents (jointly), and The Utility Reform Network (TURN). CFC, DRA, and Respondents (jointly) also filed timely Reply Comments.

<sup>5</sup> See *Joint Ruling of Assigned Commissioner and Administrative Law Judge Inviting Comment on Further Proposal for Revisions to the Rules IV, V and VI of the Affiliate Transaction Rules Applicable to Large California Energy Utilities and Correcting Omission in Draft Revisions to GO 77 Attached to the Proposed Decision*, November 7, 2006 (November 7 AC/ALJ Ruling). DRA and Respondents (jointly) filed timely Comments.

### **3. Revised Affiliate Transaction Rules**

#### **3.1. Overview – Major Amendments**

Appendices A-1 and A-2 to this decision show, in redlined format, the complete text of the Affiliate Transaction Rules Applicable to Large California Energy Utilities (Revised Affiliate Transaction Rules or Revised Rules) which we adopt today. Appendix A-3 is a “clean” version of the Revised Rules. These appendices replace the Proposed Decision’s Appendix A. The Revised Rules, applicable only to Respondents, are based on the Affiliate Transaction Rules (Original Rules) adopted nearly ten years ago by D.97-12-088, as subsequently amended.<sup>6</sup> The Original Rules will continue to apply to all California energy utilities, other than Respondents, except those which have been expressly exempted by prior Commission decisions. To avoid confusion about applicability in the future, we will soon open a rulemaking for the sole purpose of amending the Original Rules to exempt the large energy utilities from them and to include a cross-reference to the Revised Rules.

The Revised Rules are not identical to either the staff proposals released with the September 12 ALJ Ruling, the Proposed Decision’s Appendix A, or the proposals released with the November 7 AC/ALJ Ruling. We have refined these working drafts (to clarify, remove ambiguity, or reduce burden, etc.) and we have discarded several proposals altogether. The Comments on the Amended OIR, the workshop discussion, the written workshop statements and the Comments on the Proposed Decision and November 7 AC/ALJ Ruling have all

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<sup>6</sup> D.97-12-088, 77 CPUC 2d 422, 449, as amended by D.98-08-035, 81 CPUC 2d 607 and D.98-12-075, 84 CPUC 2d 155.

been helpful. Where Respondents have suggested changes to reporting or compliance deadlines so as to allow more lead time for compliance, improve efficiency, or minimize duplication of effort, we have incorporated all reasonable suggestions.

The amendments include the following changes, as well as other, minor revisions intended, for example, to improve internal consistency or delete outdated provisions concerning initial compliance with the Original Rules:<sup>7</sup>

- Add Table of Contents
- I. Definitions
  - Clarify ban on circumvention of Revised Rules by prohibiting use of a utility consultant or contractor as a conduit.
- II. Applicability
  - Clarify applicability of the Revised Rules to utility's holding company.
  - Expressly provide that utility holding company shall not be used to circumvent the Revised Rules.
  - Expressly exempt transactions involving broadband over power lines from the Revised Rules (recognizing D.06-04-070).
  - Delete outdated provisions concerning initial compliance with the Original Rules.
- III. Nondiscrimination
  - Clarify scope of permitted utility-affiliate transactions.
  - Prohibit utility resource procurement from affiliates without prior Commission approval.
- IV. Disclosure and Information

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<sup>7</sup> Parties' Comments have not objected to these minor changes.

- Delete provision requiring utility to compile, update and provide to customers a list of service providers that compete with its affiliate in offering gas- or electric-related goods or services, since there has been no customer demand for such lists.
- V. Separation
  - Expressly provide that utility, its affiliates, and its holding company shall be separate corporate entities and keep separate books and records.
  - Reiterate that Commission may review books and records of utility holding company.
  - Provide utility and its holding company with an election: (1) retain authorization to engage in sharing of all services permitted under Original Rules but eliminate any duplication of personnel among key corporate officers at utility and holding company, or (2) retain ability to name individuals to multiple key offices at utility and holding company but prohibit sharing of regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services that remain authorized. Key corporate officers consist of the Chair of the entire corporate enterprise, the President at the utility and at the holding company, the chief executive officer at each, the chief financial officer at each, the chief regulatory officer at each – or the functional equivalent, where other titles are used.
  - Delete outdated provisions concerning initial compliance with the Original Rules.
- VI. Regulatory Oversight
  - Require utility compliance plans by June 30, 2007.
  - Require utility to file advice letter with Commission upon formation of a new affiliate.
  - Require Commission staff, rather than utility, to direct compliance audits and perform audits on a biennial, rather than annual, basis.
  - Reiterate witness availability must be provided pursuant to existing law.

- Require key corporate officers (as defined above) at utility and its holding company to annually certify to personal compliance with the Revised Rules.
- Add VIII. Complaint Procedures and Remedies (adopted by D.98-12-075).
- Add new IX. Protecting the Utility's Financial Health
  - Require annual utility reports on capital budgets and policies (i.e., annual updates on the six categories of information requested by the OIR).
  - Reiterate that utility shall retain the capital structure authorized by the Commission and request a waiver whenever equity falls by 1% or more.
  - Require utility to provide a non-consolidation opinion that demonstrates that the "ring-fencing" around the utility is sufficient to prevent it from being pulled into the bankruptcy of its holding company; require utility to notify Commission if ring-fencing measures are changed.

Respondents' initial Comments and Workshop Statements oppose much of the content of the earlier versions of the Revised Rules. DRA and CFC support most of the earlier versions and in some instances urge us to go further, if the Commission is to exercise adequate utility oversight short of holding company divestiture. Though IEP and TURN each focus on single (and different) issues, they both strongly recommend action -- IEP, to prevent utility favoritism toward generation affiliates and TURN, to insulate utilities from any financial problems at the holding company level.

Respondents' recent Comments on the November 7, 2006 AC/ALJ Ruling are comparatively muted. Respondents acknowledge the efforts the November 7 Ruling has made to address their concerns about the Proposed Decision's perceived compliance burden and impact upon corporate governance.

Respondents indicate that they support the changes the Ruling proposes to Rule

VI (officer certification) and “are reluctantly willing to accept” the proposals to revise Rule V E to provide an election (shared services versus officer duplication). (Respondents’ November 17, 2006 Comments, pp. 5, 8.)

Several rule revisions have been uncontroversial. These include two revisions to Rule VI, Regulatory Oversight. Respondents appear to recognize that the Commission, rather than a utility, should determine whether a new utility affiliate is covered by the Revised Affiliate Transaction Rules (Rule VI A and B) and that it is reasonable for the Commission to take a lead role in selecting the auditor hired to perform the required utility audits (Rule VI C). Neither have Respondents contested the revisions to Rule IV, Disclosure and Information, which remove the requirement to compile, for dissemination to customers, lists of the service providers that compete with utility affiliates in offering gas- or electric-related goods or services. Commission staff have been advised that because customers have not asked for the lists, the ongoing effort to update the lists is unnecessarily time consuming.

Below, we discuss the major issues that Respondents and the other parties raise.

### **3.2. Discussion**

The impetus for our examination of the Affiliate Transaction Rules now is the recent repeal of the Public Utilities Holding Company Act (PUHCA)<sup>8</sup> coupled with potentially serious flaws in Respondents’ interpretation of and compliance with the Original Rules.

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<sup>8</sup> The Energy Policy Act of 2005 (EPA 2005), Public Law 109-58, among other things repealed the Public Utility Holding Company Act of 1935, 12 USC §§ 79 – 79z-6.

Respondents contend that the repeal of PUHCA does not necessitate further review of the Original Rules, because each of the holding companies was exempt from PUHCA. However, Respondents miss the point. Until PUHCA was repealed, a state commission could always petition the Securities and Exchange Commission (SEC) to remove the exemption if the holding company structure thwarted effective state regulation of a utility. For example, in 1973, the SEC considered but rejected its staff's recommendation to remove the exemption for Pacific Lighting Corporation (PLC), the parent holding company of Southern California Gas Company at that time. The SEC found, among other things, that notwithstanding PLC's expanding diversification, the California Commission could still effectively regulate the utility and protect its ratepayers.<sup>9</sup> Because one of the main purposes of PUHCA was to facilitate effective state regulation of the utilities, the SEC gave considerable weight to state commissions' views concerning an exemption.<sup>10</sup> Therefore, if a holding company's acquisitions or operations ever threatened effective state regulation of the utility, the state commission had the remedy of petitioning the SEC to remove the holding company's exemption. With the repeal of PUHCA, that remedy no longer exists.<sup>11</sup>

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<sup>9</sup> See *In the Matter of Pacific Lighting Corporation* (1973) 173 SEC LEXIS 2231.

<sup>10</sup> See *Sempra Energy* (1998) 1998 SEC LEXIS 1310 at \*84; see also *KU Energy Corporation* (1991) 1991 SEC LEXIS 2568 at \*20-21.

<sup>11</sup> CFC's Comments and Workshop Statements contain an extensive review of the serious abuses that led to enactment of PUHCA. CFC reminds us that similar problems could arise in the future. We share CFC's concern.

D.06-06-062, which amended this Rulemaking, discusses a number of interpretation and compliance problems (selective applicability to utility holding companies and unregulated affiliates, overly narrow interpretations of the scope of covered transactions, overbroad interpretations of express exceptions, conflicts of interest, etc.). These problems give rise to two main concerns. One is the likelihood for preferential treatment, unfair competitive advantage, or the sharing of competitively sensitive confidential information within the partly regulated, mostly unregulated corporate family and the consequences such competitive abuse poses for energy markets and captive ratepayers. The second concern is the potential threat to a utility's financial health and ability to meet its public service obligations unless it is adequately insulated from the financial risks and debts of its unregulated parent and affiliates. D.06-06-062 observes that given the "substantial profits or risks at stake, there are strong incentives within the holding company structure to take advantage of confidential utility information or use ratepayer-subsidized utility facilities, whether to help affiliates maximize their profits or bail them out from risks." (D.06-06-062, p. 11, slip op.)

The Revised Affiliate Transaction Rules have been designed to close existing loopholes, primarily by ensuring that key utility and holding company officers understand the Rules and their obligations under them, by providing greater security against the sharing within the corporate family, through improper conduits, of competitively-significant, confidential information, and by ensuring a utility's financial integrity is protected from the riskier market ventures of its unregulated affiliates and holding company parent.

In their Comments and Workshop Statements, Respondents argue that our concerns are largely speculative, that the electric energy crisis is now behind us,

and that recent audits of utility compliance with the Affiliate Transaction Rules have reported few, relatively minor violations. Respondents challenge what they characterize as the failure of Commission staff to lay out adequate evidentiary support for the need for revisions to the Original Rules. The September 12 ALJ Ruling notes this controversy and the reliance of Commission staff on D.06-06-062, which states: “We are not interested in conducting additional discovery in this rulemaking or litigating, here, what happened in the past.” (D.06-06-062, *mimeo.*, p. 10.)

However, because Respondents have pointed to past audits as proof that no problems exist with their Affiliate Transaction Rules compliance, we feel compelled to take official notice of the auditors’ findings and recommendations. All of the compliance audits are public documents. Where the Commission has not reviewed an audit in a formal proceeding and made its own findings, we take official notice merely to highlight the disparity between Respondents’ characterizations and the findings in the audits themselves, but make no assessment of the merits.

The most recent and most serious problems appear in several audits for the Sempra companies.<sup>12</sup> We also are well aware that in other Commission

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<sup>12</sup> We refer here to three audits. An Affiliate Transaction Rules compliance audit of SDG&E and SoCalGas in 2004 by auditors hired and managed by Sempra Energy identified violations or partial compliance with eight Rules, including Rule V E, Corporate Support. The auditors reported:

SDG&E’s joint utilization of Energy Risk Management as a corporate shared service has resulted in the means and transfer of confidential information from the utility to the affiliate, created the potential for unfair competitive advantage, and provided a conduit for the transfer of confidential utility information to a covered affiliate. Furthermore,

*Footnote continued on next page*

Energy Risk Management had conducted hedging related activities specifically forbidden by Rule V.E. NorthStar further concludes that Sempra Energy has not complied with CPUC Decision 02-09-048 related to the receipt and use of time-sensitive non-public information from SoCalGas Acquisition and SDG&E Fuel and Power Supply. (2004 *Affiliate Transactions Audit of Southern California Gas Company, May 1, 2005*, and 2004 *Affiliate Transactions Audit of San Diego Gas & Electric Company, May 1, 2005*, by NorthStar Consulting Group, p. 62.)

The auditors recommended that: “Energy Risk Management should not be performed as a shared corporate service.” (Recommendation #9); “SoCalGas should stop the transmittal of market related information to Sempra Energy Risk Management.” (Recommendation #10.) The SDG&E audit contained a similar recommendation.

An audit four years earlier had identified the same problem. (See *Management Audit and Market Power Mitigation Analysis of the Merged Gas System Operation for Pacific Enterprises and Enova Corporation*, Vol. 1-3, July 2000, by Larkin & Associates, pp. 1-10.) The audit was ordered by D.98-03-073, which approved the merger of SoCalGas and SDG&E. In D.02-09-048, which issued after review of the audit, the Commission determined that the auditors had identified a serious problem (the transfer of confidential information to the unregulated affiliate, Sempra Energy Trading, through the shared risk management services allowed under Rule V E). The Commission attempted to impose a remedy (a delay in the transmittal of confidential information from the utility to the holding company), but the 2004 audit found this requirement often was ignored. (See 2004 *Affiliate Transactions Audit...*, p. 59.)

In Investigation (I.) 03-02-033, the Commission required a staff-managed audit of the Sempra companies to identify any Affiliate Transaction Rules violations since 1997. Auditors found that the shared risk management function “acted as a conduit for proprietary information between the utility and its affiliates in violation of Rule V E.” (*Confidential Report to the CPUC for the Affiliate Transactions Compliance Audits of Sempra Energy’s Southern California Gas Company/San Diego Gas and Electric Company*, by GDS and Associates, pp. 5 and 51.) The auditors concluded that the parent was a covered affiliate under the applicability provisions of Rule II B since it provides financial credit derivative services to its unregulated trading affiliate. The auditors recommended that the Commission prohibit risk management as a shared service and that Sempra Energy agree to comply with the affiliate rules as a covered affiliate (*Id.*, p. 5). While the report is marked “confidential” it is not. The report was filed in I.03-02-033 by the Commission’s Energy Division and served on the service list on February 28, 2006.

proceedings (I.02-11-040 and I.03-02-033), Edison has contended that certain conduct by Sempra Energy and its affiliates, including SDG&E and SoCalGas, violated the Original Rules. Recently, these parties have reached an agreement to settle their differences, and in Application 06-08-026 and in motions to withdraw claims in both investigations, they have requested that the Commission close those proceedings without adjudicating Edison's claims or the claims of the auditors. Having sought dismissal on that basis, Respondents may not refer to the past audits as evidence that their past practices have not resulted in violations of the Original Rules. Respondents cannot have it both ways.<sup>13</sup>

Respondents also challenge the evidentiary basis for any amendments to the Affiliate Transaction Rules. Because this Rulemaking is quasi-legislative in character, a hearing of a judicial type is not necessary. We are not required to rely upon evidence produced in this proceeding, but may draw upon evidence from past proceedings, our knowledge and experience, comments in this proceeding and our current policies.<sup>14</sup> Indeed, when we adopted the Original Rules in 1997, we did not conduct evidentiary hearings. Pursuant to Section 1708.5(f) of the Public Utilities Code, we may revise the Affiliate

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<sup>13</sup> D.06-06-062 discusses the different business approaches vis a vis the California market the three holding companies have taken in the last decade or so. Sempra has most actively engaged in business operations in California and the market affecting this state. PG&E Corporation emerged from the bankruptcy brought about by the energy crisis without any significant affiliates. Until recently, largely because of affiliate abuse problems related to its Mission Energy affiliate in the time period from 1984 to 1992, Edison International has restricted most of its affiliate operations to other geographic markets. (See D.93-03-021, 48 CPUC 2d 352.)

<sup>14</sup> See *City of Santa Cruz v. Local Agency Formation Commission of Santa Cruz County* (1978) 76 Cal. App. 3d 381, 388.

Transaction Rules in this proceeding through notice and comment rulemaking procedures without conducting an evidentiary hearing.<sup>15</sup> There is no dispute of fact concerning the inherent conflict of interest within the holding company structure. There is also no reason why, on a policy basis, we cannot revise the Original Rules to close certain loopholes in order to more effectively address this conflict of interest.

Additionally, the matters at issue in this Rulemaking are not, as Respondents appear to imply, unknown to the attorneys, lobbyists and other representatives of utilities, independent energy producers, and others who appear before the Commission. This has been a matter of substantial public and expert concern since the California energy crisis of 2000-2001. In the intervening five years, there has been no dearth of official reports and recommendations, to say nothing of accounts in the public press. As an example, the California Attorney General issued an “Energy White Paper”<sup>16</sup> that discussed the need for a myriad of regulatory reforms. More significantly, this Commission bears an independent obligation to look at anti-trust matters in its endeavors. In *Northern California Power Association v. Public Utilities Commission* the California Supreme Court rebuked the Commission for its failure to take into account sua sponte the anti-trust aspects of an application:

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<sup>15</sup> See *Southern Cal. Edison Co. v. Public Utilities Com.* (2002) 101 Cal.App.4th 982, 994.

<sup>16</sup> Attorney General’s Energy White Paper: A Law Enforcement Perspective on the California Energy Crisis, April 2004, <http://ag.ca.gov/publications/energywhitepaper.pdf>. We take official notice of this report.

[I]t is clear that the Commission must take into account the antitrust aspects of applications before it. It is equally obvious that the Commission failed to perform this essential duty in the instant case. Although the Commission heard extensive testimony and legal argument...its decision appears to ignore the antitrust issues entirely...

....

The task of the Commission extends far beyond the passive role of a sounding board. The Commission cannot discharge its duty by merely taking "cognizance of the contracts between PG&E and its steam suppliers," without evaluating their effect upon the interests of the public. It must weigh the opposing evidence and arguments in order "to determine whether the rights and interests of the general public will be advanced by the prosecution of the enterprise which it is proposed to carry on for the service of the public." ...The Commission must place the important public policy in favor of free competition in the scale along with the other rights and interests of the general public. Here, the Commission did not perform this task; it incorrectly found "no need to determine the issues raised by NCPA." (5 Cal. 3d 370, 379 (1971).)

### **3.2.1. Rule II – Applicability to Holding Companies**

In the 1997 decision adopting the Affiliate Transaction Rules, the Commission states, "the development of competitive markets would be undermined if the utility were able to leverage its market power into the related markets in which their affiliates compete." (D.97-12-088, 77 CPUC 2d 422, 449.) The same would be true were a holding company to leverage its utility's market power or govern the utility in a way that provided unfair competitive advantages to utility affiliates over competitors. D.06-06-062 plainly recognizes the potential for holding company abuse, stating: "Unless key aspects of the Affiliate Transaction Rules govern the relationship between a utility and its

holding company, these rules and the underlying reasons for them can be totally circumvented at the top of the corporation where the significant decisions are made.” (D.06-06-062, *mimeo.*, p. 13.)

Instead of showing that there are no problems with the Original Rules, Respondents’ Comments highlight one of the major problems motivating us to adopt these amendments. Commission staff and some auditors have tended to perceive this problem as resulting from Respondents’ overly narrow interpretation of when and how the Original Rules apply to the holding companies. Respondents insist that the holding companies are not covered by the Original Rules “unless the holding companies themselves (as opposed to their subsidiaries) directly participate in energy markets.” (Respondents’ Comments, p. 28.)<sup>17</sup>

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<sup>17</sup> Respondents take somewhat contradictory positions. On the one hand, relying upon the definition of “affiliate” in Rule I, Definitions and upon Rule II B, Applicability, Respondents assert the Original Rules clearly exempt holding companies not directly and actively engaged in the provision of electricity or natural gas services/products. On the other hand, Respondents suggest that we need not be concerned that holding companies might be used as a conduit to pass confidential information to utility affiliates because holding companies are covered by the prohibitions in Rule V E, Separation-Corporate Support.

Rule V E recognizes a corporate support exception to the basic requirement for separation between a utility and its affiliates, explicitly extends this exception to “the utility, its parent holding company, or a separate affiliate created solely to perform corporate support services...,” and emphasizes that any shared services “shall not allow or provide a means for the transfer of confidential information from the utility to the affiliate, create the opportunity for preferential treatment or unfair competitive advantage, lead to customer confusion, or create significant opportunities for cross-subsidization of affiliates.” The Rule requires mechanisms to effect utility compliance (but does not explicitly require holding company compliance).

Narrow interpretation of the Affiliate Transaction Rules creates a significant loophole and undermines their use as an adequate regulatory tool for protecting utility ratepayers and ensuring fair competition in energy markets. We examine two, simple hypothetical illustrations.

In the first, a utility provides confidential information to its corporate parent, the holding company, and unbeknownst to the utility, the holding company shares the confidential information with an affiliate or utilizes the confidential information to provide preferential treatment or an unfair competitive advantage to the affiliate.

Under Respondents' narrow interpretation, the utility may report confidential information directly to the holding company, and as long as this exchange does not utilize shared services (which may be used only if they do not create an opportunity for the transfer of confidential information), no violation of the Original Rules has occurred. The reasons? The holding company is not covered by the Rules and shared services were not utilized.

In our second hypothetical, a holding company instructs its utility to submit a particular procurement proposal to the Commission and unbeknownst to the utility, the proposal will provide preferential treatment for an affiliate. Again, if the holding company is not covered, no violation of the Rules has occurred, even though Respondents' narrow interpretation undermines the entire purpose of the Original Rules.

There are two approaches to closing this loophole. The approach we have followed is to amend specific Rules to explicitly provide that they bind the holding company. The other approach would be to interpret "affiliate" to include the holding company by virtue of its governance of the energy products/services provided by marketing affiliates. We have rejected this

approach because it creates other problems. For example, if we made the entirety of the Revised Affiliate Transaction Rules applicable to holding companies, they would be unable to keep any communications with their utilities confidential. Also, the greater structural separation required would oblige the holding company and utility to be housed in separate buildings.

The amendments to Rules II B and II C close the loophole without creating new, undesirable consequences. Specifically, Rule II B, as amended, clarifies that whenever a Rule explicitly extends its reach to a utility's holding company, that Rule is meant to apply and does apply to the holding company. The amendment rejects and prevents future use of a circular argument that, based upon the current definition of "affiliate" and the wording of Rule II. B (in the Original Rules), none of the subsequent Rules apply to a holding company which does not provide energy services, even though, the subsequent Rule, by its own terms otherwise would apply.

In Rule II C, we adopt amendments to explicitly prohibit a holding company or any other affiliate from *knowingly* directing or causing a utility to violate or circumvent the Revised Rules. This amendment revises staff's proposal by inserting the element of scienter, as Respondents' Workshop Statements argue we must. We agree that consistency with Section 2111 of California Public Utilities Code necessitates this amendment.

### **3.2.2. Rule III – Nondiscrimination**

The amendments to Rule III B do two things. One, they strengthen the requirement that any information provided by a utility to an affiliate be limited to that made generally available to all market participants. Two, they close a significant loophole in existing resource procurement transactions by extending

the requirement for Commission pre-approval of utility-affiliate procurement to cover all types of resources.

IEP supports both of these amendments and states that they “are useful tools in a multifaceted effort to ensure fair competition among utility generation affiliates and independent power producers.” (IEP Post-workshop Statement, p. 4.) IEP remarks that the other Commission tools for protecting against affiliate procurement abuse, the Independent Evaluator and Procurement Review Groups, “have not yet been shown to be effective.” (*Id.*, p. 3.) IEP adds:

[T]he Commission must ensure that no favoritism occurs in the procurement process when affiliates are involved. If utility projects or affiliate proposals are allowed to compete with independent, nonaffiliated power producers in solicitations where the utility retains the primary power to select winners, it must be beyond dispute and transparent to all participating parties that the winning projects are selected on a fair and unbiased basis. (*Ibid.*)

As we noted in D.06-06-062, while recent statutes or Commission decisions generally require some form of Commission pre-approval for utility procurement of electricity, or utility execution of liquefied natural gas (LNG) contracts and interstate pipeline contracts, at present there are no pre-approval requirements for other resources, such as natural gas supplies. Natural gas utilities file reports with the Commission which provide details of their purchases of natural gas from affiliates, but there is no way to determine if the utility is providing preferential treatment to its affiliate or to assess the reasonableness of the affiliate’s after-market sales to the utility. Such omissions open the door to the appearance of favoritism and possibly, to actual market abuse. Compliance need not be overly burdensome. For short-term purchases, for example, pre-approval need not require transaction-by-transaction assessment, but might be based on a methodology approved by the Commission.

We have revised the staff proposals to exempt blind transactions from the pre-approval requirement.

**3.2.3. Rule IV – Disclosure and Information vs.  
Rule VI – Regulatory Compliance**

The Proposed Decision included a new Rule IV C that would have required semiannual, confidential reports from a utility to the Commission disclosing when and to whom at the holding company or an affiliate the utility has provided non-public information concerning one or more of six commercially sensitive subjects: information supplied by the affiliate's competitor; negotiations with the affiliate's competitor; utility procurement plans; utility operational matters; expansion plans; and the affiliate's competition with other entities.

Respondents contend that sound governance principles and duties under state corporate law, federal securities laws and the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley),<sup>18</sup> require that holding company officials must have access to all material information about their subsidiaries' businesses. Such information, they argue, is necessary for a holding company to certify the company's financial statements and internal controls and thereby accurately disclose all material information to investors in a timely manner. We agree. As proposed, new Rule IV C would not have prohibited the utility from providing non-public information to its holding company.

Respondents also maintain that the obligation to report on these six subjects would be so burdensome as to interfere with or even deter the flow of

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<sup>18</sup> Pub. L. 107-204 (July 30, 2002).

information between the utility and its parent, particularly if the reporting requirements include communications involving the corporate support group of shared services under Rule V E. Respondents also maintain that the reporting obligation would fail to prevent abuse. For example, Respondents state:

“Indeed, if the Commission does not trust executives to comply with the existing anti-conduit rules, then a rule that would impose a recording requirement would add nothing because there would be no basis for believing that the covered communications were properly recorded.” (Respondents’ Comments, p. 21.)

One of Respondents’ spokesmen made the same point at Oral Argument, stating:

“... the key people at the holding company that have the obligation to the board and to – under Sarbanes-Oxley, if they don’t intent to honor the anti-conduit rule, none of the rest of this burdensome activity works.” (Tr. 39:1-5.)

One Commissioner present at Oral Argument, who expressed a strong concern about the burden note taking would impose, nonetheless remarked: “One fellow I used to work for used to say, “Trust, but verify.” (*Id.* at 47:14-15.) The Commissioner also observed: “... somewhere along the line there needs to be some comfort in the public that we get what we need in the process. So the point is really balance...” (*Id.* at 47:27-48:2.)

In lieu of the Proposed Decision’s approach and in our continuing effort to strike the appropriate balance, we endorse the alternative approach offered for comment by the November 7, 2006 AC/ALJ Ruling. This alternative, offered in lieu of the Proposed Decision’s new Rule IV C, instead amends Rule VI, Regulatory Compliance by adding a new Rule VI E entitled “Officer Certification.” Rule VI E requires each key officer of a utility and its holding company parent to execute an annual certification under penalty of perjury that the officer is familiar with the Revised Rules and either has complied with them

or has listed any known violations. One of the concerns underlying this rulemaking is the potential for a utility's parent holding company to serve as a conduit, whether intentionally or inadvertently, for the kinds of information that the Original Rules prohibit the utility and its affiliate from sharing directly. The certification requirement is meant to ensure that responsibility for compliance with the Revised Rules reaches all the way to the top of the corporate enterprise and influences those individuals with the greatest ability to control utility/holding company and utility/affiliate relationships.

#### **3.2.4. Rule V – Shared Services**

Our previous adoption of holding company structures for California's major natural gas and electric utilities relied upon corporate separation of the regulated and unregulated entities. When the Commission adopted the Affiliate Transaction Rules in D.97-12-088, however, it found that the development of competitive markets required even more separation between a utility and its affiliate. Rule V, Separation was the result. Nevertheless, in Rule V E (Corporate Support), the Commission allowed an exception and authorized sharing of the corporate support group of services, provided that sharing those services did not give any affiliate an unfair competitive advantage.

As we explained in D.06-06-062, we now question the breadth of some of the exceptions, particularly the exceptions for "financial planning and analysis," "regulatory affairs," "lobbying" and "legal." These exceptions could include matters affecting marketing or operational issues, for example, where an affiliate can be given an unfair competitive advantage. Although Rule V E states that the exceptions should not provide a means to transfer confidential information between the utility and the affiliate, provide preferential treatment or create an unfair advantage, we must question whether such separation is possible. In

D.06-06-062, we asked the questions: “How can an attorney or a consultant giving advice to an affiliate, completely avoid transmitting confidential utility information that he or she also holds? Even if the attorney or consultant does not disclose the confidential information, how could it not at least influence the attorney’s or consultant’s advice?” (D.06-06-062, *mimeo.*, p. 16.)

Respondents contend that professionals can keep the confidential information separate, and they give as examples law firms that may have clients in competing businesses. However, when the same law firm is hired by two clients with contrary interests, those clients typically have an opportunity to decide whether or not to waive any conflict issues. Even then, there may be a firewall imposed in the law firm.

In contrast, for holding company shared services, competitors of the affiliate or groups representing ratepayers have no opportunity to decide whether or not to waive conflict issues that may arise when the same lawyer or law firm provides shared services for the utility and its affiliate. There are no mandatory firewalls within the shared services of the holding company, and firewalls are ineffective if the same person is providing the shared services.

Another problem with shared services in Rule V E (Original Rules) is timing. The shared services allow an affiliate to obtain information prior to public disclosure, if any. In addition, the individuals providing shared services may learn an enormous amount of vital, non-public information from the utility that could be very beneficial to the affiliate. Yet, under the Original Rules, even if an individual had extensive knowledge of one or more of these subjects, he or she could provide shared services for the utility, holding company and affiliate, simply because that individual is an attorney, regulatory affairs official, lobbyist or financial planner. Similarly, under Rule V G of the Original Rules, contractors

or consultants could be jointly retained by the utility, holding company and affiliate and thereby learn about a utility's confidential matters while working concurrently for the affiliate.

Respondents claim that the shared services help to ensure that holding company officials receive necessary information and that all entities in the corporate family take consistent positions with respect to material issues that bear on public disclosures. They further contend that these shared services are necessary to enable all entities in the corporate family to take a common, coordinated position before this Commission and other state and federal bodies. However, there is nothing in the Revised Rules which precludes a holding company from obtaining information from its utility without using shared services. For example, holding company officials can call utility officials or receive written or oral reports or presentations from utility officials.

Furthermore, some of the coordination that takes place through use of shared services concerns us. Respondents contend that the corporate family should be entitled to harmonize conflicting goals in order to present coordinated positions before the Commission and other agencies. They further suggest that the First Amendment protects their right to do so. This entirely depends upon what they are harmonizing.

Often it is permissible for a utility, its holding company, and affiliates to take coordinated positions before the Commission. Just like other parties which may jointly file pleadings, the utility and its holding company and affiliate do not have to share services of the same individual in order to do so. However, if a utility, its holding company and affiliates should decide to engage in anti-

competitive conduct whereby the utility provides preferential treatment for its affiliate, this harmonization is not proper or protected by the First Amendment.<sup>19</sup>

We provide a hypothetical example. Suppose SoCalGas and SDG&E were to coordinate with their holding company and affiliates in order to purchase regasified LNG only from Sempra LNG and avoid a fair opportunity for any other potential LNG supplier to compete and offer a better supply arrangement. A coordinated effort, subsequently, to file an application with the Commission for approval of this supply arrangement would not be justifiable or protected by the First Amendment.

Coordination problems are not merely hypothetical, however. In D.06-06-062, we cited examples of significant utility/affiliate/holding company problems in California's past (Edison and Mission Energy, PG&E and PGT, SoGalGas and PITCO). We reiterate that utilities have a public service obligation to provide services in a safe, reliable and environmentally sustainable manner at the lowest reasonable cost. Preferential treatment to affiliates is prohibited. Whether or not these legal obligations conflict with holding company or affiliate goals, it is impermissible for a utility to resolve these conflicts by abandoning its public service obligations.

Because of these concerns, the Proposed Decision recommends revision of the examples of permitted and prohibited corporate support services in Rule V E.

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<sup>19</sup> See, e.g., *Columbia Steel Casting v. Portland General Electric* (9th Cir.1996) 111 F.3d 1427, 1446 ["Applying to an administrative agency for approval of an anticompetitive contract is not lobbying activity within the meaning of the *Noerr-Pennington* doctrine (which is rooted in the First Amendment protection). In any case, PGE is not being held liable for filing the application . . . PGE is being held liable for agreeing with PP&L to replace competition with area monopolies in the Portland market."]

The Proposed Decision would exclude sharing by utility and affiliates of regulatory affairs, lobbying, risk management, and legal services (except legal services necessary to the provision of authorized shared services). However, largely based on workshop discussions in which Respondents itemized some of the specific corporate tasks which rely upon the timely sharing of information, the Proposed Decision would expand the examples of permitted sharing to include cash management, banking relations, communications with rating agencies, trust management, and corporate compliance with the Revised Rules. The Proposed Decision also would revised Rule V G (Employees) to extend the prohibition on the sharing of employees by utility and affiliates to ban the sharing of consultants and contractors (though it would expressly exempt auditors and providers of accounting services).

Respondents' Comments strongly oppose the Proposed Decision's approach to Rule V and continue to assert that its suggestions for amendment to Rule V are unwarranted, inefficient and in some cases, unworkable. After considering Respondents' concerns and reconsidering the Commission's regulatory objectives, the November 7 AC/ALJ Ruling suggests an alternative approach, which provides a utility and its holding company with an election. This election involves modifying Rule V to provide that if these corporate entities prefer to retain the provisions on shared services or shared employees, consultant, and contractors found in the Original Rules, they must eliminate any duplication of personnel among key corporate officers. If they prefer not to eliminate overlap among key officers, then they must cease sharing services in the areas of legal, regulatory affairs and lobbying. The definition of key officers for the purposes of Rule V is the same as for the new officer certification requirement in Rule IV. In lieu of the change to Rule V G, we also make a minor,

clarifying amendment to Rule I, Definitions to stress that the utility shall not use a consultant or contractor as a conduit to circumvent the Revised Rules.

We think that the election goes far to solve the matters of greatest concern to us, either by directly limiting the scope of shared services or by restricting the potential conflict of interest among top corporate decision makers. The present high degree of overlap among key corporate officers at each utility and its holding company parent means either option will take time to implement. Accordingly, we require implementation by 180 days after the effective date of today's decision.

Our adoption of these revisions strikes a different balance than the Proposed Decision would, but the objectives are the same. Today's decision offers Respondents greater flexibility to determine how to conduct their businesses efficiently, minimize duplication and enjoy any economies of scale that may be available but also requires clearer protections against preferential treatment of utility affiliates.

### **3.2.5. Rule IX – Protecting the Utility's Financial Health**

The new Rule IX consists of four provisions, A-D, previously articulated in various Commission decisions. Rule IX A is designed to ensure that we receive, on an ongoing basis, the same information (about capital budgets, etc.) that we called for in the OIR. Rule IX B imposes on all the utilities the obligation to retain a capital structure consistent with the Commission-authorized structure. We imposed this requirement on PG&E in 1996, in D.96-11-017. Respondents would prefer that we did not add this requirement to the Revised Rules, but have not established that it is unreasonable. As Respondents' suggest, however,

we have revised the staff proposal and Proposed Decision so that the Rule tracks the language in D.96-11-017.

We have deleted the final two staff proposals and added two ring-fencing proposals which TURN advocates. One of the deleted rules would prohibit a utility from issuing dividends or repurchasing stocks when its senior, unsecured long-term debt rating falls to the lowest investment grade unless the utility first obtains Commission approval to do so. We imposed this condition in our approval of the PacifiCorp merger, D.06-02-033, where it was offered as one of the many terms of the multi-state settlement. Respondents oppose this staff proposal, partly because it inadvertently referenced the wrong debt benchmarks. Respondents also argue that the rule may have adverse consequences and offer, in support, the opinion of their consultant, Steven M. Fetter.<sup>20</sup> We conclude that we should not impose this condition, broadly, without further study. The other deleted rule would prohibit a utility from becoming or remaining liable for the indebtedness of its affiliates without Commission approval, also a condition of approval of the PacifiCorp merger. This condition essentially restates the prohibitions in Public Utilities Code Section 701.5, and as such, need not be restated in the Revised Rules.

Rules IX C and IX D are two of the ring-fencing measures which we approved in the context of the PacifiCorp merger. TURN urges us to adopt these two provisions which focus “on the *effect* of the intended ring-fencing, rather

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<sup>20</sup> Fetter is President of Regulation, UnFettered, an energy advisory firm. He served as head of the utility ratings practice at Fitch Ratings (1993-2002) and Chairman of the Michigan Public Service Commission (1987-1993). By motion filed September 29, 2006, Respondents seek leave to file Fetter’s Declaration. The motion is unopposed.

than the detailed provisions required to achieve such an outcome.” (TURN Post-workshop Comments, p. 2.) That effect, of course, is to ensure that a utility is not pulled into the bankruptcy of its holding company, should serious financial problems develop. We have amended the Revised Rules to adopt TURN’s recommendation.

Rule IX C simply requires a utility to obtain a non-consolidation opinion that demonstrates that the ring-fencing measures it has in place are adequate to keep the utility out of a bankruptcy filed by its holding company parent. Rule IX C does not mandate what types of ring-fencing measures the utility must adopt. We make no changes to this Rule. However, after further consideration, we have revised Rule IX D to require only that a utility notify the Commission if it subsequently makes changes to its ring-fencing measures.

#### **4. GO 77-M**

The new GO 77-M, appended to this decision as Appendices B-1 and B-2, consists of our amendments to GO 77-L, the prior version of the general order.<sup>21</sup> Appendix B-3 is a “clean” version of the general order. The amendments have been developed to yield a more complete and accurate picture of Respondent’s compensation practices while protecting reasonable privacy interests. Greenlining urged us to expand the OIR to consider a number of issues related to

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<sup>21</sup> The Appendices show corrections made to reinsert in draft GO 77-M an existing paragraph that was unintentionally dropped from the working draft. That paragraph makes the existing general order applicable to utilities having gross operating revenues of \$1 billion or more. It will continue to apply to all such utilities other than Respondents, consistent with Public Utilities Code Section 1708, which requires notice and opportunity to be heard before the Commission may alter a prior decision. Because this Rulemaking applies only to Respondents, any modifications to existing law made by today’s decision apply only to Respondents.

executive compensation. We did so in D.06-06-062 and stated our intent to consider revisions to GO 77-L. In response, the September 12 ALJ Ruling released the staff proposals. We have looked closely at the pre- and post-workshop statements and other comments and have refined the staff proposals by incorporating suggestions from Respondents and from Greenlining. In summary, the amendments to the general order require:

- reporting of total compensation, by category and in the aggregate, for all utility Executive Officers and employees with a base salary of \$250,000. (For employees earning a base salary of more than \$125,000 but less than \$250,000, the current practice continues to be adequate, i.e., reporting all compensation and expenses but excluding pension and benefits.);
- reporting of total compensation, by category and in the aggregate, for all Executive Officers of the utility's holding company for whom compensation disclosures must be made in the holding company's proxy statement (already required for PG&E and Edison);
- disclosure of the proportion of utility or holding company Executive Officer compensation paid, directly or indirectly, by a utility's ratepayers;
- a statement explaining in plain-English all elements of compensation to utility Executive Officers and employees with a base salary of \$250,000, including the performance metrics or criteria used to determine incentive compensation;
- an independent auditor's letter verifying that all elements of total compensation have been disclosed and described (already required for PG&E), and because of tax season workload, a two-month extension in the time for submitting the report and letter, from March 31 to May 31; and
- posting on the utility's website of internet links to all public compensation documents filed at the SEC or with this Commission. (SEC link already required of PG&E and Edison.)

In addition, GO 77-M incorporates a provision adopted in D.04-08-055 and D.05-04-030, which issued in Rulemaking 03-08-019, the Commission's last review of this general order but which was not made part of the general order's formal text. The provision authorizes a utility to annually report names of highly compensated individuals in conditional access reports as long as any utility that chooses this option also files a report for public inspection from which the individual names have been redacted. The public version is available for review by members of the public without qualification.

The new reporting provisions in the amendments have been drawn, in significant part, from Commission decisions in the last general rate cases (GRCs) for PG&E and Edison and from recent SEC orders that require public disclosure of the total compensation awarded a corporation's top executives and others.

The GRC decisions require several things. D.04-05-055 directs PG&E to supplement its GO 77 report with a separate list showing the total compensation awarded to all of its officers and to those top officers of its holding company for whom compensation disclosures must be made in the holding company's proxy statement. The decision also requires PG&E to include an independent auditor's letter verifying that all elements of compensation are fully disclosed, clearly described and totally comprehensive. Further, the decision requires PG&E to include an internet site-link to all documents filed with the SEC that relate to any elements of executive compensation.<sup>22</sup> D.06-05-016 requires Edison's next GO 77 report to follow the PG&E model.

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<sup>22</sup> Ordering paragraph 12 of D.04-05-055 states:

PG&E shall file in its GO 77-K reports a separate tab listing the total compensation of the top executive officers of the utility's holding company

*Footnote continued on next page*

On July 26, 2006, the SEC voted to amend its rules governing disclosure of compensation to directors and top officers and determined to take additional comment on extending these disclosures to three other highly compensated employees. The SEC released a final version of the new disclosure rules for directors and for the principal executive officer, principal financial officer, and three other highest paid executive officers on August 11, 2006. The SEC's new rules require comprehensive tabular disclosure of total compensation for each of the past three years, including holdings of outstanding equity-related interests received as compensation that are a source of future gains, and retirement plans,

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whose compensation is listed in the holding company's proxy statement as well as the total compensation of all other utility officers. This additional information shall include not only compensation received in the prior year as now required by GO 77-K [the predecessor of GO 77-L] but also compensation awarded in the last year but not yet received, including but not limited to stock option grants. PG&E shall also include an independent auditor's letter verifying that all elements of compensation as required are fully disclosed, clearly described, and totally comprehensive. Disclosure shall include internet site links to all documents filed with the Securities and Exchange Commission that relate to any and all elements of executive compensation as required herein.

Though Ordering Paragraph 12 refers to "total compensation" (and a comprehensive definition of that term is discussed in D.04-05-055 at Section 10.3.1), GO 77 traditionally has sought disclosure of annual compensation only (e.g., salary, expense accounts, and contingent fees, excluding pension or benefits), and has not necessarily captured short- or long-term incentive payments. While Ordering Paragraph 12 clearly seeks disclosure of incentive payments, its intent to require disclosure of total compensation may have been less clear. Review indicates that PG&E's 2005 report continues to exclude pensions and benefits. Note also the directive in Edison's most recent GRC decision, D.06-05-016, that Edison not only follow the PG&E model for GO 77 reporting but also, in its next GRC "provide full transparent and understandable information on the present and future market value of the retirement severance benefits of its top executives." (D.06-05-015, Conclusion of Law 31.)

deferred compensation, and other post-employment payments and benefits. The tabular format requires reporting of the value of all components of the compensation package, as well as a single figure total. The tabular disclosure must be accompanied by a narrative disclosure, in plain English.

Respondents' workshop statements observe that the GO 77 amendments on total compensation reporting will apply to a greater number of executives and employees than the SEC rule. While true, we do not think that observation exposes an infirmity in our reporting requirements, as our regulatory purposes (e.g., ratemaking) are not identical to the SEC's. Moreover, we have limited the burden of compliance by extending the total compensation reporting requirement only to those executives and employees who receive a base salary of \$250,000 or more. Furthermore, though we maintain the objective of the staff proposal to obtain, for these individuals, a plain-English explanation of the elements of the compensation package and description of the basis for any incentive compensation awards, we have revised the text. We have deleted the stand-alone paragraph that staff proposed, rewritten the proposal to remove any normative judgment, and added the revised text to the paragraph that lists all other compensation-related disclosure requirements applicable to the large energy utilities.

We have added two requirements to the staff proposal, both based on suggestions made by Greenlining and both consistent with current practices. First, we require the GO 77 report to include an independent auditor's letter verifying that all elements of total compensation have been disclosed and properly described. PG&E is already subject to this requirement, per D.04-05-055, and D.06-05-016 recently extended the requirement to Edison. Second, recognizing that PG&E and Edison already must provide an internet-

link on their respective websites to public, compensation-related filings at the SEC, we require the major energy utilities to make the public version of the GO 77-M report available by that means as well. The additional burden should be minimal and will provide reasonable public access. We think Greenlining's suggestions that we do more are not warranted (e.g., requiring a summary of the report in notices mailed to ratepayers when rate increases are sought; requiring each major energy utility to provide in its own report, for comparison purposes, compensation information for the top officers of the others).

Finally, Greenlining asks that we open a generic proceeding, now, to examine the "indirect impacts" of executive compensation on compensation of middle managers and union employees, on morale and efficiency, and on ratepayers. We decline to do so at this time.

## **5. Motions**

Because IEP is a party to this Rulemaking already, IEP's unopposed motion for party status is moot and we take no action on it. IEP's Post-workshop Statement should be filed. We grant Respondents' unopposed motion to file the Declaration of Steven M. Fetter.

## **6. Comments on Proposed Decision**

The Proposed Decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and Rule 14.2(a) of the Commission's Rules of Practice and Procedure. We have amended the "Background and Procedural History" to list all Comments filed. The remainder of the decision has been revised after further consideration of all of the Comments. As revised, this is the Proposed Decision of Commissioner Brown.

## **7. Assignment of Proceeding**

Geoffrey F. Brown is the assigned Commissioner and Jean Vieth is the assigned ALJ in this proceeding.

### **Findings of Fact**

1. With the repeal of PUHCA, the Commission has lost the remedy of applying to the SEC for revocation of the PUHCA-exemptions formerly held by Respondent holding companies.

2. Respondents contend that our concerns about their compliance with the Affiliate Transaction Rules are speculative and that recent compliance audits do not reveal any problems. Respondents' have not accurately characterized the audit findings. Respondents also ignore California's history, which reflects serious affiliate abuse problems in the past.

3. All audits referred to herein are public documents.

4. Respondent electric and natural gas utilities exist to provide energy services in a safe, reliable and environmentally sustainable manner at the lowest reasonable cost. This fundamental principle must guide the Commission in balancing the public interest and the private interests of unregulated utility affiliates and the individuals employed within the holding company structure.

5. The staff proposals for amendment to the Affiliate Transaction Rules have been reviewed and refined to better balance the Commission's regulatory need for information and the burden of compliance.

6. The Revised Affiliate Transaction Rules are designed to close existing loopholes, primarily by ensuring that key utility and holding company officers understand the Rules and their obligations under them, providing greater security against the sharing within the corporate family, through improper conduits, of competitively-significant, confidential information, and ensuring a

utility's financial integrity is protected from the riskier market ventures of its unregulated affiliates and holding company parent.

7. The staff proposals for amendment to GO 77-L have been reviewed and refined to better balance the Commission's regulatory need for information and the burden of compliance.

8. GO 77-M has been developed to yield a more complete and accurate picture of Respondents' compensation practices while protecting reasonable privacy interests.

9. No hearing is necessary.

### **Conclusions of Law**

1. IEP's motion to become a party is moot; IEP's Post-Workshop Statement should be filed.

2. Respondents' unopposed motion for leave to file the declaration of Steven M. Fetter should be granted.

3. We may adopt rule changes in a quasi-legislative Rulemaking such as this one, as long as we provide notice and an opportunity for comment.

4. Where the Commission has not reviewed an audit in a formal proceeding and made its own findings, we may nonetheless take official notice merely to highlight the disparity between Respondents' characterizations and the findings in the audits themselves, but make no assessment of the merits.

5. As revised by today's order, the amendments to Affiliate Transaction Rules are reasonable and should be adopted.

6. As revised by today's order, the amendments to GO 77-L are reasonable and should be adopted.

**O R D E R**

**IT IS ORDERED** that:

1. The Affiliate Transaction Rules Applicable to Large California Energy Utilities, appended as Appendix A-3 to this decision, and General Order (GO) 77-M, appended as Appendix B-3 to this decision, are adopted. Both apply to Respondents (Southern California Edison Company/Edison International, Pacific Gas and Electric Company/PG&E Corporation, and Southern California Gas Company and San Diego Gas & Electric Company, both owned by Sempra Energy).
2. Within three months of the effective date of today's order, or as otherwise extended by the assigned Commissioner or assigned Administrative Law Judge and in order to avoid confusion, Commission staff shall place on the Commission's public meeting agenda a draft Rulemaking which proposes amendment of the Affiliate Transaction Rules adopted by Decision 97-12-088 as subsequently amended by other Commission decisions, for the sole purpose of exempting the large energy utilities from them. The amendments proposed shall include a cross-reference to today's order and The Affiliate Transaction Rules Applicable to Large California Energy Utilities Revised Rules.
3. The Motion of the Independent Energy Producers Association to Become a Party, filed September 29, 2006, is moot. The Post-workshop Statement attached to the Motion shall be filed as of September 29, 2006.

4. Respondent Utilities' and Holding Companies' Motion for Leave to File Declaration of Steven M. Fetter, filed September 29, 2006, is granted.

5. Rulemaking 05-10-030 is closed.

This order is effective today.

Dated December 14, 2006, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
GEOFFREY F. BROWN  
DIAN M. GRUENEICH  
JOHN A. BOHN  
RACHELLE B. CHONG  
Commissioners

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## APPENDIX A-1

### Affiliate Transaction Rules Applicable to Large California Energy Utilities

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#### I. Definitions

Unless the context otherwise requires, the following definitions govern the construction of these Rules:

- A. "Affiliate" means any person, corporation, utility, partnership, or other entity 5 per cent or more of whose outstanding securities are owned, controlled, or held with power to vote, directly or indirectly either by a utility or any of its subsidiaries, or by that utility's controlling corporation and/or any of its subsidiaries as well as any company in which the utility, its controlling corporation, or any of the utility's affiliates exert substantial control over the operation of the company and/or indirectly have substantial financial interests in the company exercised through means other than ownership. For purposes of these Rules, "substantial control" includes, but is not limited to, the possession, directly or indirectly and whether acting alone or in conjunction with others, of the authority to direct or cause the direction of the management or policies of a company. A direct or indirect voting interest of 5% or more by the utility in an entity's company creates a rebuttable presumption of control.

For purposes of this Rule, "affiliate" shall include the utility's parent or holding company, or any company which directly or indirectly owns, controls, or holds the power to vote 10% or more of the outstanding voting securities of a utility (holding company), to the extent the holding company is engaged in the provision of products or services as set out in Rule II B. However, in its compliance plan filed pursuant to Rule VI, the utility shall demonstrate both the specific mechanism and procedures that the utility and holding company have in place to assure that the utility is not utilizing the holding company or any of its affiliates not covered by these Rules as a conduit to circumvent any of these Rules. Examples include but are not limited to specific mechanisms and procedures to assure the Commission that the utility will not use the holding company, ~~or another utility affiliate not covered by these Rules,~~ or a consultant or contractor as a vehicle to (1)

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disseminate information transferred to them by the utility to an affiliate covered by these Rules in contravention of these Rules, (2) provide services to its affiliates covered by these Rules in contravention of these Rules or (3) to transfer employees to its affiliates covered by these Rules in contravention of these Rules. In the compliance plan, a corporate officer from the utility and holding company shall verify the adequacy of these specific mechanisms and procedures to ensure that the utility is not utilizing the holding company or any of its affiliates not covered by these Rules as a conduit to circumvent any of these Rules. Regulated subsidiaries of a utility, defined as subsidiaries of a utility, the revenues and expenses of which are subject to regulation by the Commission and are included by the Commission in establishing rates for the utility, are not included within the definition of affiliate. However, these Rules apply to all interactions any regulated subsidiary has with other affiliated entities covered by these rules.

- B. "Commission" means the California Public Utilities Commission or its succeeding state regulatory body.
- C. "Customer" means any person or corporation, as defined in Sections 204, 205 and 206 of the California Public Utilities Code, that is the ultimate consumer of goods and services.
- D. "Customer Information" means non-public information and data specific to a utility customer which the utility acquired or developed in the course of its provision of utility services.
- E. "FERC" means the Federal Energy Regulatory Commission.
- F. "Fully Loaded Cost" means the direct cost of good or service plus all applicable indirect charges and overheads.
- G. "Utility" means any public utility subject to the jurisdiction of the Commission as an Electrical Corporation or Gas Corporation, as defined in California Public Utilities Code Sections 218 and 222, and with gross annual operating revenues in California of \$1 billion or more.

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H. "Resource Procurement" means the investment in and the production or acquisition of the energy facilities, supplies, and ~~related other~~ energy products or services necessary for California public utility gas corporations and California public utility electrical corporations to meet their statutory obligation to serve their customers.

## II. Applicability

- A. These Rules shall apply to California public utility gas corporations and California public utility electrical corporations, subject to regulation by the California Public Utilities Commission and with gross annual operating revenues in California of \$1 billion or more.
- B. For purposes of a combined gas and electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, unless specifically exempted below. For purposes of an electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses electricity or the provision of services that relate to the use of electricity. For purposes of a gas utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or the provision of services that relate to the use of gas. However, regardless of the foregoing, where explicitly provided, these Rules also apply to a utility's parent holding company and to all of its affiliates, whether or not they engage in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity.
- C. No holding company nor any utility affiliate, whether or not engaged in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, shall knowingly:
  - ~~(1)~~ 1. \_\_\_\_\_ direct or cause a utility to violate or circumvent these Rules, including but not limited to the prohibitions against the utility providing preferential treatment, unfair competitive advantages or non-public information to its affiliates;

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~~(2)~~2. \_\_\_\_\_ knowingly aid or abet a utility's violation of these Rules; or

~~(3)~~3. \_\_\_\_\_ be used as a conduit to provide non-public information to a utility's affiliate.

- D. These Rules apply to transactions between a Commission-regulated utility and another affiliated utility, unless specifically modified by the Commission in addressing a separate application to merge or otherwise conduct joint ventures related to regulated services.
- E. These Rules do not apply to the exchange of operating information, including the disclosure of customer information to its FERC-regulated affiliate to the extent such information is required by the affiliate to schedule and confirm nominations for the interstate transportation of natural gas, between a utility and its FERC-regulated affiliate, to the extent that the affiliate operates an interstate natural gas pipeline. These Rules do not apply to transactions between an electric utility and an affiliate providing ~~transactions involving~~ broadband over power lines (BPL).
- F. **Existing Rules:** Existing Commission rules for each utility and its parent holding company shall continue to apply except to the extent they conflict with these Rules. In such cases, these Rules shall supersede prior rules and guidelines, provided that nothing herein shall supersede the Commission's regulatory framework for broadband over power lines (BPL) adopted in D. 06-04-070 nor shall preclude (1) the Commission from adopting other utility-specific guidelines; or (2) a utility or its parent holding company from adopting other utility-specific guidelines, with advance Commission approval.
- G. **Civil Relief:** These Rules shall not preclude or stay any form of civil relief, or rights or defenses thereto, that may be available under state or federal law.
- H. These Rules should be interpreted broadly, to effectuate our stated objectives of fostering competition and protecting consumer interests.

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If any provision of these Rules, or the application thereof to any person, company, or circumstance, is held invalid, the remainder of the Rules, or the application of such provision to other persons, companies, or circumstances, shall not be affected thereby.

### III. Nondiscrimination

A. **No Preferential Treatment Regarding Services Provided by the Utility:** Unless otherwise authorized by the Commission or the FERC, or permitted by these Rules, a utility shall not:

1. represent that, as a result of the affiliation with the utility, its affiliates or customers of its affiliates will receive any different treatment by the utility than the treatment the utility provides to other, unaffiliated companies or their customers; or
2. provide its affiliates, or customers of its affiliates, any preference (including but not limited to terms and conditions, pricing, or timing) over non-affiliated suppliers or their customers in the provision of services provided by the utility.

B. **Affiliate Transactions:** ~~Except for transactions provided for in Sections V D and V E (joint purchases and corporate support),~~ transactions Transactions between a utility and its affiliates shall be limited to tariffed products and services, to the ~~utility's~~ sale of goods, property, products or services made generally available by the utility or affiliate to all market participants through an open, competitive bidding process, to the provision of information made generally available by the utility to all market participants, to Commission-approved resource procurement by the utility, or ~~to transactions as provided for in Rules V D (joint purchases), V E (corporate support) and Section VII (new products and services) below.~~

1. Resource Procurement. No utility shall engage in resource procurement, as defined in these Rules, from an affiliate without prior approval from the Commission. Blind transactions between a utility and its affiliate, defined as those transactions in which neither party knows the identity of the counterparty until the transaction is consummated, are exempted from this Rule. A transaction shall be

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deemed to have prior Commission approval (a) before the effective date of this Rule, if authorized by the Commission specifically or through the delegation of authority to Commission staff or (b) after the effective date of this Rule, if authorized by the Commission generally or specifically or through the delegation of authority to Commission staff.

**2. Provision of Supply, Capacity, Services or Information:** Except as provided for in ~~Sections~~Rules V D, V E, and VII, a utility shall provide access to utility information, services, and unused capacity or supply on the same terms for all similarly situated market participants. If a utility provides supply, capacity, services, or information to its affiliate(s), it shall contemporaneously make the offering available to all similarly situated market participants, which include all competitors serving the same market as the utility's affiliates.

**3. Offering of Discounts:** Except when made generally available by the utility through an open, competitive bidding process, if a utility offers a discount or waives all or any part of any other charge or fee to its affiliates, or offers a discount or waiver for a transaction in which its affiliates are involved, the utility shall contemporaneously make such discount or waiver available to all similarly situated market participants. The utilities should not use the "similarly situated" qualification to create such a unique discount arrangement with their affiliates such that no competitor could be considered similarly situated. All competitors serving the same market as the utility's affiliates should be offered the same discount as the discount received by the affiliates. A utility shall document the cost differential underlying the discount to its affiliates in the affiliate discount report described in Rule III F 7 below.

**4. Tariff Discretion:** If a tariff provision allows for discretion in its application, a utility shall apply that tariff provision in the same manner to its affiliates and other market participants and their respective customers.

**5. No Tariff Discretion:** If a utility has no discretion in the application of a tariff provision, the utility shall strictly enforce that tariff provision.

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**6. Processing Requests for Services Provided by the Utility:** A utility shall process requests for similar services provided by the utility in the same manner and within the same time for its affiliates and for all other market participants and their respective customers.

**C. Tying of Services Provided by a Utility Prohibited:** A utility shall not condition or otherwise tie the provision of any services provided by the utility, nor the availability of discounts of rates or other charges or fees, rebates, or waivers of terms and conditions of any services provided by the utility, to the taking of any goods or services from its affiliates.

**D. No Assignment of Customers:** A utility shall not assign customers to which it currently provides services to any of its affiliates, whether by default, direct assignment, option or by any other means, unless that means is equally available to all competitors.

**E. Business Development and Customer Relations:** Except as otherwise provided by these Rules, a utility shall not:

1. provide leads to its affiliates;
2. solicit business on behalf of its affiliates;
3. acquire information on behalf of or to provide to its affiliates;
4. share market analysis reports or any other types of proprietary or nonpublicly available reports, including but not limited to market, forecast, planning or strategic reports, with its affiliates;
5. request authorization from its customers to pass on customer information exclusively to its affiliates;
6. give the appearance that the utility speaks on behalf of its affiliates or that the customer will receive preferential treatment as a consequence of conducting business with the affiliates; or
7. give any appearance that the affiliate speaks on behalf of the utility.

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**F. Affiliate Discount Reports:** If a utility provides its affiliates a discount, rebate, or other waiver of any charge or fee associated with products or services provided by the utility, the utility shall, within 24 hours of the time at which the product or service provided by the utility is so provided, post a notice on its electronic bulletin board providing the following information:

1. the name of the affiliate involved in the transaction;
2. the rate charged;
3. the maximum rate;
4. the time period for which the discount or waiver applies;
5. the quantities involved in the transaction;
6. the delivery points involved in the transaction;
7. any conditions or requirements applicable to the discount or waiver, and a documentation of the cost differential underlying the discount as required in Rule III B 2 above; and
8. procedures by which a nonaffiliated entity may request a comparable offer.

A utility that provides an affiliate a discounted rate, rebate, or other waiver of a charge or fee associated with services provided by the utility shall maintain, for each billing period, the following information:

9. the name of the entity being provided services provided by the utility in the transaction;
10. the affiliate's role in the transaction (i.e., shipper, marketer, supplier, seller);
11. the duration of the discount or waiver;
12. the maximum rate;

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13. the rate or fee actually charged during the billing period; and
14. the quantity of products or services scheduled at the discounted rate during the billing period for each delivery point.

All records maintained pursuant to this provision shall also conform to FERC rules where applicable.

### IV. Disclosure and Information

A. **Customer Information:** A utility shall provide customer information to its affiliates and unaffiliated entities on a strictly non-discriminatory basis, and only with prior affirmative customer written consent.

B. **Non-Customer Specific Non-Public Information:** A utility shall make non-customer specific non-public information, including but not limited to information about a utility's natural gas or electricity purchases, sales, or operations or about the utility's gas-related goods or services and electricity-related goods or services, available to the utility's affiliates only if the utility makes that information contemporaneously available to all other service providers on the same terms and conditions, and keeps the information open to public inspection. Unless otherwise provided by these Rules, a utility continues to be bound by all Commission-adopted pricing and reporting guidelines for such transactions. A utility is also permitted to exchange proprietary information on an exclusive basis with its affiliates, provided the utility follows all Commission-adopted pricing and reporting guidelines for such transactions, and it is necessary to exchange this information in the provision of the corporate support services permitted by Rule V E below. The affiliate's use of such proprietary information is limited to use in conjunction with the permitted corporate support services, and is not permitted for any other use. Nothing in this Rule precludes the exchange of information pursuant to D.97-10-031. Nothing in this Rule is intended to limit the Commission's right to information under Public Utilities Code Sections 314 and 581.

~~C. Information a Utility Must Provide to the Commission: Except for information exchanged in the provision of corporate support services~~

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~~permitted by Rule V E below, a utility shall report to the Commission, on a semi-annual basis, any exchange of or discussion about non-public information between employees, consultants, or agents of the utility and employees, consultants, or agents of the utility's parent holding company or any affiliates, whether in person or by other means, if the non-public information concerns:~~

- ~~1. information supplied to the utility from a competitor of the utility's affiliate;~~
- ~~2. negotiations between the utility and a competitor of its affiliate;~~
- ~~3. utility procurement plans for electricity or natural gas, which could include procurement from an affiliate;~~
- ~~4. the utility's operational matters, which could materially affect the utility's affiliate(s) and its competitors;~~
- ~~5. expansion plans of the utility; or~~
- ~~6. the utility affiliate's competition or potential competition with other entities.~~

~~The report shall be provided to the Directors of the Commission's Energy Division and Division of Ratepayer Advocates and shall disclose: the date and place of the exchange or discussion; the names and positions of the people who communicated or received the information; and the nature of the information. The utility shall also retain, for a minimum of three years, copies of any document or other records in its possession or control pertaining to all such exchanges or discussions. The utility shall provide copies of the retained documents or other records upon the request of the Commission or its staff, whether or not in the context of a pending proceeding. Reports and retained documents may be submitted confidentially pursuant to California Public Utilities Code Section 583 and the Commission's General Order 66-C.~~

DC. **Service Provider Information:** Except upon request by a customer or as otherwise authorized by the Commission, or ~~approved by~~ another governmental body, a utility shall not provide its customers with any list of service providers, which includes or identifies the utility's affiliates,

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regardless of whether such list also includes or identifies the names of unaffiliated entities.

~~E~~D. **Supplier Information:** A utility may provide non-public information and data which has been received from unaffiliated suppliers to its affiliates or non-affiliated entities only if the utility first obtains written affirmative authorization to do so from the supplier. A utility shall not actively solicit the release of such information exclusively to its own affiliate in an effort to keep such information from other unaffiliated entities.

~~F~~E. **Affiliate-Related Advice or Assistance:** Except as otherwise provided in these Rules, a utility shall not offer or provide customers advice or assistance with regard to its affiliates or other service providers.

~~G~~F. **Record-Keeping:** A utility shall maintain contemporaneous records documenting all tariffed and nontariffed transactions with its affiliates, including but not limited to, all waivers of tariff or contract provisions, ~~and~~ all discounts, and all negotiations of any sort between the utility and its affiliate whether or not they are consummated. A utility shall maintain such records for a minimum of three years and longer if this Commission or another government agency so requires. For consummated transactions, ~~the utility shall make such records~~ final transaction documents available for third party review upon 72 hours' notice, or at a time mutually agreeable to the utility and third party.

If D.97-06-110 is applicable to the information the utility seeks to protect, the utility should follow the procedure set forth in D.97-06-110, except that the utility should serve the third party making the request in a manner that the third party receives the utility's D.97-06-110 request for confidentiality within 24 hours of service.

~~H~~G. **Maintenance of Affiliate Contracts and Related Bids:** A utility shall maintain a record of all contracts and related bids for the provision of work, products or services between the utility and its affiliates for no less than a period of three years, and longer if this Commission or another government agency so requires.

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**II. FERC Reporting Requirements:** To the extent that reporting rules imposed by the FERC require more detailed information or more expeditious reporting, nothing in these Rules shall be construed as modifying the FERC rules.

## V. Separation

- A. **Corporate Entities:** A utility, its parent holding company, and its affiliates shall be separate corporate entities.
- B. **Books and Records:** A utility, its parent holding company, and its affiliates shall keep separate books and records.
  1. Utility books and records shall be kept in accordance with applicable Uniform System of Accounts (USOA) and Generally Accepted Accounting Procedures (GAAP).
  2. The books and records of ~~the utilities'~~ a utility's parent holding ~~companies~~ company and affiliates shall be open for examination by the Commission and its staff consistent with the provisions of Public Utilities Code Sections 314 and 701, the conditions in the Commission's orders authorizing the utilities' holding companies and/or mergers and these Rules.
- C. **Sharing of Plant, Facilities, Equipment or Costs:** A utility shall not share office space, office equipment, services, and systems with its affiliates, nor shall a utility access the computer or information systems of its affiliates or allow its affiliates to access its computer or information systems, except to the extent appropriate to perform shared corporate support functions permitted under ~~Section~~ Rule V E of these Rules. Physical separation required by this rule shall be accomplished preferably by having office space in a separate building, or, in the alternative, through the use of separate elevator banks and/or security-controlled access. This provision does not preclude a utility from offering a joint service provided this service is authorized by the Commission and is available to all non-affiliated service providers on the same terms and conditions (e.g., joint billing services pursuant to D.97-05-039).

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D. **Joint Purchases:** To the extent not precluded by any other Rule, the utilities and their affiliates may make joint purchases of good and services, but not those associated with the traditional utility merchant function. For purpose of these Rules, to the extent that a utility is engaged in the marketing of the commodity of electricity or natural gas to customers, as opposed to the marketing of transmission and distribution services, it is engaging in merchant functions. Examples of permissible joint purchases include joint purchases of office supplies and telephone services. Examples of joint purchases not permitted include gas and electric purchasing for resale, purchasing of gas transportation and storage capacity, purchasing of electric transmission, systems operations, and marketing. The utility must insure that all joint purchases are priced, reported, and conducted in a manner that permits clear identification of the utility and affiliate portions of such purchases, and in accordance with applicable Commission allocation and reporting rules.

E. **Corporate Support:** As a general principle, a utility, its parent holding company, or a separate affiliate created solely to perform corporate support services may share with its affiliates ~~only~~ joint corporate oversight, governance, support systems and personnel, as further specified below. Any shared support shall be priced, reported and conducted in accordance with the Separation and Information Standards set forth herein, as well as other applicable Commission pricing and reporting requirements.

As a general principle, sSuch joint utilization shall not allow or provide a means for the transfer of confidential information from the utility to the affiliate, create the opportunity for preferential treatment or unfair competitive advantage, lead to customer confusion, or create significant opportunities for cross-subsidization of affiliates. In the compliance plan, a corporate officer from the utility and holding company shall verify the adequacy of the specific mechanisms and procedures in place to ensure the utility follows the mandates of this paragraph, and to ensure the utility is not utilizing joint corporate support services as a conduit to circumvent these Rules.

Examples of services that may be shared include: payroll, taxes, shareholder services, insurance, ~~cash management, banking relations,~~

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~~communications with rating agencies,~~ financial reporting, financial planning and analysis, corporate accounting, corporate security, human resources (compensation, benefits, ~~and~~ employment policies), employee records, regulatory affairs, lobbying, legal, and pension and trust management, ~~and corporate compliance with these Rules.~~ However, if a utility and its parent holding company share any key officers after 180 days following the effective date of the decision adopting these Rule modifications, then the following services shall no longer be shared: regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services still authorized. For purposes of this Rule, key officers are the Chair of the entire corporate enterprise, the President at the utility and at its holding company parent, the chief executive officer at each, the chief financial officer at each, and the chief regulatory officer at each, or in each case, any and all officers whose responsibilities are the functional equivalent of the foregoing.

Examples of services that may not be shared include: employee recruiting, engineering, ~~regulatory affairs, lobbying, risk management (including hedging and financial derivatives and arbitrage services),~~ gas ~~and~~ or electric purchasing for resale, purchasing of gas transportation ~~and~~ or storage capacity, purchasing of electric transmission, system operations, and marketing. However, if a utility and its parent holding company share any key officers (as defined in the preceding paragraph) after 180 days following the effective date of the decision adopting these Rule modifications, then the following services shall no longer be shared: regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services still expressly authorized by the preceding paragraph.

### F. Corporate Identification and Advertising:

1. A utility shall not trade upon, promote, or advertise its affiliate's affiliation with the utility, nor allow the utility name or logo to be used by the affiliate or in any material circulated by the affiliate, unless it discloses in plain legible or audible language, on the first page or at the first point where the utility name or logo appears that:

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a. the affiliate "is not the same company as [i.e. PG&E, Edison, the Gas Company, etc.], the utility,";

b. the affiliate is not regulated by the California Public Utilities Commission; and

c. "you do not have to buy [the affiliate's] products in order to continue to receive quality regulated services from the utility."  
The application of the name/logo disclaimer is limited to the use of the name or logo in California.

2. A utility, through action or words, shall not represent that, as a result of the affiliate's affiliation with the utility, its affiliates will receive any different treatment than other service providers.

3. A utility shall not offer or provide to its affiliates advertising space in utility billing envelopes or any other form of utility customer written communication unless it provides access to all other unaffiliated service providers on the same terms and conditions.

4. A utility shall not participate in joint advertising or joint marketing with its affiliates. This prohibition means that utilities may not engage in activities which include, but are not limited to the following:

a. A utility shall not participate with its affiliates in joint sales calls, through joint call centers or otherwise, or joint proposals (including responses to requests for proposals (RFPs)) to existing or potential customers. At a customer's unsolicited request, a utility may participate, on a nondiscriminatory basis, in non-sales meetings with its affiliates or any other market participant to discuss technical or operational subjects regarding the utility's provision of transportation service to the customer;

b. Except as otherwise provided for by these Rules, a utility shall not participate in any joint activity with its affiliates. The term "joint activities" includes, but is not limited to, advertising, sales, marketing, communications and correspondence with any existing or potential customer;

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c. A utility shall not participate with its affiliates in trade shows, conferences, or other information or marketing events held in California.

5. A utility shall not share or subsidize costs, fees, or payments with its affiliates associated with research and development activities or investment in advanced technology research.

### G. Employees:

1. Except as permitted in ~~Section~~ Rule V E (corporate support), a utility and its affiliates shall not jointly employ the same employees, ~~consultants, and contractors. However, auditors and providers of accounting services shall not be considered consultants or contractors for purposes of this Rule.~~ This Rule prohibiting joint employees also applies to Board Directors, and corporate officers except for the following circumstances: In instances when this Rule is applicable to holding companies, any board member or corporate officer may serve on the holding company and with either the utility or affiliate (but not both) to the extent consistent with Rule V E (corporate support). Where the utility is a multi-state utility, is not a member of a holding company structure, and assumes the corporate governance functions for the affiliates, the prohibition against any board member or corporate officer of the utility also serving as a board member or corporate officer of an affiliate shall only apply to affiliates that operate within California. In the case of shared directors and officers, a corporate officer from the utility and holding company shall describe and verify in the utility's compliance plan required ~~by~~ in Rule VI the adequacy of the specific mechanisms and procedures in place to ensure that the utility is not utilizing shared officers and directors as a conduit to circumvent any of these Rules. In its compliance plan, the utility shall list all shared directors and officers between the utility and affiliates. No later than 30 days following a change to this list, the utility shall notify the Commission's Energy Division and the parties on the service list of R.97-04-011/I.97-04-012 of any change to this list. ~~A utility may apply for additional exceptions to this Rule.~~
2. All employee movement between a utility and its affiliates shall be consistent with the following provisions:

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a. A utility shall track and report to the Commission all employee movement between the utility and affiliates. The utility shall report this information annually pursuant to our Affiliate Transaction Reporting Decision, D.93-02-016, 48 CPUC2d 163, 171-172 and 180 (Appendix A, Section I and Section II H.).

b. Once an employee of a utility becomes an employee of an affiliate, the employee may not return to the utility for a period of one year. This Rule is inapplicable if the affiliate to which the employee transfers goes out of business during the one-year period. In the event that such an employee returns to the utility, such employee cannot be retransferred, reassigned, or otherwise employed by the affiliate for a period of two years. Employees transferring from the utility to the affiliate are expressly prohibited from using information gained from the utility in a discriminatory or exclusive fashion, to the benefit of the affiliate or to the detriment of other unaffiliated service providers.

c. When an employee of a utility is transferred, assigned, or otherwise employed by the affiliate, the affiliate shall make a one-time payment to the utility in an amount equivalent to 25% of the employee's base annual compensation, unless the utility can demonstrate that some lesser percentage (equal to at least 15%) is appropriate for the class of employee included. In the limited case where a rank-and-file (non-executive) employee's position is eliminated as a result of electric industry restructuring, a utility may demonstrate that no fee or a lesser percentage than 15% is appropriate. All such fees paid to the utility shall be accounted for in a separate memorandum account to track them for future ratemaking treatment (i.e. credited to the Electric Revenue Adjustment Account or the Core and Noncore Gas Fixed Cost Accounts, or other ratemaking treatment, as appropriate), on an annual basis, or as otherwise necessary to ensure that the utility's ratepayers receive the fees. This transfer payment provision will not apply to clerical workers. Nor will it apply to the initial transfer of employees to the utility's holding company to perform corporate support functions or to a separate affiliate performing corporate support functions, provided that that transfer is made during the initial implementation period of these rules or pursuant to a § 851 application or other Commission proceeding. However, the rule will

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apply to any subsequent transfers or assignments between a utility and its affiliates of all covered employees at a later time.

d. Any utility employee hired by an affiliate shall not remove or otherwise provide information to the affiliate which the affiliate would otherwise be precluded from having pursuant to these Rules.

e. A utility shall not make temporary or intermittent assignments, or rotations to its energy marketing affiliates. Utility employees not involved in marketing may be used on a temporary basis (less than 30% of an employee's chargeable time in any calendar year) by affiliates not engaged in energy marketing only if:

i. All such use is documented, priced and reported in accordance with these Rules and existing Commission reporting requirements, except that when the affiliate obtains the services of a non-executive employee, compensation to the utility should be priced at a minimum of the greater of fully loaded cost plus 10% of direct labor cost, or fair market value. When the affiliate obtains the services of an executive employee, compensation to the utility should be priced at a minimum of the greater of fully loaded cost plus 15% of direct labor cost, or fair market value.

ii. Utility needs for utility employees always take priority over any affiliate requests;

iii. No more than 5% of full time equivalent utility employees may be on loan at a given time;

iv. Utility employees agree, in writing, that they will abide by these Affiliate Transaction Rules; and

v. Affiliate use of utility employees must be conducted pursuant to a written agreement approved by appropriate utility and affiliate officers.

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**H. Transfer of Goods and Services:** To the extent that these Rules do not prohibit transfers of goods and services between a utility and its affiliates, and except for as provided by Rule V.G.2.e, all such transfers shall be subject to the following pricing provisions:

1. Transfers from the utility to its affiliates of goods and services produced, purchased or developed for sale on the open market by the utility will be priced at fair market value.
2. Transfers from an affiliate to the utility of goods and services produced, purchased or developed for sale on the open market by the affiliate shall be priced at no more than fair market value.
3. For goods or services for which the price is regulated by a state or federal agency, that price shall be deemed to be the fair market value, except that in cases where more than one state commission regulates the price of goods or services, this Commission's pricing provisions govern.
4. Goods and services produced, purchased or developed for sale on the open market by the utility will be provided to its affiliates and unaffiliated companies on a nondiscriminatory basis, except as otherwise required or permitted by these Rules or applicable law.
5. Transfers from the utility to its affiliates of goods and services not produced, purchased or developed for sale by the utility will be priced at fully loaded cost plus 5% of direct labor cost.
6. Transfers from an affiliate to the utility of goods and services not produced, purchased or developed for sale by the affiliate will be priced at the lower of fully loaded cost or fair market value.

## VI. Regulatory Oversight

**A. Compliance Plans:** No later than June 30, 2007, each utility shall file a compliance plan by advice letter with the Energy Division of the Commission. The compliance plan shall include:

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1. A list of all affiliates of the utility, as defined in Rule I A of these Rules, and for each affiliate, its purpose or activities, and whether the utility claims that Rule II B makes these Rules applicable to the affiliate;
2. A ~~comprehensive demonstration to of the Commission that there are~~ adequate procedures in place ~~that will ensure~~ to assure compliance with these Rules.

The utility's compliance plan shall be in effect between the filing and a Commission determination of the advice letter. A utility shall file a compliance plan annually thereafter by advice letter where there is some change in the compliance plan (i.e., when there has been a change in the purpose or activities of an affiliate, a new affiliate has been created, or the utility has changed the compliance plan for any other reason).

**B. New Affiliate Compliance Plans:** Upon the creation of a new affiliate the utility shall immediately notify the Commission of the creation of the new affiliate, as well as posting notice on its electronic bulletin board. No later than 60 days after the creation of this affiliate, the utility shall file an advice letter with the Energy Division of the Commission. The advice letter shall state the affiliate's purpose or activities, whether the utility claims that Rule II B makes these Rules applicable to the affiliate, and shall include a ~~comprehensive demonstration to~~ the Commission that there are adequate procedures in place that will ensure compliance with these Rules.

**C. Affiliate Audit:** The Commission's Energy Division shall have audits performed biennially by independent auditors. The audits shall ~~that~~ cover the last two each calendar years which ends on December 31, and shall ~~that~~ verify that the utility is in compliance with the Rules set forth herein. The Energy Division shall post the audit reports on the Commission's web site. The audits shall be at shareholder expense.

**D. Witness Availability:** Affiliate officers and employees shall be made available to testify before the Commission as necessary or required, without subpoena, consistent with the provisions of Public Utilities Code Sections 314 and 701, the conditions in the Commission's orders authorizing the utilities' holding companies and/or mergers and these Rules.



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4. "Tariff" or "tariffed" refers to rates, terms and conditions of services as approved by this Commission or the Federal Energy Regulatory Commission (FERC), whether by traditional tariff, approved contract or other such approval process as the Commission or the FERC may deem appropriate.

**C. Utility Products and Services:** Except as provided in these Rules, a utility shall not offer nontariffed products and services. In no event shall a utility offer natural gas or electricity commodity service on a nontariffed basis. A utility may only offer for sale the following products and services:

1. Existing products and services offered by the utility pursuant to tariff;
2. Unbundled versions of existing utility products and services, with the unbundled versions being offered on a tariffed basis;
3. New products and services that are offered on a tariffed basis; and
4. Products and services which are offered on a nontariffed basis and which meet the following conditions:
  - a. The nontariffed product or service utilizes a portion of a utility asset or capacity;
  - b. such asset or capacity has been acquired for the purpose of and is necessary and useful in providing tariffed utility services;
  - c. the involved portion of such asset or capacity may be used to offer the product or service on a nontariffed basis without adversely affecting the cost, quality or reliability of tariffed utility products and services;
  - d. the products and services can be marketed with minimal or no incremental ratepayer capital, minimal or no new forms of liability or business risk being incurred by utility ratepayers, and no undue diversion of utility management attention; and
  - e. The utility's offering of such nontariffed product or service does not violate any law, regulation, or Commission policy regarding anticompetitive practices.

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**D. Conditions Precedent to Offering New Products and Services:** This Rule does not represent an endorsement by the Commission of any particular nontariffed utility product or service. A utility may offer new nontariffed products and services only if the Commission has adopted and the utility has established:

1. A mechanism or accounting standard for allocating costs to each new product or service to prevent cross-subsidization between services a utility would continue to provide on a tariffed basis and those it would provide on a nontariffed basis;
2. A reasonable mechanism for treatment of benefits and revenues derived from offering such products and services, except that in the event the Commission has already approved a performance-based ratemaking mechanism for the utility and the utility seeks a different sharing mechanism, the utility should petition to modify the performance-based ratemaking decision if it wishes to alter the sharing mechanism, or clearly justify why this procedure is inappropriate, rather than doing so by application or other vehicle.
3. Periodic reporting requirements regarding pertinent information related to nontariffed products and services; and
4. Periodic auditing of the costs allocated to and the revenues derived from nontariffed products and services.

**E. Requirement to File an Advice Letter:** Prior to offering a new category of nontariffed products or services as set forth in ~~Section~~ Rule VII C above, a utility shall file an advice letter in compliance with the following provisions of this paragraph.

1. The advice letter shall:
  - a. demonstrate compliance with these rules;
  - b. address the amount of utility assets dedicated to the non-utility venture, in order to ensure that a given product or service does not threaten the provision of utility service, and show that the new product or service will not result in a degradation of cost, quality, or reliability of tariffed goods and services;

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- c. address the potential impact of the new product or service on competition in the relevant market including but not limited to the degree in which the relevant market is already competitive in nature and the degree to which the new category of products or services is projected to affect that market.
    - d. be served on the service list of Rulemaking 97-04-011/Investigation 97-04-012, as well as on any other party appropriately designated by the rules governing the Commission's advice letter process.
  2. For categories of nontariffed products or services targeted and offered to less than 1% of the number of customers in the utility's customer base, in the absence of a protest alleging non-compliance with these Rules or any law, regulation, decision, or Commission policy, or allegations of harm, the utility may commence offering the product or service 30 days after submission of the advice letter. For categories of nontariffed products or services targeted and offered to 1% or more of the number of customers in the utility's customer base, the utility may commence offering the product or service after the Commission approves the advice letter through the normal advice letter process.
  3. A protest of an advice letter filed in accordance with this paragraph shall include:
    - a. An explanation of the specific Rules, or any law, regulation, decision, or Commission policy the utility will allegedly violate by offering the proposed product or service, with reasonable factual detail; or
    - b. An explanation of the specific harm the protestant will allegedly suffer.
  4. If such a protest is filed, the utility may file a motion to dismiss the protest within 5 working days if it believes the protestant has failed to provide the minimum grounds for protest required above. The protestant has 5 working days to respond to the motion.

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5. The intention of the Commission is to make its best reasonable efforts to rule on such a motion to dismiss promptly. Absent a ruling granting a motion to dismiss, the utility shall begin offering that category of products and services only after Commission approval through the normal advice letter process.

**F. Existing Offerings:** Unless and until further Commission order to the contrary as a result of the advice letter filing or otherwise, a utility that is offering tariffed or nontariffed products and services, as of the effective date of this decision, may continue to offer such products and services, provided that the utility complies with the cost allocation and reporting requirements in this rule. No later than January 30, ~~2007~~1998, each utility shall submit an advice letter describing the existing products and services (both tariffed and nontariffed) currently being offered by the utility and the number of the Commission decision or advice letter approving this offering, if any, and requesting authorization or continuing authorization for the utility's continued provision of this product or service in compliance with the criteria set forth in Rule VII. This requirement applies to both existing products and services explicitly approved and not explicitly approved by the Commission.

**G. Section 851 Application:** A utility must continue to comply fully with the provisions of Public Utilities Code Section 851 when necessary or useful utility property is sold, leased, assigned, mortgaged, disposed of, or otherwise encumbered as part of a nontariffed product or service offering by the utility. If an application pursuant to Section 851 is submitted, the utility need not file a separate advice letter, but shall include in the application those items which would otherwise appear in the advice letter as required in this Rule.

**H. Periodic Reporting of Nontariffed Products and Services:** Any utility offering nontariffed products and services shall file periodic reports with the Commission's Energy Division twice annually for the first two years following the effective date of these Rules, then annually thereafter unless otherwise directed by the Commission. The utility shall serve periodic reports on the service list of this proceeding. The periodic reports shall contain the following information:

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1. A description of each existing or new category of nontariffed products and services and the authority under which it is offered;
2. A description of the types and quantities of products and services contained within each category (so that, for example, "leases for agricultural nurseries at 15 sites" might be listed under the category "leases of land under utility transmission lines," although the utility would not be required to provide the details regarding each individual lease);
3. The ~~total and marginal~~ costs allocated to and revenues derived from each category;
4. Current information on the proportion of relevant utility assets used to offer each category of product and service.
5. ~~A showing that the provision of each product and service provides additional value to the utility, the ratepayers, and to customers in the relevant market.~~

**I. Offering of Nontariffed Products and Services to Affiliates:** Nontariffed products and services which are allowed by this Rule may be offered to utility affiliates only in compliance with all other provisions of these Affiliate Rules. Similarly, this Rule does not prohibit affiliate transactions which are otherwise allowed by all other provisions of these Affiliate Rules.

**VIII. Complaint Procedures and Remedies** (adopted by D.98-12-075) – insert these here

## **IX. Protecting the Utility's Financial Health**

**A. Information from Utility on Necessary Capital.** Each utility shall provide to the Commission on the last business day of November of each year a report with the following information:

1. the utility's estimate of investment capital needed to build or acquire long-term assets (i.e., greater than one year), such as operating assets and utility infrastructure, over each of the next five years;
2. the utility's estimate of capital needed to meet resource procurement goals over each of the next five years;

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3. the utility's policies concerning dividends, stock repurchase and retention of capital for each year;
4. the names of individuals involved in deciding corporate policies for the utility's dividends, stock repurchase and retention of capital;
5. the process by which corporate policies concerning dividends, stock repurchase and retention of capital are implemented; and
6. how the utility expects or intends to meet its investment capital needs.

### B. **Restrictions on Deviations from Authorized Capital Structure.**

A utility shall maintain a balanced capital structure consistent with that determined to be reasonable by the Commission in its most recent decision on the utility's capital structure. The utility's equity shall be retained such that the Commission's adopted capital structure shall be maintained on average over the period the capital structure is in effect for ratemaking purposes. Provided, however, that ~~the a~~ utility shall file an application for a waiver ~~from this condition~~, on a case by case basis and in a timely manner, of this Rule if an adverse financial event at the utility reduces the utility's equity ratio by 1% or more. In order to assure that regulatory staff has adequate time to review and assess the application and to permit the consideration of all relevant facts, ~~The utility shall not be considered in violation of this Rule during the period the time that its advice letter or application for a waiver is pending resolution.~~ Nothing in this provision creates a presumption of either reasonableness or unreasonableness of the utility's actions which may have caused the adverse financial event.

C. **Ring-Fencing.** Within three months of the effective date of the decision adopting this amendment to the Rules, a utility shall obtain a non-consolidation opinion that demonstrates that the ring fencing around the utility is sufficient to prevent the utility from being pulled into bankruptcy of its parent holding company. The utility shall promptly provide the opinion to the Commission. If the current ring-fencing provisions are insufficient to obtain a non-consolidation opinion, the utility shall promptly undertake the following actions:

1. notify the Commission of the inability to obtain a non-consolidation opinion;

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2. propose and implement, upon Commission approval, such ring-fencing provisions that are sufficient to prevent the utility from being pulled into the bankruptcy of its parent holding company; and then

3. obtain a non-consolidation opinion.

D. Changes to Ring-Fencing Provisions. A utility shall notify the Commission of any changes made to its ring-fencing provisions within 30 days. ~~Such notice shall include verification that:~~

- ~~1. the change has been approved by the utility's independent director; and~~
- ~~2. the rating agencies have confirmed that there will be no credit downgrade from the changed ring-fencing protections.~~

(END OF APPENDIX A-1)

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## APPENDIX A-2

### Affiliate Transaction Rules Applicable to Large Energy Utilities

#### Table of Contents – insert this here

#### **I. Definitions**

Unless the context otherwise requires, the following definitions govern the construction of these Rules:

- A. **“Affiliate”** means any person, corporation, utility, partnership, or other entity 5 per cent or more of whose outstanding securities are owned, controlled, or held with power to vote, directly or indirectly either by a utility or any of its subsidiaries, or by that utility’s controlling corporation and/or any of its subsidiaries as well as any company in which the utility, its controlling corporation, or any of the utility’s affiliates exert substantial control over the operation of the company and/or indirectly have substantial financial interests in the company exercised through means other than ownership. For purposes of these Rules, “substantial control” includes, but is not limited to, the possession, directly or indirectly and whether acting alone or in conjunction with others, of the authority to direct or cause the direction of the management or policies of a company. A direct or indirect voting interest of 5% or more by the utility in an entity’s company creates a rebuttable presumption of control.

For purposes of this Rule, “affiliate” shall include the utility’s parent or holding company, or any company which directly or indirectly owns, controls, or holds the power to vote 10% or more of the outstanding voting securities of a utility (holding company), to the extent the holding company is engaged in the provision of products or services as set out in Rule II B. However, in its compliance plan filed pursuant to Rule VI, the utility shall demonstrate both the specific mechanism and procedures that the utility and holding company have in place to assure that the utility is not utilizing the holding company or any of its affiliates not covered by these Rules as a conduit to circumvent any of these Rules. Examples include but are not limited to specific mechanisms and procedures to assure the Commission that the utility will not use the holding company, ~~or~~ another utility affiliate not

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covered by these Rules, or a consultant or contractor as a vehicle to (1) disseminate information transferred to them by the utility to an affiliate covered by these Rules in contravention of these Rules, (2) provide services to its affiliates covered by these Rules in contravention of these Rules or (3) to transfer employees to its affiliates covered by these Rules in contravention of these Rules. In the compliance plan, a corporate officer from the utility and holding company shall verify the adequacy of these specific mechanisms and procedures to ensure that the utility is not utilizing the holding company or any of its affiliates not covered by these Rules as a conduit to circumvent any of these Rules. Regulated subsidiaries of a utility, defined as subsidiaries of a utility, the revenues and expenses of which are subject to regulation by the Commission and are included by the Commission in establishing rates for the utility, are not included within the definition of affiliate. However, these Rules apply to all interactions any regulated subsidiary has with other affiliated entities covered by these rules.

- B. **"Commission"** means the California Public Utilities Commission or its succeeding state regulatory body.
- C. **"Customer"** means any person or corporation, as defined in Sections 204, 205 and 206 of the California Public Utilities Code, that is the ultimate consumer of goods and services.
- D. **"Customer Information"** means non-public information and data specific to a utility customer which the utility acquired or developed in the course of its provision of utility services.
- E. **"FERC"** means the Federal Energy Regulatory Commission.
- F. **"Fully Loaded Cost"** means the direct cost of good or service plus all applicable indirect charges and overheads.
- G. **"Utility"** means any public utility subject to the jurisdiction of the Commission as an Electrical Corporation or Gas Corporation, as defined in California Public Utilities Code Sections 218 and 222, and

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with gross annual operating revenues in California of \$1 billion or more.

H. **"Resource Procurement"** means the investment in and the production or acquisition of the energy facilities, supplies, and other energy products or services necessary for California public utility gas corporations and California public utility electrical corporations to meet their statutory obligation to serve their customers.

## II. Applicability

- A. These Rules shall apply to California public utility gas corporations and California public utility electrical corporations, subject to regulation by the California Public Utilities Commission and with gross annual operating revenues in California of \$1 billion or more.
- B. For purposes of a combined gas and electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, unless specifically exempted below. For purposes of an electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses electricity or the provision of services that relate to the use of electricity. For purposes of a gas utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or the provision of services that relate to the use of gas. However, regardless of the foregoing, where explicitly provided, these Rules also apply to a utility's parent holding company and to all of its affiliates, whether or not they engage in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity.
- C. No holding company nor any utility affiliate, whether or not engaged in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, shall knowingly:

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(1) direct or cause a utility to violate or circumvent these Rules, including but not limited to the prohibitions against the utility providing preferential treatment, unfair competitive advantages or non-public information to its affiliates;

(2) aid or abet a utility's violation of these Rules; or

(3) be used as a conduit to provide non-public information to a utility's affiliate.

D. These Rules apply to transactions between a Commission-regulated utility and another affiliated utility, unless specifically modified by the Commission in addressing a separate application to merge or otherwise conduct joint ventures related to regulated services.

~~E~~D. These ~~R~~rules do not apply to the exchange of operating information, including the disclosure of customer information to its FERC-regulated affiliate to the extent such information is required by the affiliate to schedule and confirm nominations for the interstate transportation of natural gas, between a utility and its FERC-regulated affiliate, to the extent that the affiliate operates an interstate natural gas pipeline. These Rules do not apply to transactions between an electric utility and an affiliate providing broadband over power lines (BPL).

~~F~~E. **Existing Rules:** Existing Commission rules for each utility and its parent holding company shall continue to apply except to the extent they conflict with these Rules. In such cases, these Rules shall supersede prior rules and guidelines, provided that nothing herein shall supersede the Commission's regulatory framework for broadband over power lines (BPL) adopted in D. 06-04-070 nor shall preclude (1) the Commission from adopting other utility-specific guidelines; or (2) a utility or its parent holding company from adopting other utility-specific guidelines, with advance Commission approval.

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~~GF. Civil Relief:~~ These Rules shall not preclude or stay any form of civil relief, or rights or defenses thereto, that may be available under state or federal law.

~~G. Exemption (Advice Letter):~~ A Commission jurisdictional utility may be exempted from these Rules if it files an advice letter with the Commission requesting exemption. The utility shall file the advice letter within 30 days after the effective date of this decision adopting these Rules and shall serve it on all parties to this proceeding. In the advice letter filing, the utility shall:

1. Attest that no affiliate of the utility provides services as defined by Rule II B above; and
2. Attest that if an affiliate is subsequently created which provides services as defined by Rule II B above, then the utility shall:

~~a. Notify the Commission, at least 30 days before the affiliate begins to provide services as defined by Rule II B above, that such an affiliate has been created; notification shall be accomplished by means of a letter to the Executive Director, served on all parties to this proceeding; and~~

~~b. Agree in this notice to comply with the Rules in their entirety.~~

~~H. Limited Exemption (Application):~~ A California utility which is also a multistate utility and subject to the jurisdiction of other state regulatory commissions, may file an application, served on all parties to this proceeding, requesting a limited exemption from these Rules or a part thereof, for transactions between the utility solely in its capacity serving its jurisdictional areas wholly outside of California, and its affiliates. The applicant has the burden of proof.

~~I.~~ These Rules should be interpreted broadly, to effectuate our stated objectives of fostering competition and protecting consumer interests. If any provision of these Rules, or the application thereof to any person, company, or circumstance, is held invalid, the remainder of the Rules, or the application of such provision to other persons, companies, or circumstances, shall not be affected thereby.

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### III. Nondiscrimination

A. **No Preferential Treatment Regarding Services Provided by the Utility:** Unless otherwise authorized by the Commission or the FERC, or permitted by these Rules, a utility shall not:

1. represent that, as a result of the affiliation with the utility, its affiliates or customers of its affiliates will receive any different treatment by the utility than the treatment the utility provides to other, unaffiliated companies or their customers; or
2. provide its affiliates, or customers of its affiliates, any preference (including but not limited to terms and conditions, pricing, or timing) over non-affiliated suppliers or their customers in the provision of services provided by the utility.

B. **Affiliate Transactions:** Transactions between a utility and its affiliates shall be limited to tariffed products and services, to the sale or purchase of goods, property, products or services made generally available by the utility or affiliate to all market participants through an open, competitive bidding process, to the provision of information made generally available by the utility to all market participants, to Commission-approved resource procurement by the utility, or as provided for in Rules Sections V D (joint purchases), and V E (joint purchases and corporate support) and Section VII (new products and services) below, provided the transactions provided for in Section VII comply with all of the other adopted Rules.

1. Resource Procurement. No utility shall engage in resource procurement, as defined in these Rules, from an affiliate without prior approval from the Commission. Blind transactions between a utility and its affiliate, defined as those transactions in which neither party knows the identity of the counterparty until the transaction is consummated, are exempted from this Rule. A transaction shall be deemed to have prior Commission approval (a) before the effective date of this Rule, if authorized by the Commission specifically or through the delegation of authority to Commission staff or (b) after the effective date of this Rule, if authorized by the Commission generally

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or specifically or through the delegation of authority to Commission staff.

**2. Provision of Supply, Capacity, Services or Information:** Except as provided for in ~~Sections Rules V D, V E, and VII, provided the transactions provided for in Section VII comply with all of the other adopted Rules,~~ a utility shall provide access to utility information, services, and unused capacity or supply on the same terms for all similarly situated market participants. If a utility provides supply, capacity, services, or information to its affiliate(s), it shall contemporaneously make the offering available to all similarly situated market participants, which include all competitors serving the same market as the utility's affiliates.

**32. Offering of Discounts:** Except when made generally available by the utility through an open, competitive bidding process, if a utility offers a discount or waives all or any part of any other charge or fee to its affiliates, or offers a discount or waiver for a transaction in which its affiliates are involved, the utility shall contemporaneously make such discount or waiver available to all similarly situated market participants. The utilities should not use the "similarly situated" qualification to create such a unique discount arrangement with their affiliates such that no competitor could be considered similarly situated. All competitors serving the same market as the utility's affiliates should be offered the same discount as the discount received by the affiliates. A utility shall document the cost differential underlying the discount to its affiliates in the affiliate discount report described in Rule III F 7 below.

**43. Tariff Discretion:** If a tariff provision allows for discretion in its application, a utility shall apply that tariff provision in the same manner to its affiliates and other market participants and their respective customers.

**54. No Tariff Discretion:** If a utility has no discretion in the application of a tariff provision, the utility shall strictly enforce that tariff provision.

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**65. Processing Requests for Services Provided by the Utility:** A utility shall process requests for similar services provided by the utility in the same manner and within the same time for its affiliates and for all other market participants and their respective customers.

**C. Tying of Services Provided by a Utility Prohibited:** A utility shall not condition or otherwise tie the provision of any services provided by the utility, nor the availability of discounts of rates or other charges or fees, rebates, or waivers of terms and conditions of any services provided by the utility, to the taking of any goods or services from its affiliates.

**D. No Assignment of Customers:** A utility shall not assign customers to which it currently provides services to any of its affiliates, whether by default, direct assignment, option or by any other means, unless that means is equally available to all competitors.

**E. Business Development and Customer Relations:** Except as otherwise provided by these Rules, a utility shall not:

1. provide leads to its affiliates;
2. solicit business on behalf of its affiliates;
3. acquire information on behalf of or to provide to its affiliates;
4. share market analysis reports or any other types of proprietary or nonpublicly available reports, including but not limited to market, forecast, planning or strategic reports, with its affiliates;
5. request authorization from its customers to pass on customer information exclusively to its affiliates;
6. give the appearance that the utility speaks on behalf of its affiliates or that the customer will receive preferential treatment as a consequence of conducting business with the affiliates; or
7. give any appearance that the affiliate speaks on behalf of the utility.

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**F. Affiliate Discount Reports:** If a utility provides its affiliates a discount, rebate, or other waiver of any charge or fee associated with services provided by the utility, the utility shall, within 24 hours of the time at which the service provided by the utility is so provided, post a notice on its electronic bulletin board providing the following information:

1. the name of the affiliate involved in the transaction;
2. the rate charged;
3. the maximum rate;
4. the time period for which the discount or waiver applies;
5. the quantities involved in the transaction;
6. the delivery points involved in the transaction;
7. any conditions or requirements applicable to the discount or waiver, and a documentation of the cost differential underlying the discount as required in Rule III B 2 above; and
8. procedures by which a nonaffiliated entity may request a comparable offer.

A utility that provides an affiliate a discounted rate, rebate, or other waiver of a charge or fee associated with services provided by the utility shall maintain, for each billing period, the following information:

9. the name of the entity being provided services provided by the utility in the transaction;
10. the affiliate's role in the transaction (i.e., shipper, marketer, supplier, seller);
11. the duration of the discount or waiver;
12. the maximum rate;

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13. the rate or fee actually charged during the billing period; and
14. the quantity of products or services scheduled at the discounted rate during the billing period for each delivery point.

All records maintained pursuant to this provision shall also conform to FERC rules where applicable.

### IV. Disclosure and Information

A. **Customer Information:** A utility shall provide customer information to its affiliates and unaffiliated entities on a strictly non-discriminatory basis, and only with prior affirmative customer written consent.

B. **Non-Customer Specific Non-Public Information:** A utility shall make non-customer specific non-public information, including but not limited to information about a utility's natural gas or electricity purchases, sales, or operations or about the utility's gas-related goods or services and, electricity-related goods or services, available to the utility's affiliates only if the utility makes that information contemporaneously available to all other service providers on the same terms and conditions, and keeps the information open to public inspection. Unless otherwise provided by these Rules, a utility continues to be bound by all Commission-adopted pricing and reporting guidelines for such transactions. A utility is ~~Utilities are~~ also permitted to exchange proprietary information on an exclusive basis with its ~~their~~ affiliates, provided the utility follows all Commission-adopted pricing and reporting guidelines for such transactions, and it is necessary to exchange this information in the provision of the corporate support services permitted by Rule V E below. The affiliate's use of such proprietary information is limited to use in conjunction with the permitted corporate support services, and is not permitted for any other use. Nothing in this Rule precludes the exchange of information pursuant to D.97-10-031. Nothing in this Rule is intended to limit the Commission's right to information under Public Utilities Code Sections 314 and 581.

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### C. Service Provider Information:

~~1. Except upon request by a customer or as otherwise authorized by the Commission, or approved by another governmental body, a utility shall not provide its customers with any list of service providers, which includes or identifies the utility's affiliates, regardless of whether such list also includes or identifies the names of unaffiliated entities. A utility shall submit lists approved by other governmental bodies in the first semi-annual advice letter filing referenced in Rule IV.C.2 following such approval, but may provide customers with such lists pending action on the advice letter.~~

~~2. If a customer requests information about any affiliated service provider, the utility shall provide a list of all providers of gas related, electricity related, or other utility related goods and services operating in its service territory, including its affiliates. The Commission shall authorize, by semi-annual utility advice letter filing, and either the utility, the Commission, or a Commission authorized third party provider shall maintain on file with the Commission a copy of the most updated lists of service providers which have been created to disseminate to a customer upon a customer's request. Any service provider may request that it be included on such list, and, barring Commission direction, the utility shall honor such request. Where maintenance of such list would be unduly burdensome due to the number of service providers, subject to Commission approval by advice letter filing, the utility shall direct the customer to a generally available listing of service providers (e.g., the Yellow Pages). In such cases, no list shall be provided. If there is no Commission authorized list available, utilities may refer customers to a generally available listing of service providers (e.g., the Yellow Pages.) The list of service providers should make clear that the Commission does not guarantee the financial stability or service quality of the service providers listed by the act of approving this list.~~

D. **Supplier Information:** A utility may provide non-public information and data which has been received from unaffiliated suppliers to its affiliates or non-affiliated entities only if the utility first obtains written affirmative authorization to do so from the supplier. A utility shall not

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actively solicit the release of such information exclusively to its own affiliate in an effort to keep such information from other unaffiliated entities.

- E. **Affiliate-Related Advice or Assistance:** Except as otherwise provided in these Rules, a utility shall not offer or provide customers advice or assistance with regard to its affiliates or other service providers.
- F. **Record-Keeping:** A utility shall maintain contemporaneous records documenting all tariffed and nontariffed transactions with its affiliates, including but not limited to, all waivers of tariff or contract provisions, ~~and all discounts, and all negotiations of any sort between the utility and its affiliate whether or not they are consummated.~~ A utility shall maintain such records for a minimum of three years and longer if this Commission or another government agency so requires. For consummated transactions, the utility shall make final transaction documents such records available for third party review upon 72 hours' notice, or at a time mutually agreeable to the utility and third party.
- If D.97-06-110 is applicable to the information the utility seeks to protect, the utility should follow the procedure set forth in D.97-06-110, except that the utility should serve the third party making the request in a manner that the third party receives the utility's D.97-06-110 request for confidentiality within 24 hours of service.
- G. **Maintenance of Affiliate Contracts and Related Bids:** A utility shall maintain a record of all contracts and related bids for the provision of work, products or services ~~between to and from the utility and to its affiliates~~ between to and from the utility and to its affiliates for no less than a period of three years, and longer if this Commission or another government agency so requires.
- H. **FERC Reporting Requirements:** To the extent that reporting rules imposed by the FERC require more detailed information or more expeditious reporting, nothing in these Rules shall be construed as modifying the FERC rules.

## V. Separation

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- A. **Corporate Entities:** A utility, its parent holding company, and its affiliates shall be separate corporate entities.
- B. **Books and Records:** A utility, its parent holding company, and its affiliates shall keep separate books and records.
1. Utility books and records shall be kept in accordance with applicable Uniform System of Accounts (USOA) and Generally Accepted Accounting Procedures (GAAP).
  2. The books and records of a utility's parent holding company and affiliates shall be open for examination by the Commission and its staff consistent with the provisions of Public Utilities Code Section 314 and 701, the conditions in the Commission's orders authorizing the utilities' holding companies and/or mergers and these Rules.
- C. **Sharing of Plant, Facilities, Equipment or Costs:** A utility shall not share office space, office equipment, services, and systems with its affiliates, nor shall a utility access the computer or information systems of its affiliates or allow its affiliates to access its computer or information systems, except to the extent appropriate to perform shared corporate support functions permitted under ~~Section Rule~~ Section Rule V E of these Rules. Physical separation required by this rule shall be accomplished preferably by having office space in a separate building, or, in the alternative, through the use of separate elevator banks and/or security-controlled access. This provision does not preclude a utility from offering a joint service provided this service is authorized by the Commission and is available to all non-affiliated service providers on the same terms and conditions (e.g., joint billing services pursuant to D.97-05-039).
- D. **Joint Purchases:** To the extent not precluded by any other Rule, the utilities and their affiliates may make joint purchases of good and services, but not those associated with the traditional utility merchant function. For purpose of these Rules, to the extent that a utility is engaged in the marketing of the commodity of electricity or natural

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gas to customers, as opposed to the marketing of transmission and distribution services, it is engaging in merchant functions. Examples of permissible joint purchases include joint purchases of office supplies and telephone services. Examples of joint purchases not permitted include gas and electric purchasing for resale, purchasing of gas transportation and storage capacity, purchasing of electric transmission, systems operations, and marketing. The utility must insure that all joint purchases are priced, reported, and conducted in a manner that permits clear identification of the utility and affiliate portions of such purchases, and in accordance with applicable Commission allocation and reporting rules.

- E. **Corporate Support:** As a general principle, a utility, its parent holding company, or a separate affiliate created solely to perform corporate support services may share with its affiliates joint corporate oversight, governance, support systems and personnel, as further specified below. Any shared support shall be priced, reported and conducted in accordance with the Separation and Information Standards set forth herein, as well as other applicable Commission pricing and reporting requirements.

As a general principle, such joint utilization shall not allow or provide a means for the transfer of confidential information from the utility to the affiliate, create the opportunity for preferential treatment or unfair competitive advantage, lead to customer confusion, or create significant opportunities for cross-subsidization of affiliates. In the compliance plan, a corporate officer from the utility and holding company shall verify the adequacy of the specific mechanisms and procedures in place to ensure the utility follows the mandates of this paragraph, and to ensure the utility is not utilizing joint corporate support services as a conduit to circumvent these Rules.

Examples of services that may be shared include: payroll, taxes, shareholder services, insurance, financial reporting, financial planning and analysis, corporate accounting, corporate security, human resources (compensation, benefits, employment policies), employee records, regulatory affairs, lobbying, legal, and pension management. However, if a utility and its parent holding company share any key

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officers after 180 days following the effective date of the decision adopting these Rule modifications, then the following services shall no longer be shared: regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services still authorized. For purposes of this Rule, key officers are the Chair of the entire corporate enterprise, the President at the utility and at its holding company parent, the chief executive officer at each, the chief financial officer at each, and the chief regulatory officer at each, or in each case, any and all officers whose responsibilities are the functional equivalent of the foregoing.

Examples of services that may not be shared include: employee recruiting, engineering, hedging and financial derivatives and arbitrage services, gas and electric purchasing for resale, purchasing of gas transportation and storage capacity, purchasing of electric transmission, system operations, and marketing. However, if a utility and its parent holding company share any key officers (as defined in the preceding paragraph) after 180 days following the effective date of the decision adopting these Rule modifications, then the following services shall no longer be shared: regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services still authorized.

### F. Corporate Identification and Advertising:

1. A utility shall not trade upon, promote, or advertise its affiliate's affiliation with the utility, nor allow the utility name or logo to be used by the affiliate or in any material circulated by the affiliate, unless it discloses in plain legible or audible language, on the first page or at the first point where the utility name or logo appears that:
  - a. the affiliate "is not the same company as [i.e. PG&E, Edison, the Gas Company, etc.], the utility,";
  - b. the affiliate is not regulated by the California Public Utilities Commission; and

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c. "you do not have to buy [the affiliate's] products in order to continue to receive quality regulated services from the utility."  
The application of the name/logo disclaimer is limited to the use of the name or logo in California.

2. A utility, through action or words, shall not represent that, as a result of the affiliate's affiliation with the utility, its affiliates will receive any different treatment than other service providers.

3. A utility shall not offer or provide to its affiliates advertising space in utility billing envelopes or any other form of utility customer written communication unless it provides access to all other unaffiliated service providers on the same terms and conditions.

4. A utility shall not participate in joint advertising or joint marketing with its affiliates. This prohibition means that utilities may not engage in activities which include, but are not limited to the following:

a. A utility shall not participate with its affiliates in joint sales calls, through joint call centers or otherwise, or joint proposals (including responses to requests for proposals (RFPs)) to existing or potential customers. At a customer's unsolicited request, a utility may participate, on a nondiscriminatory basis, in non-sales meetings with its affiliates or any other market participant to discuss technical or operational subjects regarding the utility's provision of transportation service to the customer;

b. Except as otherwise provided for by these Rules, a utility shall not participate in any joint activity with its affiliates. The term "joint activities" includes, but is not limited to, advertising, sales, marketing, communications and correspondence with any existing or potential customer;

c. A utility shall not participate with its affiliates in trade shows, conferences, or other information or marketing events held in California.

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5. A utility shall not share or subsidize costs, fees, or payments with its affiliates associated with research and development activities or investment in advanced technology research.

### G. Employees:

1. Except as permitted in ~~Section~~ Rule V E (corporate support), a utility and its affiliates shall not jointly employ the same employees. This Rule prohibiting joint employees also applies to Board Directors, and corporate officers, except for the following circumstances: In instances when this Rule is applicable to holding companies, any board member or corporate officer may serve on the holding company and with either the utility or affiliate (but not both) to the extent consistent with Rule V E (corporate support). Where the utility is a multi-state utility, is not a member of a holding company structure, and assumes the corporate governance functions for the affiliates, the prohibition against any board member or corporate officer of the utility also serving as a board member or corporate officer of an affiliate shall only apply to affiliates that operate within California. In the case of shared directors and officers, a corporate officer from the utility and holding company shall describe and verify in the utility's compliance plan required by Rule VI the adequacy of the specific mechanisms and procedures in place to ensure that the utility is not utilizing shared officers and directors as a conduit to circumvent any of these Rules. In its compliance plan ~~required in Rule VI~~, the utility shall list all shared directors and officers between the utility and affiliates. No later than 30 days following a change to this list, the utility shall notify the Commission's Energy Division and the parties on the service list of R.97-04-011/I.97-04-012 of any change to this list.

2. All employee movement between a utility and its affiliates shall be consistent with the following provisions:

a. A utility shall track and report to the Commission all employee movement between the utility and affiliates. The utility shall report this information annually pursuant to our Affiliate Transaction Reporting Decision, D.93-02-016, 48 CPUC2d 163, 171-172 and 180 (Appendix A, Section I and Section II H.).

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b. Once an employee of a utility becomes an employee of an affiliate, the employee may not return to the utility for a period of one year. This Rule is inapplicable if the affiliate to which the employee transfers goes out of business during the one-year period. In the event that such an employee returns to the utility, such employee cannot be retransferred, reassigned, or otherwise employed by the affiliate for a period of two years. Employees transferring from the utility to the affiliate are expressly prohibited from using information gained from the utility in a discriminatory or exclusive fashion, to the benefit of the affiliate or to the detriment of other unaffiliated service providers.

c. When an employee of a utility is transferred, assigned, or otherwise employed by the affiliate, the affiliate shall make a one-time payment to the utility in an amount equivalent to 25% of the employee's base annual compensation, unless the utility can demonstrate that some lesser percentage (equal to at least 15%) is appropriate for the class of employee included. In the limited case where a rank-and-file (non-executive) employee's position is eliminated as a result of electric industry restructuring, a utility may demonstrate that no fee or a lesser percentage than 15% is appropriate. ~~The Board of Directors must vote to classify these employees as "impacted" by electric restructuring and these employees must be transferred no later than December 31, 1998, except for the transfer of employees working at divested plants. In that instance, the Board of Directors must vote to classify these employees as "impacted" by electric restructuring and these employees must be transferred no later than within 60 days after the end of the O&M contract with the new plant owners.~~ All such fees paid to the utility shall be accounted for in a separate memorandum account to track them for future ratemaking treatment (i.e. credited to the Electric Revenue Adjustment Account or the Core and Noncore Gas Fixed Cost Accounts, or other ratemaking treatment, as appropriate), on an annual basis, or as otherwise necessary to ensure that the utility's ratepayers receive the fees. This transfer payment provision will not apply to clerical workers. Nor will it apply to the initial transfer of employees to the utility's holding company to perform corporate support functions or to a separate affiliate performing corporate support functions, provided that that transfer is made during the initial implementation period of these rules or pursuant to a § 851

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application or other Commission proceeding. However, the rule will apply to any subsequent transfers or assignments between a utility and its affiliates of all covered employees at a later time.

d. Any utility employee hired by an affiliate shall not remove or otherwise provide information to the affiliate which the affiliate would otherwise be precluded from having pursuant to these Rules.

e. A utility shall not make temporary or intermittent assignments, or rotations to its energy marketing affiliates. Utility employees not involved in marketing may be used on a temporary basis (less than 30% of an employee's chargeable time in any calendar year) by affiliates not engaged in energy marketing only if:

i. All such use is documented, priced and reported in accordance with these Rules and existing Commission reporting requirements, except that when the affiliate obtains the services of a non-executive employee, compensation to the utility should be priced at a minimum of the greater of fully loaded cost plus 10% of direct labor cost, or fair market value. When the affiliate obtains the services of an executive employee, compensation to the utility should be priced at a minimum of the greater of fully loaded cost plus 15% of direct labor cost, or fair market value.

ii. Utility needs for utility employees always take priority over any affiliate requests;

iii. No more than 5% of full time equivalent utility employees may be on loan at a given time;

iv. Utility employees agree, in writing, that they will abide by these Affiliate Transaction Rules; and

v. Affiliate use of utility employees must be conducted pursuant to a written agreement approved by appropriate utility and affiliate officers.

**H. Transfer of Goods and Services:** To the extent that these Rules do not

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prohibit transfers of goods and services between a utility and its affiliates, and except for as provided by Rule V.G.2.e, all such transfers shall be subject to the following pricing provisions:

1. Transfers from the utility to its affiliates of goods and services produced, purchased or developed for sale on the open market by the utility will be priced at fair market value.
2. Transfers from an affiliate to the utility of goods and services produced, purchased or developed for sale on the open market by the affiliate shall be priced at no more than fair market value.
3. For goods or services for which the price is regulated by a state or federal agency, that price shall be deemed to be the fair market value, except that in cases where more than one state commission regulates the price of goods or services, this Commission's pricing provisions govern.
4. Goods and services produced, purchased or developed for sale on the open market by the utility will be provided to its affiliates and unaffiliated companies on a nondiscriminatory basis, except as otherwise required or permitted by these Rules or applicable law.
5. Transfers from the utility to its affiliates of goods and services not produced, purchased or developed for sale by the utility will be priced at fully loaded cost plus 5% of direct labor cost.
6. Transfers from an affiliate to the utility of goods and services not produced, purchased or developed for sale by the affiliate will be priced at the lower of fully loaded cost or fair market value.

### VI. Regulatory Oversight

A. **Compliance Plans:** No later than June 30, 2007~~December 31, 1997~~, each utility shall file a compliance plan by advice letter with the Energy Division of the Commission. The compliance plan shall include:

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1. A list of all affiliates of the utility, as defined in Rule I A of these Rules, and for each affiliate, its purpose or activities, and whether the utility claims that Rule II B makes these Rules applicable to the affiliate;
2. A demonstration of the procedures in place to assure compliance with these Rules.

~~demonstrating to the Commission that there are adequate procedures in place that will preclude the sharing of information with its affiliates that is prohibited by these Rules. The utility should file its compliance plan as an advice letter with the Commission's Energy Division and serve it on the parties to this proceeding.~~ The utility's compliance plan shall be in effect between the filing and a Commission determination of the advice letter. A utility shall file a compliance plan annually thereafter by advice letter ~~served on all parties to this proceeding where~~ when there has been is some change in the compliance plan (i.e., when there has been a change in the purpose or activities of an affiliate, a new affiliate has been created, or the utility has changed the compliance plan for any other reason).

**B. New Affiliate Compliance Plans:** ~~Upon the creation of a new affiliate which is addressed by these Rules,~~ the utility shall immediately notify the Commission of the creation of the new affiliate, as well as posting notice on its electronic bulletin board. No later than 60 days after the creation of this affiliate, the utility shall file an advice letter with the Energy Division of the Commission, ~~served on the parties to this proceeding.~~ The advice letter shall state the affiliate's purpose or activities, whether the utility claims that Rule II B makes these Rules applicable to the affiliate, and shall include demonstration to the Commission that there are adequate procedures in place that will ensure compliance with how the utility will implement these Rules with respect to the new affiliate.

**C. Affiliate Audit:** The Commission's Energy Division ~~No later than December 31, 1998, and every year thereafter,~~ the utility shall have audits performed biennially by independent auditors. The audits shall ~~that~~ cover the last two calendar years which ends on December 31, and ~~that shall~~ verify that the utility is in compliance with the Rules set forth herein. The Energy Division ~~utilities shall~~ post the audit file the independent auditor's reports on ~~with the Commission's web site~~ Energy Division beginning no later than May 1, 1999, and



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2. "Existing" products and services are those which a utility is offering on the effective date of these Rules.

3. "Products" include use of property, both real and intellectual, other than those uses authorized under General Order 69-C.

4. "Tariff" or "tariffed" refers to rates, terms and conditions of services as approved by this Commission or the Federal Energy Regulatory Commission (FERC), whether by traditional tariff, approved contract or other such approval process as the Commission or the FERC may deem appropriate.

**C. Utility Products and Services:** Except as provided in these Rules, a utility shall not offer nontariffed products and services. In no event shall a utility offer natural gas or electricity commodity service on a nontariffed basis. A utility may only offer for sale the following products and services:

1. Existing products and services offered by the utility pursuant to tariff;
2. Unbundled versions of existing utility products and services, with the unbundled versions being offered on a tariffed basis;
3. New products and services that are offered on a tariffed basis; and
4. Products and services which are offered on a nontariffed basis and which meet the following conditions:
  - a. The nontariffed product or service utilizes a portion of a utility asset or capacity;
  - b. such asset or capacity has been acquired for the purpose of and is necessary and useful in providing tariffed utility services;
  - c. the involved portion of such asset or capacity may be used to offer the product or service on a nontariffed basis without adversely affecting the cost, quality or reliability of tariffed utility products and services;
  - d. the products and services can be marketed with minimal or no incremental ratepayer capital, minimal or no new forms of liability or business risk being incurred by utility ratepayers, and no undue

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diversion of utility management attention; and  
e. The utility's offering of such nontariffed product or service does not violate any law, regulation, or Commission policy regarding anticompetitive practices.

**D. Conditions Precedent to Offering New Products and Services:** This Rule does not represent an endorsement by the Commission of any particular nontariffed utility product or service. A utility may offer new nontariffed products and services only if the Commission has adopted and the utility has established:

1. A mechanism or accounting standard for allocating costs to each new product or service to prevent cross-subsidization between services a utility would continue to provide on a tariffed basis and those it would provide on a nontariffed basis;
2. A reasonable mechanism for treatment of benefits and revenues derived from offering such products and services, except that in the event the Commission has already approved a performance-based ratemaking mechanism for the utility and the utility seeks a different sharing mechanism, the utility should petition to modify the performance-based ratemaking decision if it wishes to alter the sharing mechanism, or clearly justify why this procedure is inappropriate, rather than doing so by application or other vehicle.
3. Periodic reporting requirements regarding pertinent information related to nontariffed products and services; and
4. Periodic auditing of the costs allocated to and the revenues derived from nontariffed products and services.

**E. Requirement to File an Advice Letter:** Prior to offering a new category of nontariffed products or services as set forth in ~~Section~~ Rule VII C above, a utility shall file an advice letter in compliance with the following provisions of this paragraph.

1. The advice letter shall:
  - a. demonstrate compliance with these rules;

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## APPENDIX A-2

- b. address the amount of utility assets dedicated to the non-utility venture, in order to ensure that a given product or service does not threaten the provision of utility service, and show that the new product or service will not result in a degradation of cost, quality, or reliability of tariffed goods and services;
  - ~~c. demonstrate that the utility has not received competition transition charge (CTC) recovery in the Transition Cost Proceeding, A.96-08-001, or other related CTC Commission proceeding, for the portion of the utility asset dedicated to the non-utility venture; and~~
  - ~~d.~~ address the potential impact of the new product or service on competition in the relevant market including but not limited to the degree in which the relevant market is already competitive in nature and the degree to which the new category of products or services is projected to affect that market.
  - de. be served on the service list of Rulemaking 97-04-011/Investigation 97-04-012, as well as on any other party appropriately designated by the rules governing the Commission's advice letter process.
2. For categories of nontariffed products or services targeted and offered to less than 1% of the number of customers in the utility's customer base, in the absence of a protest alleging non-compliance with these Rules or any law, regulation, decision, or Commission policy, or allegations of harm, the utility may commence offering the product or service 30 days after submission of the advice letter. For categories of nontariffed products or services targeted and offered to 1% or more of the number of customers in the utility's customer base, the utility may commence offering the product or service after the Commission approves the advice letter through the normal advice letter process.
  3. A protest of an advice letter filed in accordance with this paragraph shall include:
    - a. An explanation of the specific Rules, or any law, regulation, decision, or Commission policy the utility will allegedly violate by offering the proposed product or service, with reasonable factual detail; or

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b. An explanation of the specific harm the protestant will allegedly suffer.

4. If such a protest is filed, the utility may file a motion to dismiss the protest within 5 working days if it believes the protestant has failed to provide the minimum grounds for protest required above. The protestant has 5 working days to respond to the motion.

5. The intention of the Commission is to make its best reasonable efforts to rule on such a motion to dismiss promptly. Absent a ruling granting a motion to dismiss, the utility shall begin offering that category of products and services only after Commission approval through the normal advice letter process.

**F. Existing Offerings:** Unless and until further Commission order to the contrary as a result of the advice letter filing or otherwise, a utility that is offering tariffed or nontariffed products and services, as of the effective date of this decision, may continue to offer such products and services, provided that the utility complies with the cost allocation and reporting requirements in this rule. No later than January 30, 1998, each utility shall submit an advice letter describing the existing products and services (both tariffed and nontariffed) currently being offered by the utility and the number of the Commission decision or advice letter approving this offering, if any, and requesting authorization or continuing authorization for the utility's continued provision of this product or service in compliance with the criteria set forth in Rule VII. This requirement applies to both existing products and services explicitly approved and not explicitly approved by the Commission.

**G. Section 851 Application:** A utility must continue to comply fully with the provisions of Public Utilities Code Section 851 when necessary or useful utility property is sold, leased, assigned, mortgaged, disposed of, or otherwise encumbered as part of a nontariffed product or service offering by the utility. If an application pursuant to Section 851 is submitted, the utility need not file a separate advice letter, but shall include in the application those items which would otherwise appear in the advice letter as required in this Rule.

**H. Periodic Reporting of Nontariffed Products and Services:** Any utility

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offering nontariffed products and services shall file periodic reports with the Commission's Energy Division twice annually for the first two years following the effective date of these Rules, then annually thereafter unless otherwise directed by the Commission. The utility shall serve periodic reports on the service list of this proceeding. The periodic reports shall contain the following information:

1. A description of each existing or new category of nontariffed products and services and the authority under which it is offered;
2. A description of the types and quantities of products and services contained within each category (so that, for example, "leases for agricultural nurseries at 15 sites" might be listed under the category "leases of land under utility transmission lines," although the utility would not be required to provide the details regarding each individual lease);
3. The costs allocated to and revenues derived from each category; and
4. Current information on the proportion of relevant utility assets used to offer each category of product and service.

**I. Offering of Nontariffed Products and Services to Affiliates:** Nontariffed products and services which are allowed by this Rule may be offered to utility affiliates only in compliance with all other provisions of these Affiliate Rules. Similarly, this Rule does not prohibit affiliate transactions which are otherwise allowed by all other provisions of these Affiliate Rules.

**VIII. Complaint Procedures and Remedies** (adopted by D.98-12-075) – insert these here

### **IX. Protecting the Utility's Financial Health**

**A. Information from Utility on Necessary Capital.** Each utility shall provide to the Commission on the last business day of November of each year a report with the following information:

1. the utility's estimate of investment capital needed to build or acquire long-term assets (i.e., greater than one year), such as

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- operating assets and utility infrastructure, over each of the next five years;
2. the utility's estimate of capital needed to meet resource procurement goals over each of the next five years;
3. the utility's policies concerning dividends, stock repurchase and retention of capital for each year;
4. the names of individuals involved in deciding corporate policies for the utility's dividends, stock repurchase and retention of capital;
5. the process by which corporate policies concerning dividends, stock repurchase and retention of capital are implemented; and
6. how the utility expects or intends to meet its investment capital needs.

### **B. Restrictions on Deviations from Authorized Capital Structure.**

A utility shall maintain a balanced capital structure consistent with that determined to be reasonable by the Commission in its most recent decision on the utility's capital structure. The utility's equity shall be retained such that the Commission's adopted capital structure shall be maintained on average over the period the capital structure is in effect for ratemaking purposes. Provided, however, that a utility shall file an application for a waiver, on a case by case basis and in a timely manner, of this Rule if an adverse financial event at the utility reduces the utility's equity ratio by 1% or more. In order to assure that regulatory staff has adequate time to review and assess the application and to permit the consideration of all relevant facts, the utility shall not be considered in violation of this Rule during the period the waiver is pending resolution. Nothing in this provision creates a presumption of either reasonableness or unreasonableness of the utility's actions which may have caused the adverse financial event.

**C. Ring-Fencing.** Within three months of the effective date of the decision adopting this amendment to the Rules, a utility shall obtain a non-consolidation opinion that demonstrates that the ring fencing around the utility is sufficient to prevent the utility from being pulled into bankruptcy of its parent holding company. The utility shall promptly provide the opinion to the Commission. If the current ring-fencing provisions are

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insufficient to obtain a non-consolidation opinion, the utility shall promptly undertake the following actions:

1. notify the Commission of the inability to obtain a non-consolidation opinion;
2. propose and implement, upon Commission approval, such ring-fencing provisions that are sufficient to prevent the utility from being pulled into the bankruptcy of its parent holding company; and then
3. obtain a non-consolidation opinion.

**D. Changes to Ring-Fencing Provisions.** A utility shall notify the Commission of any changes made to its ring-fencing provisions within 30 days.

(END OF APPENDIX A-2)

**APPENDIX A-3**

**AFFILIATE TRANSACTION RULES APPLICABLE  
LARGE CALIFORNIA ENERGY UTILITIES**

## APPENDIX A-3

### Affiliate Transaction Rules Applicable to Large California Energy Utilities

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### Affiliate Transaction Rules Applicable to Large California Energy Utilities

#### I. Definitions

Unless the context otherwise requires, the following definitions govern the construction of these Rules:

- A. **“Affiliate”** means any person, corporation, utility, partnership, or other entity 5 per cent or more of whose outstanding securities are owned, controlled, or held with power to vote, directly or indirectly either by a utility or any of its subsidiaries, or by that utility’s controlling corporation and/or any of its subsidiaries as well as any company in which the utility, its controlling corporation, or any of the utility’s affiliates exert substantial control over the operation of the company and/or indirectly have substantial financial interests in the company exercised through means other than ownership. For purposes of these Rules, “substantial control” includes, but is not limited to, the possession, directly or indirectly and whether acting alone or in conjunction with others, of the authority to direct or cause the direction of the management or policies of a company. A direct or indirect voting interest of 5% or more by the utility in an entity’s company creates a rebuttable presumption of control.

For purposes of this Rule, “affiliate” shall include the utility’s parent or holding company, or any company which directly or indirectly owns, controls, or holds the power to vote 10% or more of the outstanding voting securities of a utility (holding company), to the extent the holding company is engaged in the provision of products or services as set out in Rule II B. However, in its compliance plan filed pursuant to Rule VI, the utility shall demonstrate both the specific mechanism and procedures that the utility and holding company have in place to assure that the utility is not utilizing the holding company or any of its affiliates not covered by these Rules as a conduit to circumvent any of these Rules. Examples include but are not limited to specific mechanisms and procedures to assure the Commission that the utility will not use the holding company, another utility affiliate not covered by these Rules, or a consultant or contractor as a vehicle to (1) disseminate information transferred to them by the utility to an affiliate covered by these Rules in contravention of these Rules, (2) provide services to its affiliates covered by these Rules in contravention of these Rules or (3) to transfer employees to its affiliates

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covered by these Rules in contravention of these Rules. In the compliance plan, a corporate officer from the utility and holding company shall verify the adequacy of these specific mechanisms and procedures to ensure that the utility is not utilizing the holding company or any of its affiliates not covered by these Rules as a conduit to circumvent any of these Rules. Regulated subsidiaries of a utility, defined as subsidiaries of a utility, the revenues and expenses of which are subject to regulation by the Commission and are included by the Commission in establishing rates for the utility, are not included within the definition of affiliate. However, these Rules apply to all interactions any regulated subsidiary has with other affiliated entities covered by these rules.

- B. **“Commission”** means the California Public Utilities Commission or its succeeding state regulatory body.
- C. **“Customer”** means any person or corporation, as defined in Sections 204, 205 and 206 of the California Public Utilities Code, that is the ultimate consumer of goods and services.
- D. **“Customer Information”** means non-public information and data specific to a utility customer which the utility acquired or developed in the course of its provision of utility services.
- E. **“FERC”** means the Federal Energy Regulatory Commission.
- F. **“Fully Loaded Cost”** means the direct cost of good or service plus all applicable indirect charges and overheads.
- G. **“Utility”** means any public utility subject to the jurisdiction of the Commission as an Electrical Corporation or Gas Corporation, as defined in California Public Utilities Code Sections 218 and 222, and with gross annual operating revenues in California of \$1 billion or more.
- H. **“Resource Procurement”** means the investment in and the production or acquisition of the energy facilities, supplies, and other energy products or services necessary for California public utility gas corporations and California public utility electrical corporations to meet their statutory obligation to serve their customers.

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### II. Applicability

- A. These Rules shall apply to California public utility gas corporations and California public utility electrical corporations, subject to regulation by the California Public Utilities Commission and with gross annual operating revenues in California of \$1 billion or more.
- B. For purposes of a combined gas and electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, unless specifically exempted below. For purposes of an electric utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses electricity or the provision of services that relate to the use of electricity. For purposes of a gas utility, these Rules apply to all utility transactions with affiliates engaging in the provision of a product that uses gas or the provision of services that relate to the use of gas. However, regardless of the foregoing, where explicitly provided, these Rules also apply to a utility's parent holding company and to all of its affiliates, whether or not they engage in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity.
- C. No holding company nor any utility affiliate, whether or not engaged in the provision of a product that uses gas or electricity or the provision of services that relate to the use of gas or electricity, shall knowingly:
  - 1. direct or cause a utility to violate or circumvent these Rules, including but not limited to the prohibitions against the utility providing preferential treatment, unfair competitive advantages or non-public information to its affiliates;
  - 2. aid or abet a utility's violation of these Rules; or
  - 3. be used as a conduit to provide non-public information to a utility's affiliate.

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- D. These Rules apply to transactions between a Commission-regulated utility and another affiliated utility, unless specifically modified by the Commission in addressing a separate application to merge or otherwise conduct joint ventures related to regulated services.
- E. These Rules do not apply to the exchange of operating information, including the disclosure of customer information to its FERC-regulated affiliate to the extent such information is required by the affiliate to schedule and confirm nominations for the interstate transportation of natural gas, between a utility and its FERC-regulated affiliate, to the extent that the affiliate operates an interstate natural gas pipeline. These Rules do not apply to transactions between an electric utility and an affiliate providing broadband over power lines (BPL).
- F. **Existing Rules:** Existing Commission rules for each utility and its parent holding company shall continue to apply except to the extent they conflict with these Rules. In such cases, these Rules shall supersede prior rules and guidelines, provided that nothing herein shall supersede the Commission's regulatory framework for broadband over power lines (BPL) adopted in D. 06-04-070 nor shall preclude (1) the Commission from adopting other utility-specific guidelines; or (2) a utility or its parent holding company from adopting other utility-specific guidelines, with advance Commission approval.
- G. **Civil Relief:** These Rules shall not preclude or stay any form of civil relief, or rights or defenses thereto, that may be available under state or federal law.
- H. These Rules should be interpreted broadly, to effectuate our stated objectives of fostering competition and protecting consumer interests. If any provision of these Rules, or the application thereof to any person, company, or circumstance, is held invalid, the remainder of the Rules, or the application of such provision to other persons, companies, or circumstances, shall not be affected thereby.

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### III. Nondiscrimination

A. **No Preferential Treatment Regarding Services Provided by the Utility:** Unless otherwise authorized by the Commission or the FERC, or permitted by these Rules, a utility shall not:

1. represent that, as a result of the affiliation with the utility, its affiliates or customers of its affiliates will receive any different treatment by the utility than the treatment the utility provides to other, unaffiliated companies or their customers; or
2. provide its affiliates, or customers of its affiliates, any preference (including but not limited to terms and conditions, pricing, or timing) over non-affiliated suppliers or their customers in the provision of services provided by the utility.

B. **Affiliate Transactions:** Transactions between a utility and its affiliates shall be limited to tariffed products and services, to the sale of goods, property, products or services made generally available by the utility or affiliate to all market participants through an open, competitive bidding process, to the provision of information made generally available by the utility to all market participants, to Commission-approved resource procurement by the utility, or as provided for in Rules V D (joint purchases), V E (corporate support) and VII (new products and services) below.

1. **Resource Procurement.** No utility shall engage in resource procurement, as defined in these Rules, from an affiliate without prior approval from the Commission. Blind transactions between a utility and its affiliate, defined as those transactions in which neither party knows the identity of the counterparty until the transaction is consummated, are exempted from this Rule. A transaction shall be deemed to have prior Commission approval (a) before the effective date of this Rule, if authorized by the Commission specifically or through the delegation of authority to Commission staff or (b) after the effective date of this Rule, if authorized by the Commission generally or specifically or through the delegation of authority to Commission staff.
2. **Provision of Supply, Capacity, Services or Information:** Except as provided for in Rules V D, V E, and VII, a utility shall provide access to utility information, services, and unused capacity or

### APPENDIX A-3

supply on the same terms for all similarly situated market participants. If a utility provides supply, capacity, services, or information to its affiliate(s), it shall contemporaneously make the offering available to all similarly situated market participants, which include all competitors serving the same market as the utility's affiliates.

3. **Offering of Discounts:** Except when made generally available by the utility through an open, competitive bidding process, if a utility offers a discount or waives all or any part of any other charge or fee to its affiliates, or offers a discount or waiver for a transaction in which its affiliates are involved, the utility shall contemporaneously make such discount or waiver available to all similarly situated market participants. The utilities should not use the "similarly situated" qualification to create such a unique discount arrangement with their affiliates such that no competitor could be considered similarly situated. All competitors serving the same market as the utility's affiliates should be offered the same discount as the discount received by the affiliates. A utility shall document the cost differential underlying the discount to its affiliates in the affiliate discount report described in Rule III F 7 below.
4. **Tariff Discretion:** If a tariff provision allows for discretion in its application, a utility shall apply that tariff provision in the same manner to its affiliates and other market participants and their respective customers.
5. **No Tariff Discretion:** If a utility has no discretion in the application of a tariff provision, the utility shall strictly enforce that tariff provision.
6. **Processing Requests for Services Provided by the Utility:** A utility shall process requests for similar services provided by the utility in the same manner and within the same time for its affiliates and for all other market participants and their respective customers.

## APPENDIX A-3

- C. **Tying of Services Provided by a Utility Prohibited:** A utility shall not condition or otherwise tie the provision of any services provided by the utility, nor the availability of discounts of rates or other charges or fees, rebates, or waivers of terms and conditions of any services provided by the utility, to the taking of any goods or services from its affiliates.
- D. **No Assignment of Customers:** A utility shall not assign customers to which it currently provides services to any of its affiliates, whether by default, direct assignment, option or by any other means, unless that means is equally available to all competitors.
- E. **Business Development and Customer Relations:** Except as otherwise provided by these Rules, a utility shall not:
1. provide leads to its affiliates;
  2. solicit business on behalf of its affiliates;
  3. acquire information on behalf of or to provide to its affiliates;
  4. share market analysis reports or any other types of proprietary or nonpublicly available reports, including but not limited to market, forecast, planning or strategic reports, with its affiliates;
  5. request authorization from its customers to pass on customer information exclusively to its affiliates;
  6. give the appearance that the utility speaks on behalf of its affiliates or that the customer will receive preferential treatment as a consequence of conducting business with the affiliates; or
  7. give any appearance that the affiliate speaks on behalf of the utility.
- F. **Affiliate Discount Reports:** If a utility provides its affiliates a discount, rebate, or other waiver of any charge or fee associated with products or services provided by the utility, the utility shall, within 24 hours of the time at which the product or service provided by the utility is so provided, post a notice on its electronic bulletin board providing the following information:
1. the name of the affiliate involved in the transaction;

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2. the rate charged;
3. the maximum rate;
4. the time period for which the discount or waiver applies;
5. the quantities involved in the transaction;
6. the delivery points involved in the transaction;
7. any conditions or requirements applicable to the discount or waiver, and a documentation of the cost differential underlying the discount as required in Rule III B 2 above; and
8. procedures by which a nonaffiliated entity may request a comparable offer.

A utility that provides an affiliate a discounted rate, rebate, or other waiver of a charge or fee associated with services provided by the utility shall maintain, for each billing period, the following information:

9. the name of the entity being provided services provided by the utility in the transaction;
10. the affiliate's role in the transaction (i.e., shipper, marketer, supplier, seller);
11. the duration of the discount or waiver;
12. the maximum rate;
13. the rate or fee actually charged during the billing period; and
14. the quantity of products or services scheduled at the discounted rate during the billing period for each delivery point.

All records maintained pursuant to this provision shall also conform to FERC rules where applicable.

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### IV. Disclosure and Information

- A. **Customer Information:** A utility shall provide customer information to its affiliates and unaffiliated entities on a strictly non-discriminatory basis, and only with prior affirmative customer written consent.
- B. **Non-Customer Specific Non-Public Information:** A utility shall make non-customer specific non-public information, including but not limited to information about a utility's natural gas or electricity purchases, sales, or operations or about the utility's gas-related goods or services and electricity-related goods or services, available to the utility's affiliates only if the utility makes that information contemporaneously available to all other service providers on the same terms and conditions, and keeps the information open to public inspection. Unless otherwise provided by these Rules, a utility continues to be bound by all Commission-adopted pricing and reporting guidelines for such transactions. A utility is also permitted to exchange proprietary information on an exclusive basis with its affiliates, provided the utility follows all Commission-adopted pricing and reporting guidelines for such transactions, and it is necessary to exchange this information in the provision of the corporate support services permitted by Rule V E below. The affiliate's use of such proprietary information is limited to use in conjunction with the permitted corporate support services, and is not permitted for any other use. Nothing in this Rule precludes the exchange of information pursuant to D.97-10-031. Nothing in this Rule is intended to limit the Commission's right to information under Public Utilities Code Sections 314 and 581.
- C. **Service Provider Information:** Except upon request by a customer or as otherwise authorized by the Commission or another governmental body, a utility shall not provide its customers with any list of service providers, which includes or identifies the utility's affiliates, regardless of whether such list also includes or identifies the names of unaffiliated entities.
- D. **Supplier Information:** A utility may provide non-public information and data which has been received from unaffiliated suppliers to its affiliates or non-affiliated entities only if the utility first obtains written affirmative authorization to do so from the supplier. A utility shall not actively solicit the release of such information exclusively to its own

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affiliate in an effort to keep such information from other unaffiliated entities.

- E. **Affiliate-Related Advice or Assistance:** Except as otherwise provided in these Rules, a utility shall not offer or provide customers advice or assistance with regard to its affiliates or other service providers.
- F. **Record-Keeping:** A utility shall maintain contemporaneous records documenting all tariffed and nontariffed transactions with its affiliates, including but not limited to, all waivers of tariff or contract provisions, all discounts, and all negotiations of any sort between the utility and its affiliate whether or not they are consummated. A utility shall maintain such records for a minimum of three years and longer if this Commission or another government agency so requires. For consummated transactions, the utility shall make such final transaction documents available for third party review upon 72 hours' notice, or at a time mutually agreeable to the utility and third party.

If D.97-06-110 is applicable to the information the utility seeks to protect, the utility should follow the procedure set forth in D.97-06-110, except that the utility should serve the third party making the request in a manner that the third party receives the utility's D.97-06-110 request for confidentiality within 24 hours of service.

- G. **Maintenance of Affiliate Contracts and Related Bids:** A utility shall maintain a record of all contracts and related bids for the provision of work, products or services between the utility and its affiliates for no less than a period of three years, and longer if this Commission or another government agency so requires.
- H. **FERC Reporting Requirements:** To the extent that reporting rules imposed by the FERC require more detailed information or more expeditious reporting, nothing in these Rules shall be construed as modifying the FERC rules.

### V. Separation

- A. **Corporate Entities:** A utility, its parent holding company, and its affiliates shall be separate corporate entities.

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- B. **Books and Records:** A utility, its parent holding company, and its affiliates shall keep separate books and records.
1. Utility books and records shall be kept in accordance with applicable Uniform System of Accounts (USOA) and Generally Accepted Accounting Procedures (GAAP).
  2. The books and records of a utility's parent holding company and affiliates shall be open for examination by the Commission and its staff consistent with the provisions of Public Utilities Code Sections 314 and 701, the conditions in the Commission's orders authorizing the utilities' holding companies and/or mergers and these Rules.
- C. **Sharing of Plant, Facilities, Equipment or Costs:** A utility shall not share office space, office equipment, services, and systems with its affiliates, nor shall a utility access the computer or information systems of its affiliates or allow its affiliates to access its computer or information systems, except to the extent appropriate to perform shared corporate support functions permitted under Rule V E of these Rules. Physical separation required by this rule shall be accomplished preferably by having office space in a separate building, or, in the alternative, through the use of separate elevator banks and/or security-controlled access. This provision does not preclude a utility from offering a joint service provided this service is authorized by the Commission and is available to all non-affiliated service providers on the same terms and conditions (e.g., joint billing services pursuant to D.97-05-039).
- D. **Joint Purchases:** To the extent not precluded by any other Rule, the utilities and their affiliates may make joint purchases of good and services, but not those associated with the traditional utility merchant function. For purpose of these Rules, to the extent that a utility is engaged in the marketing of the commodity of electricity or natural gas to customers, as opposed to the marketing of transmission and distribution services, it is engaging in merchant functions. Examples of permissible joint purchases include joint purchases of office supplies and telephone services. Examples of joint purchases not permitted include gas and electric purchasing for resale, purchasing of gas transportation and storage capacity, purchasing of electric transmission, systems operations, and marketing. The utility must insure that all joint purchases are priced, reported, and conducted in a manner that permits clear identification of the utility and affiliate

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portions of such purchases, and in accordance with applicable Commission allocation and reporting rules.

- E. **Corporate Support:** As a general principle, a utility, its parent holding company, or a separate affiliate created solely to perform corporate support services may share with its affiliates joint corporate oversight, governance, support systems and personnel, as further specified below. Any shared support shall be priced, reported and conducted in accordance with the Separation and Information Standards set forth herein, as well as other applicable Commission pricing and reporting requirements.

As a general principle, such joint utilization shall not allow or provide a means for the transfer of confidential information from the utility to the affiliate, create the opportunity for preferential treatment or unfair competitive advantage, lead to customer confusion, or create significant opportunities for cross-subsidization of affiliates. In the compliance plan, a corporate officer from the utility and holding company shall verify the adequacy of the specific mechanisms and procedures in place to ensure the utility follows the mandates of this paragraph, and to ensure the utility is not utilizing joint corporate support services as a conduit to circumvent these Rules.

Examples of services that may be shared include: payroll, taxes, shareholder services, insurance, financial reporting, financial planning and analysis, corporate accounting, corporate security, human resources (compensation, benefits, employment policies), employee records, regulatory affairs, lobbying, legal, and pension management. However, if a utility and its parent holding company share any key officers after 180 days following the effective date of the decision adopting these Rule modifications, then the following services shall no longer be shared: regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services still authorized. For purposes of this Rule, key officers are the Chair of the entire corporate enterprise, the President at the utility and at its holding company parent, the chief executive officer at each, the chief financial officer at each, and the chief regulatory officer at each, or in each case, any and all officers whose responsibilities are the functional equivalent of the foregoing.

Examples of services that may not be shared include: employee recruiting, engineering, hedging and financial derivatives and arbitrage services, gas and electric purchasing for resale, purchasing of

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gas transportation and storage capacity, purchasing of electric transmission, system operations, and marketing. However, if a utility and its parent holding company share any key officers (as defined in the preceding paragraph) after 180 days following the effective date of the decision adopting these Rule modifications, then the following services shall no longer be shared: regulatory affairs, lobbying, and all legal services except those necessary to the provision of shared services still authorized.

### F. Corporate Identification and Advertising:

1. A utility shall not trade upon, promote, or advertise its affiliate's affiliation with the utility, nor allow the utility name or logo to be used by the affiliate or in any material circulated by the affiliate, unless it discloses in plain legible or audible language, on the first page or at the first point where the utility name or logo appears that:
  - a. the affiliate "is not the same company as [i.e. PG&E, Edison, the Gas Company, etc.], the utility,";
  - b. the affiliate is not regulated by the California Public Utilities Commission; and
  - c. "you do not have to buy [the affiliate's] products in order to continue to receive quality regulated services from the utility." The application of the name/logo disclaimer is limited to the use of the name or logo in California.
2. A utility, through action or words, shall not represent that, as a result of the affiliate's affiliation with the utility, its affiliates will receive any different treatment than other service providers.
3. A utility shall not offer or provide to its affiliates advertising space in utility billing envelopes or any other form of utility customer written communication unless it provides access to all other unaffiliated service providers on the same terms and conditions.
4. A utility shall not participate in joint advertising or joint marketing with its affiliates. This prohibition means that utilities may not engage in activities which include, but are not limited to the following:

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- a. A utility shall not participate with its affiliates in joint sales calls, through joint call centers or otherwise, or joint proposals (including responses to requests for proposals (RFPs)) to existing or potential customers. At a customer's unsolicited request, a utility may participate, on a nondiscriminatory basis, in non-sales meetings with its affiliates or any other market participant to discuss technical or operational subjects regarding the utility's provision of transportation service to the customer;
  - b. Except as otherwise provided for by these Rules, a utility shall not participate in any joint activity with its affiliates. The term "joint activities" includes, but is not limited to, advertising, sales, marketing, communications and correspondence with any existing or potential customer;
  - c. A utility shall not participate with its affiliates in trade shows, conferences, or other information or marketing events held in California.
5. A utility shall not share or subsidize costs, fees, or payments with its affiliates associated with research and development activities or investment in advanced technology research.

#### G. Employees:

1. Except as permitted in Rule V E (corporate support), a utility and its affiliates shall not jointly employ the same employees. This Rule prohibiting joint employees also applies to Board Directors, and corporate officers except for the following circumstances: In instances when this Rule is applicable to holding companies, any board member or corporate officer may serve on the holding company and with either the utility or affiliate (but not both) to the extent consistent with Rule V E (corporate support). Where the utility is a multi-state utility, is not a member of a holding company structure, and assumes the corporate governance functions for the affiliates, the prohibition against any board member or corporate officer of the utility also serving as a board member or corporate officer of an affiliate shall only apply to affiliates that operate within California. In the case of shared directors and officers, a corporate officer from the utility and holding company shall describe and verify in the utility's compliance plan required by Rule VI the adequacy of the specific mechanisms and procedures in place to ensure that the utility is not utilizing shared officers and directors as a conduit to circumvent any of these Rules. In its compliance plan, the

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utility shall list all shared directors and officers between the utility and affiliates. No later than 30 days following a change to this list, the utility shall notify the Commission's Energy Division and the parties on the service list of R.97-04-011/I.97-04-012 of any change to this list.

2. All employee movement between a utility and its affiliates shall be consistent with the following provisions:
  - a. A utility shall track and report to the Commission all employee movement between the utility and affiliates. The utility shall report this information annually pursuant to our Affiliate Transaction Reporting Decision, D.93-02-016, 48 CPUC2d 163, 171-172 and 180 (Appendix A, Section I and Section II H.).
  - b. Once an employee of a utility becomes an employee of an affiliate, the employee may not return to the utility for a period of one year. This Rule is inapplicable if the affiliate to which the employee transfers goes out of business during the one-year period. In the event that such an employee returns to the utility, such employee cannot be retransferred, reassigned, or otherwise employed by the affiliate for a period of two years. Employees transferring from the utility to the affiliate are expressly prohibited from using information gained from the utility in a discriminatory or exclusive fashion, to the benefit of the affiliate or to the detriment of other unaffiliated service providers.
  - c. When an employee of a utility is transferred, assigned, or otherwise employed by the affiliate, the affiliate shall make a one-time payment to the utility in an amount equivalent to 25% of the employee's base annual compensation, unless the utility can demonstrate that some lesser percentage (equal to at least 15%) is appropriate for the class of employee included. In the limited case where a rank-and-file (non-executive) employee's position is eliminated as a result of electric industry restructuring, a utility may demonstrate that no fee or a lesser percentage than 15% is appropriate. All such fees paid to the utility shall be accounted for in a separate memorandum account to track them for future ratemaking treatment (i.e. credited to the Electric Revenue Adjustment Account or the Core and Noncore Gas Fixed Cost Accounts, or other ratemaking treatment, as appropriate), on an annual basis, or as otherwise necessary to ensure that the utility's ratepayers receive the fees. This transfer payment provision will not apply to clerical workers. Nor will it apply to the initial transfer

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of employees to the utility's holding company to perform corporate support functions or to a separate affiliate performing corporate support functions, provided that that transfer is made during the initial implementation period of these rules or pursuant to a § 851 application or other Commission proceeding. However, the rule will apply to any subsequent transfers or assignments between a utility and its affiliates of all covered employees at a later time.

- d. Any utility employee hired by an affiliate shall not remove or otherwise provide information to the affiliate which the affiliate would otherwise be precluded from having pursuant to these Rules.
- e. A utility shall not make temporary or intermittent assignments, or rotations to its energy marketing affiliates. Utility employees not involved in marketing may be used on a temporary basis (less than 30% of an employee's chargeable time in any calendar year) by affiliates not engaged in energy marketing only if:
  - i. All such use is documented, priced and reported in accordance with these Rules and existing Commission reporting requirements, except that when the affiliate obtains the services of a non-executive employee, compensation to the utility should be priced at a minimum of the greater of fully loaded cost plus 10% of direct labor cost, or fair market value. When the affiliate obtains the services of an executive employee, compensation to the utility should be priced at a minimum of the greater of fully loaded cost plus 15% of direct labor cost, or fair market value.
  - ii. Utility needs for utility employees always take priority over any affiliate requests;
  - iii. No more than 5% of full time equivalent utility employees may be on loan at a given time;
  - iv. Utility employees agree, in writing, that they will abide by these Affiliate Transaction Rules; and
  - v. Affiliate use of utility employees must be conducted pursuant to a written agreement approved by appropriate utility and affiliate officers.

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H. **Transfer of Goods and Services:** To the extent that these Rules do not prohibit transfers of goods and services between a utility and its affiliates, and except for as provided by Rule V.G.2.e, all such transfers shall be subject to the following pricing provisions:

1. Transfers from the utility to its affiliates of goods and services produced, purchased or developed for sale on the open market by the utility will be priced at fair market value.
2. Transfers from an affiliate to the utility of goods and services produced, purchased or developed for sale on the open market by the affiliate shall be priced at no more than fair market value.
3. For goods or services for which the price is regulated by a state or federal agency, that price shall be deemed to be the fair market value, except that in cases where more than one state commission regulates the price of goods or services, this Commission's pricing provisions govern.
4. Goods and services produced, purchased or developed for sale on the open market by the utility will be provided to its affiliates and unaffiliated companies on a nondiscriminatory basis, except as otherwise required or permitted by these Rules or applicable law.
5. Transfers from the utility to its affiliates of goods and services not produced, purchased or developed for sale by the utility will be priced at fully loaded cost plus 5% of direct labor cost.
6. Transfers from an affiliate to the utility of goods and services not produced, purchased or developed for sale by the affiliate will be priced at the lower of fully loaded cost or fair market value.

## VI. Regulatory Oversight

A. **Compliance Plans:** No later than June 30, 2007, each utility shall file a compliance plan by advice letter with the Energy Division of the Commission. The compliance plan shall include:

1. A list of all affiliates of the utility, as defined in Rule I A of these Rules, and for each affiliate, its purpose or activities, and whether the utility claims that Rule II B makes these Rules applicable to the affiliate;

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2. A demonstration of the procedures in place to assure compliance with these Rules.

The utility's compliance plan shall be in effect between the filing and a Commission determination of the advice letter. A utility shall file a compliance plan annually thereafter by advice letter where there is some change in the compliance plan (i.e., when there has been a change in the purpose or activities of an affiliate, a new affiliate has been created, or the utility has changed the compliance plan for any other reason).

- B. **New Affiliate Compliance Plans:** Upon the creation of a new affiliate the utility shall immediately notify the Commission of the creation of the new affiliate, as well as posting notice on its electronic bulletin board. No later than 60 days after the creation of this affiliate, the utility shall file an advice letter with the Energy Division of the Commission. The advice letter shall state the affiliate's purpose or activities, whether the utility claims that Rule II B makes these Rules applicable to the affiliate, and shall include a demonstration to the Commission that there are adequate procedures in place that will ensure compliance with these Rules.
- C. **Affiliate Audit:** The Commission's Energy Division shall have audits performed biennially by independent auditors. The audits shall cover the last two calendar years which end on December 31, and shall verify that the utility is in compliance with the Rules set forth herein. The Energy Division shall post the audit reports on the Commission's web site. The audits shall be at shareholder expense.
- D. **Witness Availability:** Affiliate officers and employees shall be made available to testify before the Commission as necessary or required, without subpoena, consistent with the provisions of Public Utilities Code Sections 314 and 701, the conditions in the Commission's orders authorizing the utilities' holding companies and/or mergers and these Rules.

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- E. **Officer Certification.** No later than March 31 of each year, the key officers of a utility and its parent holding company, as defined in Rule V E (corporate support), shall certify to the Energy Division of the Commission in writing under penalty of perjury that each has personally complied with these Rules during the prior calendar year. The certification shall state:

I, [name], hold the office of [title] at [name of utility or holding company], and occupied this position from January 1, [year] to December 31 [year],

I hereby certify that I have reviewed the Affiliate Transaction Rules Applicable to Large California Energy Utilities of the California Public Utilities Commission and I am familiar with the provisions therein. I further certify that for the above period, I followed these Rules and am not aware of any violations of them, other than the following: [list or state "none"].

I swear/affirm these representations under penalty of perjury of the laws of the State of California.

\_\_\_\_\_[Signature]  
Executed at \_\_\_\_\_ [City], County of \_\_\_\_\_, on \_\_\_\_\_ [Date ]

### VII. Utility Products and Services

- A. **General Rule:** Except as provided for in these Rules, new products and services shall be offered through affiliates.
- B. **Definitions:** The following definitions apply for the purposes of Rule VII:
1. "Category" refers to a factually similar group of products and services that use the same type of utility assets or capacity. For example, "leases of land under utility transmission lines" or "use of a utility repair shop for third party equipment repair" would each constitute a separate product or service category.
  2. "Existing" products and services are those which a utility is offering on the effective date of these Rules.
  3. "Products" include use of property, both real and intellectual, other than those uses authorized under General Order 69-C.
  4. "Tariff" or "tariffed" refers to rates, terms and conditions of services as approved by this Commission or the Federal Energy Regulatory Commission (FERC), whether by traditional tariff, approved contract or other such approval process as the Commission or the FERC may deem appropriate.

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- C. **Utility Products and Services:** Except as provided in these Rules, a utility shall not offer nontariffed products and services. In no event shall a utility offer natural gas or electricity commodity service on a nontariffed basis. A utility may only offer for sale the following products and services:
1. Existing products and services offered by the utility pursuant to tariff;
  2. Unbundled versions of existing utility products and services, with the unbundled versions being offered on a tariffed basis;
  3. New products and services that are offered on a tariffed basis; and
  4. Products and services which are offered on a nontariffed basis and which meet the following conditions:
    - a. The nontariffed product or service utilizes a portion of a utility asset or capacity;
    - b. such asset or capacity has been acquired for the purpose of and is necessary and useful in providing tariffed utility services;
    - c. the involved portion of such asset or capacity may be used to offer the product or service on a nontariffed basis without adversely affecting the cost, quality or reliability of tariffed utility products and services;
    - d. the products and services can be marketed with minimal or no incremental ratepayer capital, minimal or no new forms of liability or business risk being incurred by utility ratepayers, and no undue diversion of utility management attention; and
    - e. The utility's offering of such nontariffed product or service does not violate any law, regulation, or Commission policy regarding anticompetitive practices.
- D. **Conditions Precedent to Offering New Products and Services:** This Rule does not represent an endorsement by the Commission of any particular nontariffed utility product or service. A utility may offer new nontariffed products and services only if the Commission has adopted and the utility has established:
1. A mechanism or accounting standard for allocating costs to each new product or service to prevent cross-subsidization between services a utility would continue to provide on a tariffed basis and those it would provide on a nontariffed basis;
  2. A reasonable mechanism for treatment of benefits and revenues derived from offering such products and services, except that in the event the

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Commission has already approved a performance-based ratemaking mechanism for the utility and the utility seeks a different sharing mechanism, the utility should petition to modify the performance-based ratemaking decision if it wishes to alter the sharing mechanism, or clearly justify why this procedure is inappropriate, rather than doing so by application or other vehicle.

3. Periodic reporting requirements regarding pertinent information related to nontariffed products and services; and
4. Periodic auditing of the costs allocated to and the revenues derived from nontariffed products and services.

E. **Requirement to File an Advice Letter:** Prior to offering a new category of nontariffed products or services as set forth in Rule VII C above, a utility shall file an advice letter in compliance with the following provisions of this paragraph.

1. The advice letter shall:
  - a. demonstrate compliance with these rules;
  - b. address the amount of utility assets dedicated to the non-utility venture, in order to ensure that a given product or service does not threaten the provision of utility service, and show that the new product or service will not result in a degradation of cost, quality, or reliability of tariffed goods and services;
  - c. address the potential impact of the new product or service on competition in the relevant market including but not limited to the degree in which the relevant market is already competitive in nature and the degree to which the new category of products or services is projected to affect that market.
  - d. be served on the service list of Rulemaking 97-04-011/Investigation 97-04-012, as well as on any other party appropriately designated by the rules governing the Commission's advice letter process.
2. For categories of nontariffed products or services targeted and offered to less than 1% of the number of customers in the utility's customer base, in the absence of a protest alleging non-compliance with these Rules or any law, regulation, decision, or Commission policy, or allegations of harm, the utility may commence offering the product or service 30 days after

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- submission of the advice letter. For categories of nontariffed products or services targeted and offered to 1% or more of the number of customers in the utility's customer base, the utility may commence offering the product or service after the Commission approves the advice letter through the normal advice letter process.
3. A protest of an advice letter filed in accordance with this paragraph shall include:
    - a. An explanation of the specific Rules, or any law, regulation, decision, or Commission policy the utility will allegedly violate by offering the proposed product or service, with reasonable factual detail; or
    - b. An explanation of the specific harm the protestant will allegedly suffer.
  4. If such a protest is filed, the utility may file a motion to dismiss the protest within 5 working days if it believes the protestant has failed to provide the minimum grounds for protest required above. The protestant has 5 working days to respond to the motion.
  5. The intention of the Commission is to make its best reasonable efforts to rule on such a motion to dismiss promptly. Absent a ruling granting a motion to dismiss, the utility shall begin offering that category of products and services only after Commission approval through the normal advice letter process.
- F. **Existing Offerings:** Unless and until further Commission order to the contrary as a result of the advice letter filing or otherwise, a utility that is offering tariffed or nontariffed products and services, as of the effective date of this decision, may continue to offer such products and services, provided that the utility complies with the cost allocation and reporting requirements in this rule. No later than January 30, 1998, each utility shall submit an advice letter describing the existing products and services (both tariffed and nontariffed) currently being offered by the utility and the number of the Commission decision or advice letter approving this offering, if any, and requesting authorization or continuing authorization for the utility's continued provision of this product or service in compliance with the criteria set forth in Rule VII. This requirement applies to both existing products and services explicitly approved and not explicitly approved by the Commission.

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- G. **Section 851 Application:** A utility must continue to comply fully with the provisions of Public Utilities Code Section 851 when necessary or useful utility property is sold, leased, assigned, mortgaged, disposed of, or otherwise encumbered as part of a nontariffed product or service offering by the utility. If an application pursuant to Section 851 is submitted, the utility need not file a separate advice letter, but shall include in the application those items which would otherwise appear in the advice letter as required in this Rule.
- H. **Periodic Reporting of Nontariffed Products and Services:** Any utility offering nontariffed products and services shall file periodic reports with the Commission's Energy Division twice annually for the first two years following the effective date of these Rules, then annually thereafter unless otherwise directed by the Commission. The utility shall serve periodic reports on the service list of this proceeding. The periodic reports shall contain the following information:
1. A description of each existing or new category of nontariffed products and services and the authority under which it is offered;
  2. A description of the types and quantities of products and services contained within each category (so that, for example, "leases for agricultural nurseries at 15 sites" might be listed under the category "leases of land under utility transmission lines," although the utility would not be required to provide the details regarding each individual lease);
  3. The costs allocated to and revenues derived from each category;
  4. Current information on the proportion of relevant utility assets used to offer each category of product and service.
- I. **Offering of Nontariffed Products and Services to Affiliates:** Nontariffed products and services which are allowed by this Rule may be offered to utility affiliates only in compliance with all other provisions of these Affiliate Rules. Similarly, this Rule does not prohibit affiliate transactions which are otherwise allowed by all other provisions of these Affiliate Rules.

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### VIII. Complaint Procedures and Remedies

A. The Commission shall strictly enforce these rules. Each act or failure to act by a utility in violation of these rules may be considered a separate occurrence.

#### B. Standing:

1. Any person or corporation as defined in Sections 204, 205 and 206 of the California Public Utilities Code may complain to the Commission or to a utility in writing, setting forth any act or thing done or omitted to be done by any utility or affiliate in violation or claimed violation of any rule set forth in this document.
2. "Whistleblower complaints" will be accepted and the confidentiality of complainant will be maintained until conclusion of an investigation or indefinitely, if so requested by the whistleblower. When a whistleblower requests anonymity, the Commission will continue to pursue the complaint only where it has elected to convert it into a Commission-initiated investigation. Regardless of the complainant's status, the defendant shall file a timely answer to the complaint.

#### C. Procedure:

1. All complaints shall be filed as formal complaints with the Commission and complainants shall provide a copy to the utility's designated officer (as described below) on the same day that the complaint is filed.
2. Each utility shall designate an Affiliate Compliance Manager who is responsible for compliance with these affiliate rules and the utility's compliance plan adopted pursuant to these rules. Such officer shall also be responsible for receiving, investigating and attempting to resolve complaints. The Affiliate Compliance Manager may, however, delegate responsibilities to other officers and employees.
  - a. The utility shall investigate and attempt to resolve the complaint. The resolution process shall include a meet-and-confer session with the complainant. A Commission staff member may, upon request by the utility or the complainant, participate in such meet-and-confer sessions and shall participate in the case of a whistleblower complaint.

A party filing a complaint may seek a temporary restraining order at the time the formal complaint is filed. The defendant utility and

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other interested parties may file responses to a request for a temporary restraining order within 10 days of the filing of the request. An assigned commissioner or administrative law judge may shorten the period for responses, where appropriate. An assigned commissioner or administrative law judge, or the Commission shall act on the request for a temporary restraining order within 30 days. The request may be granted when: (1) the moving party is reasonably likely to prevail on the merits, and (2) temporary restraining order relief is necessary to avoid irreparable injury, will not substantially harm other parties, and is consistent with the public interest.

A notice of temporary restraining order issued by an assigned commissioner or administrative law judge will only stay in effect until the end of the day of the next regularly-scheduled Commission meeting at which the Commission can issue a temporary restraining order or a preliminary injunction. If the Commission declines to issue a temporary restraining order or a preliminary injunction, the notice of temporary restraining order will be immediately lifted. Whether or not a temporary restraining order or a preliminary injunction is issued, the underlying complaint may still move forward.

- b. The utility shall prepare and preserve a report on each complaint, all relevant dates, companies, customers, and employees involved, and if applicable, the resolution reached, the date of the resolution and any actions taken to prevent further violations from occurring. The report shall be provided to the Commission and all parties within four weeks of the date the complaint was filed. In addition, to providing hard copies, the utility shall also provide electronic copies to the Commission and to any party providing an e-mail address.
- c. Each utility shall file annually with the Commission a report detailing the nature and status of all complaints.
- d. The Commission may, notwithstanding any resolution reached by the utility and the complainant, convert a complaint to an investigation and determine whether the utility violated these rules, and impose any appropriate penalties under Section VIII.D. or any other remedies provided by the Commission's rules or the Public Utilities Code.

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3. The utility will inform the Commission's Energy Division and Consumer Services Division of the results of this dispute resolution process. If the dispute is resolved, the utility shall inform the Commission staff of the actions taken to resolve the complaint and the date the complaint was resolved.
4. If the utility and the complainant cannot reach a resolution of the complaint, the utility will so inform the Commission's Energy Division. It will also file an answer to the complaint within 30 days of the issuance by the Commission's Docket Office of instructions to answer the original complaint. Within 10 business days of notice of failure to resolve the complaint, Energy Division staff will meet and confer with the utility and the complainant and propose actions to resolve the complaint. Under the circumstances where the complainant and the utility cannot resolve the complaint, the Commission shall strive to resolve the complaint within 180 days of the date the instructions to answer are served on the utility.
5. The Commission shall maintain on its web page a public log of all new, pending and resolved complaints. The Commission shall update the log at least once every week. The log shall specify, at a minimum, the date the complaint was received, the specific allegations contained in the complaint, the date the complaint was resolved and the manner in which it was resolved, and a description of any similar complaints, including the resolution of such similar complaints.
6. Preliminary Discussions
  - a. Prior to filing a formal complaint, a potential complainant may contact the responsible utility officer and/or the Energy Division to inform them of the possible violation of the affiliate rules. If the potential complainant seeks an informal meeting with the utility to discuss the complaint, the utility shall make reasonable efforts to arrange such a meeting. Upon mutual agreement, Energy Division staff and interested parties may attend any such meeting.
  - b. If a potential complainant makes an informal contact with a utility regarding an alleged violation of the affiliate transaction rules, the utility officer in charge of affiliate compliance shall respond in writing to the potential complainant within 15 business days. The response would state whether or not the issues raised by the potential complainant require further investigation. (The potential complainant does not have to rely on the responses in deciding whether to file a formal complaint.)

## APPENDIX A-3

### D. Remedies

1. When enforcing these rules or any order of the Commission regarding these rules, the Commission may do any or all of the following:
  - a. Order a utility to stop doing something that violates these rules;
  - b. Prospectively limit or restrict the amount, percentage, or value of transactions entered into between the utility and its affiliate(s);
  - c. Assess fines or other penalties;
  - d. Prohibit the utility from allowing its affiliate(s) to utilize the name and logo of the utility, either on a temporary or a permanent basis;
  - e. Apply any other remedy available to the Commission.

2. Any public utility which violates a provision of these rules is subject to a fine of not less than five hundred dollars (\$500), nor more than \$20,000 for each offense. The remainder of this subsection distills the principles that the Commission has historically relied upon in assessing fines and restates them in a manner that will form the analytical foundation for future decisions in which fines are assessed. Before discussing those principles, reparations are distinguished.

- a. Reparations

Reparations are not fines and conceptually should not be included in setting the amount of a fine. Reparations are refunds of excessive or discriminatory amounts collected by a public utility. PU Code § 734. The purpose is to return funds to the victim which were unlawfully collected by the public utility. Accordingly, the statute requires that all reparation amounts are paid to the victims. Unclaimed reparations generally escheat to the state, Code of Civil Procedure § 1519.5, unless equitable or other authority directs otherwise, e.g., Public Utilities Code § 394.9.

- b. Fines

The purpose of a fine is to go beyond restitution to the victim and to effectively deter further violations by this perpetrator or others.

### APPENDIX A-3

For this reason, fines are paid to the State of California, rather than to victims.

Effective deterrence creates an incentive for public utilities to avoid violations. Deterrence is particularly important against violations which could result in public harm, and particularly against those where severe consequences could result. To capture these ideas, the two general factors used by the Commission in setting fines are: (1) severity of the offense and (2) conduct of the utility. These help guide the Commission in setting fines which are proportionate to the violation.

#### i. Severity of the Offense

The severity of the offense includes several considerations. Economic harm reflects the amount of expense which was imposed upon the victims, as well as any unlawful benefits gained by the public utility. Generally, the greater of these two amounts will be used in establishing the fine. In comparison, violations which caused actual physical harm to people or property are generally considered the most severe, with violations that threatened such harm closely following.

The fact that the economic harm may be difficult to quantify does not itself diminish the severity or the need for sanctions. For example, the Commission has recognized that deprivation of choice of service providers, while not necessarily imposing quantifiable economic harm, diminishes the competitive marketplace such that some form of sanction is warranted.

Many potential penalty cases before the Commission do not involve any harm to consumers but are instead violations of reporting or compliance requirements. In these cases, the harm may not be to consumers but rather to the integrity of the regulatory processes. For example, compliance with Commission directives is required of all California public utilities:

### APPENDIX A-3

“Every public utility shall obey and comply with every order, decision, direction, or rule made or prescribed by the Commission in the matters specified in this part, or any other matter in any way relating to or affecting its business as a public utility, and shall do everything necessary or proper to secure compliance therewith by all of its officers, agents, and employees.” Public Utilities Code § 702.

Such compliance is absolutely necessary to the proper functioning of the regulatory process. For this reason, disregarding a statutory or Commission directive, regardless of the effects on the public, will be accorded a high level of severity.

The number of the violations is a factor in determining the severity. A series of temporally distinct violations can suggest an on-going compliance deficiency which the public utility should have addressed after the first instance. Similarly, a widespread violation which affects a large number of consumers is a more severe offense than one which is limited in scope. For a “continuing offense,” PU Code § 2108 counts each day as a separate offense.

#### ii. Conduct of the Utility

This factor recognizes the important role of the public utility’s conduct in (1) preventing the violation, (2) detecting the violation, and (3) disclosing and rectifying the violation. The public utility is responsible for the acts of all its officers, agents, and employees:

“In construing and enforcing the provisions of this part relating to penalties, the act, omission, or failure of any officer, agent, or employee of any public utility, acting within the scope of his [or her] official duties or employment, shall in every case be the act, omission, or failure of such public utility.” Public Utilities Code § 2109.

## APPENDIX A-3

(1) The Utility's Actions to Prevent a Violation. Prior to a violation occurring, prudent practice requires that all public utilities take reasonable steps to ensure compliance with Commission directives. This includes becoming familiar with applicable laws and regulations, and most critically, the utility regularly reviewing its own operations to ensure full compliance. In evaluating the utility's advance efforts to ensure compliance, the Commission will consider the utility's past record of compliance with Commission directives.

(2) The Utility's Actions to Detect a Violation. The Commission expects public utilities to monitor diligently their activities. Where utilities have for whatever reason failed to meet this standard, the Commission will continue to hold the utility responsible for its actions. Deliberate as opposed to inadvertent wrong-doing will be considered an aggravating factor. The Commission will also look at the management's conduct during the period in which the violation occurred to ascertain particularly the level and extent of involvement in or tolerance of the offense by management personnel. The Commission will closely scrutinize any attempts by management to attribute wrong-doing to rogue employees. Managers will be considered, absent clear evidence to the contrary, to have condoned day-to-day actions by employees and agents under their supervision.

(3) The Utility's Actions to Disclose and Rectify a Violation. When a public utility is aware that a violation has occurred, the Commission expects the public utility to promptly bring it to the attention of the Commission. The precise timetable that constitutes "prompt" will vary based on the nature of the violation. Violations which physically endanger the public must be immediately corrected and thereafter reported to the Commission staff. Reporting violations should be remedied at the earliest administratively feasible time. Prompt reporting of violations furthers the public interest by allowing for expeditious correction. For this reason, steps taken by a public utility to promptly and cooperatively report and correct violations may be considered in assessing any penalty.

## APPENDIX A-3

### iii. Financial Resources of the Utility

Effective deterrence also requires that the Commission recognize the financial resources of the public utility in setting a fine which balances the need for deterrence with the constitutional limitations on excessive fines. Some California utilities are among the largest corporations in the United States and others are extremely modest, one-person operations. What is accounting rounding error to one company is annual revenue to another. The Commission intends to adjust fine levels to achieve the objective of deterrence, without becoming excessive, based on each utility's financial resources.

### iv. Totality of the Circumstances in Furtherance of the Public Interest

Setting a fine at a level which effectively deters further unlawful conduct by the subject utility and others requires that the Commission specifically tailor the package of sanctions, including any fine, to the unique facts of the case. The Commission will review facts which tend to mitigate the degree of wrongdoing as well as any facts which exacerbate the wrongdoing. In all cases, the harm will be evaluated from the perspective of the public interest.

### v. The Role of Precedent

The Commission adjudicates a wide range of cases which involve sanctions, many of which are cases of first impression. As such, the outcomes of cases are not usually directly comparable. In future decisions which impose sanctions the parties and, in turn, the Commission will be expected to explicitly address those previously issued decisions which involve the most reasonably comparable factual circumstances and explain any substantial differences in outcome.

## IX. Protecting the Utility's Financial Health

- A. **Information from Utility on Necessary Capital.** Each utility shall provide to the Commission on the last business day of November of each year a report with the following information:

### APPENDIX A-3

1. the utility's estimate of investment capital needed to build or acquire long-term assets (i.e., greater than one year), such as operating assets and utility infrastructure, over each of the next five years;
  2. the utility's estimate of capital needed to meet resource procurement goals over each of the next five years;
  3. the utility's policies concerning dividends, stock repurchase and retention of capital for each year;
  4. the names of individuals involved in deciding corporate policies for the utility's dividends, stock repurchase and retention of capital;
  5. the process by which corporate policies concerning dividends, stock repurchase and retention of capital are implemented; and
  6. how the utility expects or intends to meet its investment capital needs.
- B. Restrictions on Deviations from Authorized Capital Structure.** A utility shall maintain a balanced capital structure consistent with that determined to be reasonable by the Commission in its most recent decision on the utility's capital structure. The utility's equity shall be retained such that the Commission's adopted capital structure shall be maintained on average over the period the capital structure is in effect for ratemaking purposes. Provided, however, that a utility shall file an application for a waiver, on a case by case basis and in a timely manner, of this Rule if an adverse financial event at the utility reduces the utility's equity ratio by 1% or more. In order to assure that regulatory staff has adequate time to review and assess the application and to permit the consideration of all relevant facts, the utility shall not be considered in violation of this Rule during the period the waiver is pending resolution. Nothing in this provision creates a presumption of either reasonableness or unreasonableness of the utility's actions which may have caused the adverse financial event.
- C. Ring-Fencing.** Within three months of the effective date of the decision adopting this amendment to the Rules, a utility shall obtain a non-consolidation opinion that demonstrates that the ring fencing around the utility is sufficient to prevent the utility from being pulled into bankruptcy of its parent holding company. The utility shall promptly provide the opinion to the Commission. If the current ring-fencing provisions are insufficient to obtain a non-consolidation opinion, the utility shall promptly undertake the following actions:
1. notify the Commission of the inability to obtain a non-consolidation opinion;

### APPENDIX A-3

2. propose and implement, upon Commission approval, such ring-fencing provisions that are sufficient to prevent the utility from being pulled into the bankruptcy of its parent holding company; and then

3. obtain a non-consolidation opinion.

**D. Changes to Ring-Fencing Provisions.** A utility shall notify the Commission of any changes made to its ring-fencing provisions within 30 days.

**(END OF APPENDIX A-3)**

Key to edits:

- 1) Base document is Appendix B to Proposed Decision.
- 2) Underlined or deleted text is change to base document (origin of change is Proposed Decision, November 7, 2007 AC/ALJ Ruling, or in parties' Comments).

**APPENDIX B-1**

GENERAL ORDER NO. 77-~~LM~~

(Supersedes General Order No. 77-~~KL~~)

Public Utilities Commission of the State of California

IN THE MATTER OF THE FILING WITH THE PUBLIC UTILITIES COMMISSION BY  
PUBLIC UTILITIES OF DATA ON COMPENSATION, DUES, DONATIONS,  
SUBSCRIPTIONS, CONTRIBUTIONS AND LEGAL FEES.

IT IS HEREBY ORDERED, That each public utility having gross annual operating revenues of more than \$500,000 but less than \$1 billion is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year:

- (a) the names titles and duties of all Executive Officers and the compensation received by each such Executive Officer; "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent; and
- (b) the names, titles and duties of all employees other than the officers named above who received compensation at the rate of \$85,000 or more per annum, and the compensation received by each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement.

IT IS HEREBY FURTHER ORDERED, That each public utility having gross annual operating revenues of \$1 billion or more and that is not an electric corporation or a gas corporation is directed and required to prepared and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year.

- (a) the names, titles and duties of all Executive Officers and the compensation received by each such Executive Officer; "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division, or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent; and
- (b) the names, titles and duties of all employees other than the officers named above who received compensation at the rate of \$125,000 or more per annum, and the compensation received by each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement.

Key to edits:

- 1) Base document is Appendix B to Proposed Decision.
- 2) Underlined or deleted text is change to base document (origin of change is Proposed Decision, November 7, 2007 AC/ALJ Ruling, or in parties' Comments).

IT IS HEREBY FURTHER ORDERED, That each public utility having gross annual operating revenues of \$1 billion or more and that is an electric corporation or a gas corporation is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before ~~March~~May 31 of each and every year a statement showing for the preceding calendar year:

- (a) the names, titles and duties of all Executive Officers and any other employees who received compensation including a base salary of \$250,000 or more per annum, and the total compensation<sup>1</sup> received, or awarded in the past year but not yet received, by each such Executive Officer or employee. "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division, or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent. Total compensation for each such Executive Officer and employee shall be reported by category and in the aggregate; and
- (b) the names, titles and duties of all employees other than the officers and employees named above who received compensation including a base salary of \$125,000 or more per annum, and the compensation received by each such employee, excluding pension and benefits but including the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such employee; and
- (c) the names, titles and duties of the principal Executive Officers of the utility's holding company whose compensation is listed in the holding company's proxy statement and the total compensation received, or awarded in the past year but not yet received, by each such Executive Officer. Total compensation for each such Executive Officer shall be reported by category and in the aggregate; and
- (d) the proportion of the compensation disclosed in response to subsection (a) or (c), above, that is paid, directly or indirectly, by the utility's ratepayers (e.g. 100% or some lesser percentage).
- (e) The information disclosed in response to subsection (a) shall be accompanied by a narrative statement in plain-English, explaining for the preceding calendar year, all elements of compensation, including the performance metrics or criteria used to determine incentive compensation.
- (f) The information disclosed in response to subsections (a) or (c), above, shall be accompanied by an independent auditor's letter verifying that all elements of total compensation are fully disclosed, clearly described and totally comprehensive.
- (g) At the option of each utility, the names of the Executive Officers and

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<sup>1</sup> For the purposes of this General Order, total compensation means all components of the officer's or other employee's compensation, such as cash compensation (including base salary and incentives) whether paid in the prior fiscal year or awarded but not yet paid, benefits (including medical, dental, vision, life insurance, disability, pension, and savings plans), holdings of equity-related interests that relate to compensation or are potential sources of future gains, any other retirement or other post-employment benefits, and any expense account or other perquisite, whether paid directly or indirectly. The foregoing examples are not exclusive.

Key to edits:

- 1) Base document is Appendix B to Proposed Decision.
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employees subject to the reporting requirements in subsections (a) through (c) above may be listed in conditional access reports that will not be disclosed publicly in the absence of authorization by the Commission or a presiding officer during the course of a proceeding or by the Commission if no proceeding is pending, on the condition that the utility also files a report for public inspection in which the individual names are redacted.

(h) Each utility shall provide an internet site-link to all publicly available compensation documents filed with the Securities and Exchange Commission and with the California Public Utilities Commission.

IT IS HEREBY FURTHER ORDERED, that each public utility having gross annual operating revenues of \$500,000 or more is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year, the following information:

- (a) the total dues, donations, subscriptions and contributions of all kinds paid directly, or paid to each officer or employee as reimbursement for said items; the names of persons, associations, firms or corporations receiving such payments directly or indirectly; and the amount of, and account charged, for each such payment; and
- (b) the total payments to attorneys, including all attorneys who are on the payroll of the reporting public utility or who are on the payroll of or receiving payment from any corporation affiliated with the reporting public utility; the name of each attorney or legal firm receiving such payment; and the amount of, and account charged, for the total amount paid to each of said attorneys or legal firms; and
- (c) utilities conducting more than one type of utility or nonutility operation shall report the information relating to dues, donations, subscriptions, contributions, and payments to attorneys and legal firms on a total company basis, segregated by type of operations.

**EXEMPTIONS:** The provisions of this general order do not apply to competitive local exchange carriers (telephone), non-dominant interexchange carriers (telephone), non-dominant gas storage companies, commercial radio service providers, Class I railroad corporations, and any other utility or class of utility specifically exempted by formal order of the Commission.

**(END OF APPENDIX B-1)**

Key to edits:

- 1) Base document is current GO 77-L (D.04-08-055 as modified by D.05-04-030).
- 2) Underlined or deleted text is change to base document (origin of change in Proposed Decision, November 7, 2007 AC/ALJ Ruling, or in parties' Comments).

**APPENDIX B-2**

GENERAL ORDER NO. 77-~~LM~~

(Supersedes General Order No. 77-~~KL~~)

Public Utilities Commission of the State of California

IN THE MATTER OF THE FILING WITH THE PUBLIC UTILITIES COMMISSION BY  
PUBLIC UTILITIES OF DATA ON COMPENSATION, DUES, DONATIONS,  
SUBSCRIPTIONS, CONTRIBUTIONS AND LEGAL FEES.

IT IS HEREBY ORDERED, That each public utility having gross annual operating revenues of more than \$500,000 but less than \$1 billion is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year:-

- (a) the names titles and duties of all Executive ~~o~~Officers and the compensation received by each such Executive Officer; "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent; and
- (b) the names, titles and duties of all employees other than the officers named above who received compensation at the rate of \$85,000 or more per annum, and the compensation received by each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement.

IT IS HEREBY FURTHER ORDERED, That each public utility having gross annual operating revenues of \$1 billion or more and that is not an electric corporation or a gas corporation is directed and required to prepared~~d~~ and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year:-

- (a) the names, titles and duties of all Executive Officers and the compensation received by each such Executive Officer; "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division, or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent; and
- (b) the names, titles and duties of all employees other than the officers named above who received compensation at the rate of \$125,000 or more per annum, and the compensation received by each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement.

Key to edits:

- 1) Base document is current GO 77-L (D.04-08-055 as modified by D.05-04-030).
- 2) Underlined or ~~deleted~~ text is change to base document (origin of change in Proposed Decision, November 7, 2007 AC/ALJ Ruling, or in parties' Comments).

IT IS HEREBY FURTHER ORDERED, That each public utility having gross annual operating revenues of \$1 billion or more is directed and required to prepared and file with the Public Utilities Commission of the State of California on or before May 31 of each and every year a statement showing for the preceding calendar year:

(a) the names, titles and duties of all Executive Officers and any other employees who received compensation including a base salary of \$250,000 or more per annum, and the total compensation<sup>1</sup> received, or awarded in the past year but not yet received, by each such Executive Officer or employee;. "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division, or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent. Total compensation for each such Executive Officer and employee shall be reported by category and in the aggregate; and

(b) the names, titles and duties of all employees other than the officers and employees named above who received compensation including a base salary at the rate of \$125,000 or more per annum, and the compensation received by each such employee;. excluding pension and benefits but including the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such employee; and

(c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement the names, titles and duties of the principal Executive Officers of the utility's holding company whose compensation is listed in the holding company's proxy statement and the total compensation received, or awarded in the past year but not yet received, by each such Executive Officer. Total compensation for each such Executive Officer shall be reported by category and in the aggregate; and

(d) the proportion of the compensation disclosed in response to subsection (a) or (c), above, that is paid, directly or indirectly, by the utility's ratepayers (e.g. 100% or some lesser percentage).

(e) The information disclosed in response to subsection (a) shall be accompanied by a narrative statement in plain-English, explaining for the preceding calendar year, all elements of compensation, including the performance metrics or criteria used to determine incentive compensation.

(f) The information disclosed in response to subsections (a) or (c), above, shall be accompanied by an independent auditor's letter verifying that all elements of total compensation are fully disclosed, clearly described and totally comprehensive.

<sup>1</sup> For the purposes of this provision of the General Order, total compensation means all components of the officer's or other employee's compensation, such as cash compensation (including base salary and incentives) whether paid in the prior fiscal year or awarded but not yet paid, benefits (including medical, dental, vision, life insurance, disability, pension, and savings plans), holdings of equity-related interests that relate to compensation or are potential sources of future gains, any other retirement or other post-employment benefits, and any expense account or other perquisite, whether paid directly or indirectly. The foregoing examples are not exclusive.

Key to edits:

- 1) Base document is current GO 77-L (D.04-08-055 as modified by D.05-04-030).
- 2) Underlined or deleted text is change to base document (origin of change in Proposed Decision, November 7, 2007 AC/ALJ Ruling, or in parties' Comments).

(g) At the option of each utility, the names of the Executive Officers and employees subject to the reporting requirements in subsections (a) through (c) above may be listed in conditional access reports that will not be disclosed publicly in the absence of authorization by the Commission or a presiding officer during the course of a proceeding or by the Commission if no proceeding is pending, on the condition that the utility also files a report for public inspection in which the individual names are redacted.

(gh) Each utility shall provide an internet site-link to all publicly available compensation documents filed with the Securities and Exchange Commission and with the California Public Utilities Commission.

IT IS HEREBY FURTHER ORDERED, that each public utility having gross annual operating revenues of \$500,000 or more is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year, the following information:

- (a) the total dues, donations, subscriptions and contributions of all kinds paid directly, or paid to each officer or employee as reimbursement for said items; the names of persons, associations, firms or corporations receiving such payments directly or indirectly; and the amount of, and account charged, for each such payment; and
- (b) the total payments to attorneys, including all attorneys who are on the payroll of the reporting public utility or who are on the payroll of or receiving payment from any corporation affiliated with the reporting public utility; the name of each attorney or legal firm receiving such payment; and the amount of, and account charged, for the total amount paid to each of said attorneys or legal firms; and
- (c) utilities conducting more than one type of utility or nonutility operation shall report the information relating to dues, donations, subscriptions, contributions, and payments to attorneys and legal firms on a total company basis, segregated by type of operations.

EXEMPTIONS: The provisions of this general order do not apply to competitive local exchange carriers (telephone), non-dominant interexchange carriers (telephone), non-dominant gas storage companies, commercial radio service providers, Class I railroad corporations, and any other utility or class of utility specifically exempted by formal order of the Commission.

**(END OF APPENDIX B-2)**

## APPENDIX B-3

GENERAL ORDER NO. 77-M

(Supersedes General Order No. 77-L)

Public Utilities Commission of the State of California

IN THE MATTER OF THE FILING WITH THE PUBLIC UTILITIES COMMISSION BY  
PUBLIC UTILITIES OF DATA ON COMPENSATION, DUES, DONATIONS,  
SUBSCRIPTIONS, CONTRIBUTIONS AND LEGAL FEES.

IT IS HEREBY ORDERED, That each public utility having gross annual operating revenues of more than \$500,000 but less than \$1 billion is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year:

- (a) the names titles and duties of all Executive Officers and the compensation received by each such Executive Officer; "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent; and
- (b) the names, titles and duties of all employees other than the officers named above who received compensation at the rate of \$85,000 or more per annum, and the compensation received by each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement.

IT IS HEREBY FURTHER ORDERED, That each public utility having gross annual operating revenues of \$1 billion or more and that is not an electric corporation or a gas corporation is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year:

- (a) the names, titles and duties of all Executive Officers and the compensation received by each such Executive Officer; "Executive Officer" includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division, or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent; and
- (b) the names, titles and duties of all employees other than the officers named above who received compensation at the rate of \$125,000 or more per annum, and the compensation received by each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement.

IT IS HEREBY FURTHER ORDERED, That each public utility having gross annual operating revenues of \$1 billion or more is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before May 31 of each and every year a statement showing for the preceding calendar year:

- (a) the names, titles and duties of all Executive Officers and any other employees who received compensation including a base salary of \$250,000 or more per annum, and the total compensation<sup>1</sup> received, or awarded in the past year but not yet received, by each such Executive Officer or employee. “Executive Officer” includes the President, Secretary, Treasurer, and Vice President in charge of a principal business unit, division, or function of the respondent. It also includes any other person who performs policy making functions and is employed by the respondent. Total compensation for each such Executive Officer and employee shall be reported by category and in the aggregate; and
- (b) the names, titles and duties of all employees other than the officers and employees named above who received compensation including a base salary at the rate of \$125,000 or more per annum, and the compensation received by each such employee, excluding pension and benefits but including the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such employee; and
- (c) the amount of the expense account, any contingent fees or other moneys directly or indirectly paid to each such officer and employee named in the statement the names, titles and duties of the principal Executive Officers of the utility’s holding company whose compensation is listed in the holding company’s proxy statement and the total compensation received, or awarded in the past year but not yet received, by each such Executive Officer. Total compensation for each such Executive Officer shall be reported by category and in the aggregate; and
- (d) the proportion of the compensation disclosed in response to subsection (a) or (c), above, that is paid, directly or indirectly, by the utility’s ratepayers (e.g. 100% or some lesser percentage).
- (e) The information disclosed in response to subsection (a) shall be accompanied by a narrative statement in plain-English, explaining for the preceding calendar year, all elements of compensation, including the performance metrics or criteria used to determine incentive compensation.
- (f) The information disclosed in response to subsections (a) or (c), above, shall be accompanied by an independent auditor’s letter verifying that all elements of total compensation are fully disclosed, clearly described and totally comprehensive.
- (g) At the option of each utility, the names of the Executive Officers and employees subject to the reporting requirements in subsections (a) through (c) above may be listed in conditional access reports that will not be disclosed publicly in the absence of authorization by the Commission or a presiding officer during the course of a proceeding or by the Commission if no proceeding is pending, on the

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<sup>1</sup> For the purposes of this provision of the General Order, total compensation means all components of the officer’s or other employee’s compensation, such as cash compensation (including base salary and incentives) whether paid in the prior fiscal year or awarded but not yet paid, benefits (including medical, dental, vision, life insurance, disability, pension, and savings plans), holdings of equity-related interests that relate to compensation or are potential sources of future gains, any other retirement or other post-employment benefits, and any expense account or other perquisite, whether paid directly or indirectly. The foregoing examples are not exclusive.

condition that the utility also files a report for public inspection in which the individual names are redacted.

(h) Each utility shall provide an internet site-link to all publicly available compensation documents filed with the Securities and Exchange Commission and with the California Public Utilities Commission.

IT IS HEREBY FURTHER ORDERED, that each public utility having gross annual operating revenues of \$500,000 or more is directed and required to prepare and file with the Public Utilities Commission of the State of California on or before March 31 of each and every year a statement showing for the preceding calendar year, the following information:

(a) the total dues, donations, subscriptions and contributions of all kinds paid directly, or paid to each officer or employee as reimbursement for said items; the names of persons, associations, firms or corporations receiving such payments directly or indirectly; and the amount of, and account charged, for each such payment; and

(b) the total payments to attorneys, including all attorneys who are on the payroll of the reporting public utility or who are on the payroll of or receiving payment from any corporation affiliated with the reporting public utility; the name of each attorney or legal firm receiving such payment; and the amount of, and account charged, for the total amount paid to each of said attorneys or legal firms; and

(c) utilities conducting more than one type of utility or nonutility operation shall report the information relating to dues, donations, subscriptions, contributions, and payments to attorneys and legal firms on a total company basis, segregated by type of operations.

EXEMPTIONS: The provisions of this general order do not apply to competitive local exchange carriers (telephone), non-dominant interexchange carriers (telephone), non-dominant gas storage companies, commercial radio service providers, Class I railroad corporations, and any other utility or class of utility specifically exempted by formal order of the Commission.

**(END OF APPENDIX B-3)**

Response No. PSC-004  
Attachment PSC-004 (LIB-C)

Decision 10-10-017 October 14, 2010

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

Joint Application of Sierra Pacific Power Company (U903E) and California Pacific Electric Company, LLC for Transfer of Control and Additional Requests Relating to Proposed Transaction.

Application 09-10-028  
(Filed October 16, 2009)

And Related Matters.

Application 10-04-032  
(Filed April 30, 2010)

**DECISION CONDITIONALLY APPROVING  
CONSOLIDATED APPLICATIONS**

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## **LIST OF APPENDICES**

Appendix 1 - List of Abbreviations and Acronyms

Appendix 2 - CalPeco Ownership Structure

Appendix 3 - Regulatory Commitments

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**DECISION CONDITIONALLY APPROVING  
CONSOLIDATED APPLICATIONS**

**1. Summary**

Subject to the following conditions, we approve the transfer to California Pacific Electric Company, LLC (CalPeco) of the California electric distribution facilities and the Kings Beach Generating Station owned by Sierra Pacific Power Company (Sierra):

- Power from Sierra's Valmy Power Plant may be included in the supply provided under the Power Purchase Agreement and any additional power purchase agreement which Sierra and CalPeco may enter upon the expiration of the initial five-year agreement as long as Sierra makes no new ownership investment in Valmy, within the context of the Emissions Performance Standard rules adopted in Decision 07-01-039 and any relevant, subsequent modifications of that decision;
- The Internal Transfer Authority is not approved and any change of ownership affecting CalPeco's upstream owners must be sought by application filed pursuant to Public Utilities Code Section 854;
- CalPeco and its upstream owners must expressly recognize the Commission's legal right to call their officers and employees to testify in California regarding matters pertinent to CalPeco, consistent with established principles of due process and fundamental fairness.

In all other respects we approve the authority sought in the transfer application, as amended in the course of this proceeding and as conditioned by the Regulatory Commitments attached to this decision as Appendix 3. Joint Applicants have established that the transfer will not harm ratepayers; in fact, certain service improvements are likely in the near term, at no cost to ratepayers.

We also approve the two ancillary agreements involving Sierra, CalPeco and Truckee-Donner Public Utility District in order to permit the continued

cooperation that permits cost-effective, reliable service to customers in both of these contiguous, small service territories.

## **2. Identification of Parties**

### **2.1. Overview**

For ease of discussion, today's decision generally refers to Application (A.) 09-10-028, which asks the Commission to approve a change in public utility ownership and control, as the transfer application.

The three active parties include the proposed seller, Sierra Pacific Power Company (Sierra) and the proposed buyer, California Pacific Electric Company, LLC (CalPeco).<sup>1</sup> We refer to these project proponents, collectively, as Joint Applicants. The third active party, the Commission's Division of Ratepayer Advocates (DRA), opposes the transfer from Sierra to CalPeco.

Several other parties initially protested the proposed transfer, but all of them reached settlements with Joint Applicants and withdrew their protests prior to evidentiary hearing. These parties include Truckee-Donner Public Utilities District (TDPUD), which withdrew its protest on February 22, 2010, and the following entities, referred to as Aligned Protestants, which collectively withdrew their individual protests on March 29, 2010: the City of Loyalton, the City of Portola, Plumas County, Sierra County, and Plumas-Sierra Rural Electric Cooperative (PSREC).

We are aware that two other entities, which are not parties, have submitted letters of support for the proposed transfer and urge us to approve it - the International Brotherhood of Electrical Workers Local Union 1245 (Local

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<sup>1</sup> Appendix 1 contains a list of the abbreviations and acronyms used in today's decision.

1245), whose members work for Sierra and have been offered continued employment by CalPeco, and Sierra Pacific Industries, which owns a 14 megawatt (MW) biomass cogeneration facility in the City of Loyalton. Sierra Pacific Industries previously wrote to oppose the transfer but subsequently has resolved its dispute with Sierra and now supports the transfer.<sup>2</sup>

## **2.2. Sierra**

Sierra is a public utility that generates, transmits and distributes electricity to some 366,000 customers in northern Nevada and California; Sierra also serves about 150,000 natural gas customers in Reno and Sparks, Nevada. Organized as a Nevada corporation, Sierra is wholly-owned by NV Energy Inc. (NV Energy), an investor-owned holding company incorporated under Nevada law. NV Energy has five other, wholly-owned subsidiaries, including Nevada Power, the regulated public utility which serves Las Vegas and southern Nevada. In total, NV Energy serves about 1.2 million customers in Nevada.

Sierra's California retail electric customer base encompasses about 46,000 customers in seven counties (Nevada, Placer, Sierra, Plumas, Mono, Alpine and El Dorado), with approximately 80% of those customers located in the Lake Tahoe Basin. Sierra's California service territory is a winter-peaking load; the mountainous terrain rises from nearly 5,000 feet to 9,000 feet and most customers are located at elevations above 6,000 feet. In addition, the California service territory is outside the control area of the California Independent System Operator. Electricity generated in Nevada and delivered into California through

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<sup>2</sup> These letters have been placed in the correspondence file for this docket.

Sierra's transmission facilities is the source of most of the electric power supplied to the California service territory.

### **2.3. CalPeco**

CalPeco is a newly created, California limited liability company directly owned by California Pacific Utility Ventures, LLC, a California limited liability company. CalPeco's ultimate, indirect owners are two publicly traded Canadian companies -- Algonquin Power & Utilities Corp. (Algonquin) and Emera Incorporated (Emera). These entities' will hold their indirect ownership stakes -- 50.001% by Algonquin and 49.999% by Emera -- through their respective, wholly owned subsidiaries, Liberty Electric Co. and Emera US Holdings, Inc., both Delaware corporations.<sup>3</sup> Appendix 2 to today's decision illustrates this ownership chain.

Initially formed in 1987, Algonquin is a diversified electrical power generation and utility infrastructure company with a principal place of business in Toronto, Ontario. According to the transfer application: "Algonquin owns

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<sup>3</sup> The Algonquin and Emera 50%/50% ownership arrangement initially described in the transfer application has changed. Joint Applicants explain:

This change results from Canada transitioning to the International Financial Reporting Standards in 2011. Algonquin and Emera have determined that enabling Algonquin to "control" CalPeco within the meaning of these accounting standards facilitates Algonquin being authorized to account for its investment in CalPeco on a fully-consolidated basis and enables Emera to use equity consolidation treatment." (Exhibit (Ex.) 3 at 6.)

In addition, the chain of ownership of CalPeco on the Algonquin side has changed. According to the transfer application, initially Algonquin planned for its subsidiary, Algonquin Power Fund (America) Inc., to directly hold CalPeco. However, Algonquin subsequently had that subsidiary transfer 100% of its ownership interest in CalPeco to another Algonquin subsidiary, Liberty Electric Co.

and operates an approximately \$1 billion (Cdn) portfolio of renewable power generation and utility operations across North America. Over 50% of Algonquin's revenues are generated through its US-based operations."<sup>4</sup> Algonquin has two business units, a Power Generation unit that includes 45 renewable power generating facilities and 16 high-efficiency thermal generating facilities in four states and four Canadian provinces, and a Utility Services unit that owns and operates regulated water and sewer utility systems in four states.<sup>5</sup> At hearing, Joint Applicants' witness testified that the recent acquisition of a water and wastewater system in Texas has increased Algonquin's regulated utility business to 19 systems with 75,000 total customers.

Following its conversion on October 27, 2009, to a conventional, publicly traded corporation, Algonquin now trades under the symbol "AQN" on the Toronto Stock Exchange. Previously, Algonquin was known as Algonquin Power Income Fund, a mutual fund trust established under the laws of the Province of Ontario, Canada.

Emera, incorporated under the laws of the Province of Nova Scotia, Canada, is an energy holding company with a principal place of business in Halifax, Nova Scotia. According to the transfer application, Emera holds "approximately \$5.3 billion of assets (Cdn)" and "owns and operates utilities participating in the generation, transmission and distribution of electricity; utilities participating in the transmission of natural gas; and unregulated

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<sup>4</sup> Transfer Application at 4.

<sup>5</sup> In California, Algonquin owns the Sanger Cogeneration project, a 56 MW natural gas-fired facility near Fresno. Sanger sells power to Pacific Gas and Electric Company under a Commission-approved standard offer contract that will expire in 2012.

businesses participating in the energy marketing and electric generation.”<sup>6</sup> Emera has over 130 years of experience in owning and operating utility assets, a safety record nationally recognized in Canada, and extensive experience in partnership and joint ownership arrangements, including a 600 MW pumped storage facility in northern Massachusetts.

Regarding the relationship with Algonquin, Joint Applicants state:

Emera is engaged in a strategic partnership with Algonquin through which the companies may collaborate in select utility infrastructure and renewable generation investment, such as the proposed co-ownership of CalPeco. Emera has also agreed to acquire a 9.9% interest in Algonquin upon Closing.<sup>7</sup>

The transfer application does not name CalPeco’s direct owner, California Pacific Utility Ventures, LLC, or its indirect owners, Emera, Algonquin and their subsidiaries, as applicants. DRA’s opening brief raises this, for the first time, as a fatal flaw that must be corrected by amendment of the transfer application to name each of these entities. According to DRA, Public Utilities Code Section 854(a) requires such amendment.<sup>8</sup>

Section 854(a) provides, in relevant part:

No person or corporation, whether or not organized under the laws of this state, shall merge, acquire, or control either directly or indirectly any public utility organized and doing business in this state without first securing authorization to do so from the commission ... Any merger, acquisition, or control without that prior authorization shall be void and of no effect ...

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<sup>6</sup> Transfer Application at 5.

<sup>7</sup> Transfer Application at 7.

<sup>8</sup> Unless otherwise noted, all subsequent references to a statutory section or sections are to the California Public Utilities Code.

Joint Applicants' reply brief argues that DRA's contention is not only untimely but also incorrect. According to Joint Applicants, only when an upstream owner is being sold, resulting in a change of indirect ownership, must the application name indirect owners. Neither brief cites authority.

Joint Applicants also state that there is no substantive need to amend the application. They point out that Algonquin and Emera have been active participants in this proceeding from the beginning, have voluntarily presented senior executives as witnesses at hearing, and have conceded the Commission's jurisdiction to enforce the various promises and representations, termed Regulatory Commitments (see Appendix 3 to today's decision), that CalPeco and its direct and indirect owners have made to customers and to the Commission.

We need not undertake an exhaustive statutory analysis here, where CalPeco's owners are not contesting the Commission's jurisdiction. However, when a utility tier transfer results in new indirect owners for that utility, we think naming all such entities as applicants is the better practice, and we urge the Docket Office and our administrative law judges to be more vigilant in ensuring that this better practice is broadly and consistently followed.<sup>9</sup> Because Joint Applicants have fully disclosed the existence of California Pacific Utility Ventures, LLC, as well as Emera and Algonquin and their immediate subsidiaries in the chain of control of CalPeco, have presented witnesses from

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<sup>9</sup> See for example, *Joint Application of California-American Water Company, RWE Aktiengesellschaft, Thames Water Aqua Holdings GmbH, Thames Water Plc, and Apollo Acquisition Company to merge with and into American Water Works Company, resulting in a change of control of California-American Water Company*, D.02-12-068 (2002). The merger between the parent of CalAm and the subsidiary of RWE, resulted in RWE and each intervening subsidiary obtaining indirect control of CalAm and all were named as applicants.

Algonquin and Emera, and have placed issues concerning these entities directly before the Commission for decision, our ability to fully consider this transfer has not been circumscribed. We intend that the reach of today's decision extend to the direct and indirect owners of CalPeco and will require their assent as a condition of any authority granted in the Ordering Paragraphs.

### **3. Summary of Authority Sought**

Sierra proposes to transfer to CalPeco ownership and operation of Sierra's California service territory and all distribution assets, as well as the King's Beach Generating Station (King's Beach facility), a 12-MW diesel-fired generator located in King's Beach near Lake Tahoe (collectively, the California Utility).

The transfer application describes the transaction as "functionally the sale of Sierra's entire Commission-jurisdictional utility."<sup>10</sup> The sales price, to be calculated more precisely based upon various factors including outstanding accounts payables and accounts receivables at closing, is estimated to range between approximately \$132 and \$137 million. CalPeco commits not to seek to recover in rates either the premium paid for the assets of the California Utility or any transactions costs. CalPeco commits to ask, in a future 2012 CalPeco general rate case, that the Commission establish the revenue requirement according to the dollar value of CalPeco's rate base, not the purchase price, and that those subsequent ratemaking computations include any cost savings CalPeco may have realized, compared to the pre-savings baseline in Sierra's last general rate case. Appendix 3 of today's decision lists these and all other Regulatory Commitments by CalPeco and its owners. The transfer application also

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<sup>10</sup> Transfer Application at 19.

incorporates seven agreements, referred to collectively as the Operating Agreements, and asks the Commission to make certain findings about them concurrent with approval of the transfer.

We have consolidated the transfer application with A.10-04-032, which seeks approval of two ancillary agreements resulting from Joint Applicants' settlement with TDPUD. The ancillary agreements, termed the Fringe Agreement and the Reliability Support Agreement, are structured to ensure the continuation of existing, cooperative arrangements that benefit the contiguous service territories of both, small electric utilities.

Today's decision reviews the transfer application first because the ancillary agreements are dependent upon it in substantial part. Our discussion of the transfer application begins in Section 5. Our discussion of the ancillary agreements begins in Section 6.

#### **4. Standard of Review**

No party disputes that we should apply § 854, which generally governs mergers and similar transfers of control, rather than § 851, which typically governs sales of assets. In fact, Joint Applicants explain that they have structured the transaction as a sale of all California-jurisdictional assets, rather than a merger or sale of stock, simply because the California Utility is not organized, legally, as a separate entity from Sierra. Review under § 854 is consistent with the Commission's procedural approach in Decision (D.) 05-03-010, where the Commission approved the sale of Avista Corporation's South Lake Tahoe gas facilities (the California portions of Avista's multi-state utility operations) to Southwest Gas Corporation.

Consistent with the scoping memo, our review of the transfer under § 854 focuses on § 854(a), which we quote in relevant part in Section 2.3, above. Thus,

to approve the proposed transfer of control, the Commission must find that the proposal meets the public interest standard that prior Commission decisions define for § 854(a). Typically the Commission has required an applicant to show that a proposed transfer is “not adverse to the public interest” though occasionally the Commission has articulated the standard as requiring a showing that a transfer is “in the public interest.”<sup>11</sup> The scoping memo directed the parties to brief these alternative terms, if they contend that the distinction is material.

The parties’ witness testimony and briefs recast this nuanced disagreement as a much more fundamental one centered on whether the public interest requires a showing of “no harm to ratepayers” (Joint Applicants’ contention) or “positive benefits to ratepayers and the community” (DRA’s contention). DRA argues that the Commission should require showings on at least some of the criteria that §§ 854(b) and (c) specify for inquiry when one or more parties to a proposed transfer has gross California revenues of more than \$500 million, and moreover, that these showings should establish that the transfer yields net benefits to ratepayers compared to the status quo.<sup>12</sup> DRA does not dispute that

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<sup>11</sup> See for example, D.07-05-031, which approved the transfer of control over California-American Water Company (CalAm) at the holding company level:

The primary standard used by the commission to determine if a transaction should be authorized under § 854(a) is whether the transaction will adversely affect the public interest. (D.07-05-031 at 3, citing D.00-06-079 at 13.)

<sup>12</sup> Section 854(b) requires the Commission to find short-term and long-term benefits for ratepayers, an equitable allocation of such benefits between shareholders and ratepayers, and no adverse impact upon competition. Section 854(c) requires that the public interest assessment result in express findings on eight criteria (impact on the financial condition of the resulting utility, on service quality, on management quality, on utility employees, on shareholders, on state and local economies, on the

*Footnote continued on next page*

Sierra's 2008 annual California revenues were approximately \$72 million or that CalPeco had no California revenues. DRA relies on two prior Commission decisions: D.01-09-057, which authorized California-American Water Company (CalAm) to acquire Citizens Utilities Company of California and D.06-02-033, which authorized PacifiCorp's acquisition by MidAmerican Energy Holdings Company (MidAmerican). Neither decision establishes a positive benefits test for transactions such as the proposed Sierra/CalPeco transfer.

The first decision DRA cites, D.01-09-057, concerns the acquisition of one water utility by another under § 854(a) and the Public Water System Investment and Consolidation Act of 1997, consisting of §§ 2718-2720 (the Act). The Act authorizes the post-acquisition rate base of a transferred water distribution system to be set at fair market value, which in some instances may be higher than the historical value, and which therefore places an additional cost on ratepayers. Before approving such a rate base increase the Commission must find that the transaction proposed improves the health and stability of the water system in several enumerated ways, thereby benefiting ratepayers. The Office of Ratepayer Advocates, the predecessor of DRA, argued that the Commission could - and should -- look to the criteria listed in § 854(b) and (c) in assessing ratepayer value. CalAm argued that the Commission's long-term standard requires a showing of no harm to ratepayers and that its proposal clearly met

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Commission's jurisdiction, and on whether any proposed mitigations avoid adverse consequences). For a proposed transaction to gain approval, review of the first three criteria must result in findings that the transfer will "maintain or improve" the status quo; review of the second three criteria must result in findings that the transfer is "fair and reasonable."

that test, but also would meet a positive ratepayer benefits standard. Regarding the appropriate standard, Conclusion of Law 9 in D.01-09-057 merely states:

Sections 854(b) and 854(c) do not by their terms apply to water utilities. The Commission may, but need not, consider the extent to which the factors set forth in those sections bear on the public interest in this proceeding.

Furthermore, while D.01-09-057 summarizes information the applicants had put forward on some § 854(c) criteria, the decision does not tie its public interest findings or approval to § 854(c).

The second decision DRA cites, D.06-02-033, concerns a transfer at the holding company level by which MidAmerican acquired indirect ownership and control of PacifiCorp, an energy utility, from Scottish Power PLC. The decision observes that no entity to the transaction has sufficient California revenues to trigger application of § 854(b) and (c) and it does not discuss either subsection further. The decision's public interest assessment begins by setting out seven criteria to be considered given the facts of the transfer at issue, however, and simple comparison of these criteria with those in § 854(b) and (c) shows an overlap. D.06-02-033 focuses on the proposed transaction's impact on: the financial condition of the utility, service quality, management quality, affected utility employees, the state of California and local communities, Commission jurisdiction, and competition. D.06-02-033 states:

Although we are not obligated to use the above criteria to evaluate the proposed transaction, these criteria provide a useful framework for analyzing the transaction. Our use of the above

criteria is completely discretionary, and we may choose to use none, some, or all of these criteria in future proceedings.<sup>13</sup>

After assessing the evidence put forward, D.06-02-033 concludes that the transaction should be approved and rejects DRA's contention that the benefits are "meager" or insufficient:

The transaction provides modest but concrete benefits to ratepayers and the communities served by PacifiCorp, and there will be no harm to ratepayers or others with the conditions adopted by today's Decision. This is enough for the proposed transaction to garner our approval under § 854(a).<sup>14</sup>

Though we address Joint Applicants' showing in Section 5, we observe here that the transfer application, as filed, addresses each of the criteria examined in D.06-02-033.

Similarly, in D.00-06-079, which issued more than a decade ago, the Commission observed "... our decisions over the years have laid out a number of factors that should be considered in making the determination of whether a transaction will be adverse to the public interest."<sup>15</sup> D.00-06-079 mentions several factors -- antitrust considerations, economic and financial feasibility, purchase price, value of consideration exchanged, efficiencies, operating costs savings - and there are others. Clearly, not every one of them is relevant to every review under § 854(a).

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<sup>13</sup> D.06-02-033 at 23.

<sup>14</sup> D.06-02-033 at 36.

<sup>15</sup> D.00-06-079 at 14.

The parties' dispute about the standard of review applicable to the transfer application suggests confusion about several distinct concepts and so, based on the foregoing review of precedent, we provide the following guidance.

First, to ensure that a proposed transfer is not adverse to the public interest under § 854(a), the Commission must be able to evaluate evidence on the important impacts of that transfer – whatever they might be – and find no harm to ratepayers. Second, some of the criteria enumerated in §§ 854(b) and (c) mirror criteria identified by past Commission decisions as relevant to a public interest assessment under § 854(a), and depending upon the nature of the transfer at issue, may well be relevant and even necessary to the specific public interest assessment required. Third, only where §§ 854(b) and (c) expressly apply, must the Commission make all of the findings those subsections require.

Next, we turn to § 854(d), which in relevant part, requires the Commission to “consider reasonable options to the proposal recommended by other parties.” Initially PSREC challenged the proposed transfer and argued that it should be allowed to purchase the Loyalton/Portola portion of Sierra's California service territory. However, following a meeting held in the Loyalton/Portola area pursuant to the scoping memo's direction, PSREC and Joint Applications settled their differences.<sup>16</sup> PSREC, which withdrew its opposition to the transfer application before evidentiary hearings and without having put forward prepared testimony on its alternative proposal, now urges us to authorize the transfer. No other party has introduced facts to describe any alternative for us to consider under 854(d). Though DRA opposes the transfer and urges us to reject

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<sup>16</sup> The PSREC Settlement Agreement is Exhibit Q to Exhibit 1.

it, we have that authority already under § 854(a). Specifically, were we to determine that Joint Applicants have failed to show that the transfer is not adverse to the public interest, we would be obliged to deny it, unless conditions could be imposed to cure the identified defect(s). Given the procedural status of the transfer application, § 854(d) is no longer pertinent to our review.

Section 816 and § 818, which concern issuance of stocks, bonds, etc., and § 851, which as relevant here concerns the encumbrance of utility assets, provide the statutory basis for the financing authority sought. No dispute exists here.

Finally, we address application of Public Resources Code § 21080 et seq., known as of the California Environmental Quality Act (CEQA). Joint Applicants' assert and no party contests that the transfer of control of the California Utility from Sierra to CalPeco "will not result in any change in the operation of the public utility serving these California customers ... [and] does not request any new construction, or changes in the use of existing assets and facilities."<sup>17</sup> We find no evidence that operational change will result and no new facilities are proposed. Pursuant to § 15061(b)(3) of the CEQA guidelines, inasmuch as it can be seen with certainty that the project will have no significant impact upon the environment, the transfer application qualifies for an exemption from CEQA and the Commission need not perform any further environmental review.

Joint Applicants have the burden of proof to establish that the Commission should approve the transfer application and the ancillary agreements.

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<sup>17</sup> Transfer Application at 72.

## **5. The Transfer Application: Discussion**

Below we review Joint Applicants' explanation for why they and their owners seek this transfer, the evidence Joint Applicants have offered in support of the transfer, and the basis for DRA's opposition. The discussion largely follows the common organizational outline the parties' use in their concurrent briefs.

### **5.1. Reason for the Transfer**

According to the transfer application and witness testimony, Sierra wishes to sell the California Utility to enable its owner, NV Energy, to focus on Nevada operations, which now extend to most of that state. Load growth in Nevada has required NV Energy to invest an average of \$1 billion annually over the past five years to maintain reliable service to the nearly 1.2 million customers it now serves there. Because that load growth has been heaviest in areas that do not border Lake Tahoe (where most of the California Utility's 46,000 customers are located), California operations now serve less than 4% of NV Energy's customer base. The sale, if approved, also provides NV Energy the ability to consolidate all of its operations under a single state regulatory agency and respond to a single set of regulatory directives.

The transfer application describes the genesis of the proposed transaction. Sierra commenced a search in early 2008 for suitable, potential bidders and distributed bid information to an initial list of 40 entities. Sierra required any potential bidder to contractually agree to a list of regulatory commitments and to meet the following criteria:

- experience at operating, and the proven capability to operate, a distribution utility;
- the commitment and ability to continue to offer the same, or greater, level of service at comparable rates;

- the commitment and ability to carry out the regulatory initiatives and policies of California law and this Commission;
- a desire to focus primarily on California operations;
- the commitment and ability to maintain a strong local presence in the service territory within the Lake Tahoe area;
- the commitment and ability to retain Sierra's California labor force; a long-term business objective to operate an electric distribution utility; and
- in general, the abilities, qualifications, and characteristics that would best ensure that the Commission would approve the transaction and entrust the purchaser with the responsibility to provide service to Sierra's California customers and to be the employer for Sierra's California employees.<sup>18</sup>

Sierra received non-binding bids from seven entities and short-listed four of them, based on review of various criteria (price, bid viability, the completeness of the bid, the bidder's financial and operational qualifications, etc.). Following further review of these criteria and others (impact on employees and customers, etc.), Algonquin emerged as the entity with the best "overall fit."

<sup>19</sup> In late 2008, Sierra and Algonquin contemplated executing a purchase agreement, but against the backdrop of the continuing, global financial crisis, Algonquin determined to form CalPeco jointly with Emera. Joint Applicants' witness readily admitted that like many other entities, Algonquin's stock price dropped during the fall of 2008 and its access to capital was impaired. The witness testified that Algonquin's board believed that a joint acquisition with

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<sup>18</sup> Transfer Application at 16-17. The complete, initial list (Ex. 17 to the transfer application) is an earlier version of the Regulatory Commitments found in Appendix 3 of today's decision.

<sup>19</sup> Transfer Application at 15.

Emera would be “prudent” but that the rationale was not based solely on Emera’s financial strength.<sup>20</sup> The transfer application reports that the financial markets appear to have viewed the formation of CalPeco by Algonquin and Emera positively, based on stock prices and debt ratings following public announcement of their joint enterprise to purchase the California Utility.

The transfer application states that from the standpoint of CalPeco’s owners, Algonquin and Emera, the proposed transfer fits with their mutual business objectives to expand ownership and operation of regulated utility assets, with a view to long-term acquisition and, in some instances, opportunities “to develop and implement renewable energy initiatives.”<sup>21</sup> Further,

[F]or Emera, this transaction opens up a new market, while providing the opportunity to increase value to its jointly-owned energy infrastructure assets with Algonquin. For Algonquin, this transaction represent an important element in the strategic expansion of its utility infrastructure portfolio and the predictable, long-term related returns that the California Utility will contribute to the stability of its earnings year to year.<sup>22</sup>

DRA has not put forward evidence that challenges Joint Applicants’ explanation of the interest of either the sellers or the buyers in the proposed transaction.

## **5.2. Impact on Service**

Joint Applicants represent that the proposed transfer will continue safe and reliable service and will maintain, and in some instances improve, the

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<sup>20</sup> Tr. at 30.

<sup>21</sup> Transfer Application at 18.

<sup>22</sup> Transfer Application at 18-19.

quality of service customers experience today. Aligned Protestants, who are located in Loyaltan, Portola and adjacent portions of the California Utility's service territory and who raised the sole customer challenge to the proposed transfer, now support it. Initially they criticized the reliability of electric service in their remote area, claiming: (1) local generation is insufficient; (2) existing transmission cannot deliver sufficient power from more distant sources; and (3) field staffing (one person) cannot possibly handle the other kinds of equipment and infrastructure failures that occur in this mountainous and largely rural area. Notably, at the PHC Aligned Protestants did not contend that Sierra should be required to continue to serve them, but rather that PSREC should be authorized to serve instead.

Without conceding any of the alleged service problems, Joint Applicants have agreed to investigate partnering with PSREC to improve local reliability in the Loyaltan/Portola area. Generally, however, electric power throughout the entire service territory will continue to move into California from Nevada or elsewhere outside California over the same facilities as it does now (the small King's Beach facility provides very limited local generation). The Power Purchase Agreement, Ex. 10 to the transfer application, ensures delivery of CalPeco's full requirements, including 20% from renewable sources eligible for California's Renewable Portfolio Standard (RPS), at rates reflecting Sierra's actual costs and based on Sierra's system-average cost, for an initial term of five years. The Power Purchase Agreement gives CalPeco certain rights to develop and/or procure other renewable sources during the five-year term. It also provides an additional, five-year right to obtain power from Sierra in an amount up to CalPeco's full requirements for nonrenewable sources. Ongoing transmission will be negotiated in accordance with federal law on non-

discriminatory, open access transmission and Sierra's Federal Energy Regulatory Commission (FERC) tariffs.

With respect to reliability in the Loyalton/Portola area, Joint Applicants have reached an agreement with PSREC for CalPeco to contract for additional line crew assistance as needed (we discuss this below in Section 5.3.3, as part of the PSREC Settlement). In South Lake Tahoe, they propose to reopen a customer service counter that now is closed. While generally CalPeco expects to hire the same employees who now operate the system for Sierra, Joint Applicants also have disclosed CalPeco's plans to locate corporate headquarters, senior management and a customer service headquarters in the service territory. They suggest these initiatives should benefit service by increasing local accountability. Further, Joint Applicants describe CalPeco's intention to introduce software capabilities that will give customers electronic options for bill receipt, payment, service initiation, and scheduling service calls. They claim this initiative follows on Algonquin's successful efforts to introduce "innovative, state-of-the-art billing systems and customer communication programs designed to cost-effectively enhance customer service" to other, small, regulated water and sewer utilities it owns and operates in four states.<sup>23</sup> They predict the CalPeco initiative, similarly, will yield both economic and service quality benefits for many customers who live in remote areas and for others who are not domiciled in the service territory year-round. Likewise, Joint Applicants describe CalPeco's preliminary involvement in the Lake Tahoe Green Energy District, which is working to implement, locally, a number of energy efficiency measures and to pursue other

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<sup>23</sup> Transfer Application at 5.

“green” projects. Other participants in this enterprise include the local school district and community college, as well as the City of South Lake Tahoe, the State of California Tahoe Conservancy, and the United States Forest Service.

Joint Applicants also point to the favorable assessment by Local 1245 of the proposed transfer’s service quality impacts:

We [Local 1245] also believe that CalPeco’s local presence, smaller size, resulting sharper focus, and ability to concentrate on matters of particular importance to California and the Lake Tahoe Basin communities will benefit its customers in terms of the quality of the service.<sup>24</sup>

DRA disputes the need for any of the service improvements proposed for Portola/Loyalton and elsewhere. DRA’s primary contention is that these and other changes necessarily will increase costs for CalPeco. DRA predicts that as a standalone utility with 46,000 customers, CalPeco will lack the economies of scale available to Sierra and that therefore, the transfer will lead to a substantial rate increase request in the next general rate case. Service quality cannot be divorced completely from its cost, and we discuss these cost concerns below. However, nothing in the record suggests that service quality will decline under CalPeco. Rather service quality will continue at present levels generally, and in some respects may improve, given Joint Applicants’ stated intentions as well as its responsiveness to registered customer concerns.

### **5.3. Impact on Costs**

Joint Applicants maintain that the transaction has been structured to enable CalPeco, post-closing, to collect from customers the same total revenues

that Sierra is authorized to charge and collect, at the same rate levels now applicable to individual customers.<sup>25</sup> DRA does not dispute this but argues that cost increases are inevitable, that they will lead to rate increases in the future, and that for these reasons the Commission simply should deny the transfer application.

The “Premium and Cost Synergies” section of the Regulatory Commitments contains three promises that shield customers from costs solely attributable to the proposed transfer from Sierra’s ownership: (1) CalPeco will not seek to recover from customers the purchase premium (the excess of the purchase price over recorded, regulatory book values for utility assets); (2) CalPeco will use its actual recorded costs levels, including any cost savings (from installation of electronic systems, etc.), as its basis for rate requests in future general rate cases; and (3) CalPeco will not seek to recover from customers transaction costs (investment banking and legal fees, and perimeter metering costs).

However, DRA warns that if the transfer is approved, CalPeco likely will seek a sizable rate increase when it files its first general rate case in 2012. DRA

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<sup>24</sup> Ex. 1, Attachment G, November 30, 2009 letter from Local 1245 to Commissioner Grueneich.

<sup>25</sup> Joint Applicants ask the Commission to authorize CalPeco to reclassify certain components of general rates to Energy Cost Adjustment Clause (ECAC) rates. This reallocation request arises because CalPeco, which will own no transmission assets and no generation assets other than the King’s Beach facility, will purchase both services under the Power Purchase Agreement. Thus, while total revenues will not change, a greater portion of the total will be attributable to fuel and purchased power. The reallocation will avoid cost-shifting between customers and the aggregate, per kilowatt hour (kWh) charge in each customer’s monthly bill will remain the same. DRA has not opposed this reallocation.

identifies the following as areas of particular concern: Operations and Maintenance (O&M) and certain, other miscellaneous costs; the Transition Services Agreement between CalPeco and Sierra; the settlement with PSREC; and the uncertainty regarding imports of power from Sierra's coal-fired Valmy Power Plant (Valmy). We examine each of these below. Joint Applicants are correct that this transfer application should not be turned into a general rate case. Nonetheless, it is incumbent upon us to assess the record before us for signs of the kinds of serious cost consequences that necessarily must affect any public interest assessment under § 854(a).

DRA's opening brief also argues, for the first time, that CalPeco should agree to forego filing a general rate case until three years beyond 2012. Joint Applicants object to this so-called, three-year, rate case "stay out." Not only do we lack a record on any alleged benefits and detriments of this proposal vis a vis CalPeco, but a general rate case deferral is at odds with our policy preference for regular, orderly review of utility operations. We denied DRA's request for one-year rate deferrals for PacifiCorp in D.07-05-031 and for CalAm in D.02-12-068. We decline to impose a three-year deferral here.

### **5.3.1. O&M and Other Miscellaneous Costs**

DRA contends that CalPeco's smaller size will translate into reduced purchasing power, resulting in increased costs, and ultimately, higher rates. Joint Applicants contend that the evidence does not support DRA's position. They point out that over half (\$45 to \$50 million) of the current \$75 to \$80 million revenue requirement is attributable to power supply, which will continue to be incurred at the same cost under the Power Purchase Agreement. While they dispute DRA's claim that CalPeco's smaller size means the certain loss of any economies of scale that Sierra has enjoyed, they also argue that such purchasing

advantage could only apply to a portion of the O&M and administrative costs that comprise, in the aggregate, about 10% of the total revenue requirement. Over half of these costs can be expected to be quite stable, since CalPeco expects to hire the same employees under similar compensation packages (presently about \$4.6 million) and to purchase and operate the same trucks and other vehicles.

On this point Joint Applicants' witness testified:

[A]s [CalPeco looks] at the 2012 GRC . . . sitting here today there is nothing in evidence from our perspective that would lead us to believe that there would be any cost increase arising from administration or operating costs that wouldn't be present if Sierra continued to own [the California Utility].<sup>26</sup>

Joint Applicants' brief quantifies the theoretical "risk" of the rest of the O&M costs (\$3 to \$4 million) escalating at 15% and argues that the resulting increase (\$450,000 to \$600,000), which would raise the total revenue requirement by less than 1 %, could not reasonably be termed rate shock. Joint Applicants hasten to state that they do not anticipate that CalPeco's recorded costs will cause them to ask for 15% rate increase in O&M, however. Their witness testified:

CalPeco expects no such 15% increase. Nonetheless, CalPeco is comfortable that its costs with respect to the O&M costs would be comparable to the costs that Sierra would incur if it retained ownership.<sup>27</sup>

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<sup>26</sup> Tr. at 59.

<sup>27</sup> Joint Applicants Opening Brief at 40.

While a general rate case will be the place to review the reasonableness of actual costs incurred, this record does not suggest cost consequences of a magnitude large enough for us to find that the proposed transfer will harm ratepayers and therefore, is adverse to the public interest. Our assessment should not be construed to support a reasonableness finding or authorize rate recovery in a future general rate case.

DRA also discounts Joint Applicants' suggestion that cost savings will result from new, electronic capabilities for billing and for scheduling service. DRA relies on testimony that Sierra previously determined electronic billing for the California Utility did not make economic sense. But as Joint Applicants explain, CalPeco would be installing a standalone system based on California rates and tariffs, not adapting an existing system, based on Nevada rates and tariffs, for a small group of customers in California. To be sure, neither party has offered any quantification to support its economic claims. Given Algonquin's apparent past success in this area, we are not persuaded by DRA's assertion that the plan has no merit.

DRA contends that other service enhancements (the reopened customer service counter, etc.) will increase costs without providing value. Again, Joint Applicants state they expect such measures to be cost-effective. Regardless, a general rate case is the place to assess whether undertakings of this nature and relative magnitude are reasonable and warrant recovery in rates.

These issues do not compel a finding that the proposed transaction is adverse to the public interest. Again, this assessment should not be construed to support a reasonableness finding or authorize rate recovery in a future general rate case.

### **5.3.2. Transition Services Agreement**

Under the Transition Service Agreement, Ex. 12 to the transfer application, CalPeco has the option to ask Sierra to perform at cost for 24 months, with a 12-month extension, any of the services Sierra now provides to the California Utility. DRA faults the agreement and Joint Applicants for not specifying, now, precisely which services CalPeco will request. DRA also speculates that once the agreement expires, CalPeco will likely incur higher costs and will seek to collect those higher costs in rates. The Transition Services Agreement appears to be a prudent, interim arrangement to ensure continued good service to ratepayers, rather than a measure that will cause them harm. A general rate case is the place to assess the reasonableness of projections of future costs. These issues do not compel a finding that the proposed transaction is adverse to the public interest.

### **5.3.3. PSREC Settlement**

Joint Applicants' settlement with PSREC is not before us for approval. We discuss the settlement here because of its implications for future costs. While PSREC and the other Aligned Protestants in the Loyalton/Portola area support the settlement, DRA asserts that it "does not offer any benefit to the CalPeco ratepayers at all" and "has generated \$1.4 million in additional incremental costs that would not otherwise exist."<sup>28</sup>

The PSREC Settlement has two primary components. One concerns development of additional transmission capacity in that portion of the service territory and the other, line crew support for the single lineman based there. The Assigned Commissioner's scoping memo directed Joint Applicants to meet in the

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<sup>28</sup> Ex. 50 at 11.

Loyalton/Portola area with PSREC and the other Aligned Protestants to discuss the problems alleged “and assess how reasonable concerns might be addressed.”<sup>29</sup> Again, while Joint Applicants have not conceded that any portion of the California Utility suffers from reliability or service deficiencies, we observe that the executed settlement responds to all of Aligned Protestants’ allegations (lack of sufficient transmission, lack of back-up generation, and assignment of a single lineman to the area). Nonetheless, if in a future general rate case Joint Applicants fail to prove the reasonableness of either part of the settlement, neither part will ever have any effect upon rates.

With respect to transmission, the settlement provides for CalPeco and Sierra shareholders to make a capital investment of \$250,000 in PSREC’s Herlong Transmission Project. In addition, Sierra will work with PSREC to increase transmission capacity through PSREC’s Marble Substation, in order to expand reliability for both by means of additional, backup transmission service. Joint Applicants describe the Herlong Project as follows:

This project is to be structured to connect PSREC’s system directly with Sierra’s system to provide PSREC greater access to less expensive power from sources east of California. PSREC also intends that this project provide CalPeco’s customers greater reliability by the addition of an additional transmission line and also access to additional generation sources north and east of California.<sup>30</sup>

Under the settlement, if CalPeco determines the Herlong Project has sufficient, independent merit to CalPeco’s ratepayers to warrant a further capital

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<sup>29</sup> Scoping Memo and Ruling of Assigned Commissioner, February 25, 2010 at 16.

<sup>30</sup> Ex. 1 at 37.

investment, and if the Commission subsequently agrees and grants CalPeco authority to make that investment on behalf of ratepayers, CalPeco will commit a total of \$1 million to the project. In that case, the settlement provides for the initial \$250,000 shareholder payment to be credited against CalPeco's \$1 million investment. We have no reason to attempt to weigh here whether the Herlong Project will have value for CalPeco. That issue belongs in a future general rate case.<sup>31</sup>

The resource support agreement in the PSREC Settlement provides the terms by which CalPeco will obtain additional line crew services in the Loyalton/Portola area (one lineman and a bucket truck, or the equivalent, for a minimum number of hours annually over a ten-year initial term). CalPeco agrees to absorb 100% of the cost of the resource support agreement between the date of closing and the effective date for rates authorized in a 2012 general rate case.

These issues do not compel a finding that the proposed transaction is adverse to the public interest.

#### **5.3.4. Valmy**

As discussed above in Section 5.2, the Power Purchase Agreement provides for five years' continued delivery of CalPeco's full requirements for electric power at Sierra's system-average cost. Currently, Sierra's power supply mix to its California customers includes electricity generated at Sierra's coal-fired

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<sup>31</sup> Joint Applicants admit that at present there is no transmission path between the Herlong Project and customers in the Loyalton/Portola area and that this "could render the Herlong project to be of potentially limited value" to CalPeco. (Ex. 1 at 39.) For this reason the PSREC Settlement has been structured to commit PSREC to enter into other commercial arrangements that will yield a solution for CalPeco.

Valmy plant, which commenced operations in the early 1980's. The question arises whether CalPeco may contract for five years for a power supply mix that includes Valmy, given California's statutorily-mandated greenhouse gas (GHG) Emissions Performance Standard (EPS). According to DRA, the rate consequences of prohibiting inclusion of Valmy make the proposed transfer uneconomical – the 2012 impact will be an increase in the average residential rate by "9.95% from \$0.12405 per kWh to \$.13639 per kWh," following close upon a sizeable residential rate increase (7.75%) in Sierra's 2009 general rate case.<sup>32</sup> Joint Applicants calculate the rate impact for the more expensive cost supply mix at \$7.6 million starting in 2011.<sup>33</sup>

In accordance with the statutory guidance in Senate Bill (SB) 1368 (Stats. 2006, ch. 598), enacted in September 2006, the Commission opened a rulemaking to develop the EPS and appropriate rules to implement it. D.07-01-039 approves Adopted Interim EPS Rules.<sup>34</sup> Central to the issues before us is this definition in SB 1368:

"Long-term financial commitment" means either a new ownership investment in baseload generation or a new or renewed contract with a term of five years or more years, which includes procurement of baseload generation."<sup>35</sup>

The statute explicitly prohibits the Commission from approving a long-term financial commitment, and any load-serving entity from entering into one,

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<sup>32</sup> Ex. 50 at 14.

<sup>33</sup> Ex. 1 at 43.

<sup>34</sup> *Interim Opinion on Phase 1 Issues: Greenhouse Gas Emissions Performance Standard* (2007), D.07-01-039; the Adopted Interim EPS Rules are found at Attachment 7.

<sup>35</sup> SB 1368, Section 2, codifying Pub. Util. Code § 8340 (subpart (j)).

unless the baseload generation supplied under that long-term financial commitment complies with the EPS.<sup>36</sup> Under current law, Sierra may continue to supply power to its California customers from the non-EPS compliant, coal-fired Valmy, however, because Sierra has owned Valmy for several decades. Joint Applicants' witness testified that Sierra has no plans, at present, to make what D.07-01-039 has defined as new ownership investments in Valmy (major retrofits, etc., that would prolong Valmy's useful life by five years or more). Hence, as long as Sierra makes no prohibited, new ownership investments, there is no long-term financial commitment in the context of SB 1368. Enter the contractual arrangement with CalPeco, however, and the picture changes somewhat -- does the Power Purchase Agreement represent a prohibited new contract? D.07-01-039 looks at other contracting issues (what constitutes baseload, how to prevent gaming in contracts with unspecified sources for system reliability, etc.) but does not examine the issue the transfer application raises. Nor has the Commission had occasion to consider the question to date.

Joint Applicants, who argue Valmy should remain in the supply mix, urge us to "allow the pre-Closing status quo to continue - maintenance of existing power sources and customer costs."<sup>37</sup> They point out that while approving the transfer but excluding Valmy supply from California will affect the costs for California customers (since power from Valmy is produced below Sierra's system average cost), nothing else will change. Sierra will continue to operate

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<sup>36</sup> Joint Applicants report that they initially contemplated a three-year term for the Power Purchase Agreement but that discussion with the Commission's Energy Division caused them to expand the period to five years to increase supply and price stability.

<sup>37</sup> Joint Applicants' Opening Brief at 56.

the highly-depreciated Valmy at the same capacity for the benefit of Nevada customers and any emissions that migrate into California now will continue to do so. On the other hand, rejecting the transfer will obligate Sierra to continue to serve the California Utility, which also ensures the continued operation of Valmy.

Since D.07-01-039 provides no direct guidance, we turn to the policy goals of SB 1368, which D.07-01-039 summarizes as follows:

An EPS is needed to reduce California's financial risk exposure to the compliance costs associated with future GHG emissions (state and federal) and associated future reliability problems in electricity supplies. Put another way, it is needed to ensure that there is no "backsliding" as California transitions to a statewide GHG emissions cap: If LSEs [load serving entities] enter into long-term commitments with high-GHG emitting baseload plants during this transition, California ratepayers will be exposed to the high cost of retrofits (or potentially the need to purchase expensive offsets) under future emission control regulations. They will also be exposed to potential supply disruptions when these high-emitting facilities are taken off line for retrofits, or retired early, in order to comply with future regulations. A facility-based GHG emissions performance standard protects California ratepayers from these backsliding risks and costs during the transition to a load-based GHG emissions cap.<sup>38</sup>

Under the facts applicable here, it is difficult to see how prohibiting inclusion of Valmy power in the Power Purchase Agreement's supply mix for a term of five years would further SB 1368's policy goals. Rather, continued import of Valmy power under the Power Purchase Agreement simply preserves the status quo, operationally and economically. Therefore, we find that inclusion

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<sup>38</sup> D.07-01-039 at 3.

of Valmy power under the Power Purchase Agreement for a five-year term is not a covered procurement, within the context of SB 1368 and D.07-01-039, and thus, is not subject to our EPS rules.<sup>39</sup> Beyond the contract's five-year term, we should continue to view Valmy under the same rules that would apply were Sierra to continue to serve the California Utility. Thus, Valmy power may be included in the supply provided under any additional power purchase agreement which Sierra and CalPeco may enter upon the expiration of the initial five-year Power Purchase Agreement as long as Sierra makes no new ownership investment in Valmy, as defined by D.07-01-039, and any relevant, subsequent modifications. Our determination interprets D.07-01-039 solely with respect to Valmy and does not modify D.07-01-039.

#### **5.4. Impact on the Financial Condition of the California Utility**

In summary, in addition to a public interest finding under § 854(a), Joint Applicants seek authority under § 816, § 818, and § 851 for CalPeco to finance up to 50% of the acquisition price and to encumber utility assets, including accounts receivables, as security for the debt issuance. As stated previously, Algonquin and Emera have committed to fund CalPeco to ensure initial capitalization of at least 50% equity; their respective ownership shares are Algonquin, 50.001%, and Emera, 49.999%. CalPeco will exist as a stand alone financial entity, with its own capital structure, debt, and credit rating.

Joint Applicants represent that they developed the Regulatory Commitments (Appendix 3) to incorporate conditions the Commission has

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<sup>39</sup> D.07-01-039 uses the term "covered procurement" to mean the types of generation and financial commitments subject to the EPS, pursuant to SB 1368.

required in prior § 854(a) applications to safeguard the financial condition of the California jurisdictional utility. The Regulatory Commitments, which confirm a high degree of separateness in CalPeco's structural and financial relationship with its owners and their subsidiaries, include these promises:

- The sole purpose of CalPeco's immediate parent, California Pacific Utility Ventures, LLC, will be to own CalPeco;
- CalPeco's assets will be used solely to provide electric distribution services to its customers and to secure any debt it obtains;
- Any financing by Algonquin and Emera of any business activities other than CalPeco will provide the financing parties no recourse to CalPeco's assets;
- Algonquin and Emera will fund all other business activities independently of CalPeco;
- CalPeco will not provide financing to, guarantees for, extend credit to, or pledge any of its assets on behalf of Algonquin, Emera, or any of their subsidiaries;
- Algonquin and Emera commit to ensure that CalPeco has sufficient capital available for necessary capital investments;
- Dividend distributions by CalPeco may be restricted to maintain minimum, required equity levels;
- CalPeco will retain separate books, financial records, employees and assets and these will be based in California.

Joint Applicants and DRA disagree about whether these commitments provide adequate financial security and we discuss their contentions below.

#### **5.4.1. Capital and Debt Guarantees; Ring-Fencing**

DRA contends that CalPeco's owners must guarantee its needs for capital and debt, that their commitments in this respect are inadequate, and therefore, that the Commission should impose a first priority condition on them as a

condition of any transfer.<sup>40</sup> DRA also contends that the ring-fencing measures proposed are inadequate, describing them as “two-way” measures designed to protect Algonquin and Emera as much as or more than CalPeco.<sup>41</sup> From DRA’s perspective, if the Commission approves this transaction without imposing a first priority condition, it should require Joint Applicants to obtain a non-

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<sup>40</sup> The first priority condition is fundamental to the Commission’s authorization of the formation of the California holding companies that own and control this state’s major energy utilities. See for example, D.88-01-063, 1988 Cal. PUC LEXIS 2 \*78 (Southern California Edison Company); D.95-12-018, 1995 Cal. PUC LEXIS 931 \*72 (San Diego Gas & Electric Company), D.96-11-017, 1996 Cal. PUC LEXIS 1141 \*74; as modified by D.99-04-068, 1999 Cal. PUC LEXIS 242 \*151 (Pacific Gas and Electric Company); D.98-03-073, 1998 Cal. PUC LEXIS 1 \*260, \*290 (Enova [Southern California Gas Company, San Diego Gas & Electric Company merger]). The Commission also imposed a first priority condition on the transfer of control affecting jurisdictional portions of two common carrier pipeline utilities, SFPP, L.P. and Calnev Pipe Line, L.L.C., where the new ownership structure comprised a privately-held, limited liability company and a consortium of investment banks, diversified financial services providers, and private equity funds. See D.07-05-061.

<sup>41</sup> Ex. 50 at 8. The Commission discussed ring-fencing in D.07-05-061, as follows:

Ring-fencing is the legal walling off of certain assets or liabilities within a corporation. Conceptually, in the context of a public utility within a holding company structure, ring-fencing includes a number of measures that may be implemented to protect the economic viability of the utility by insulating it from the potentially riskier activities of unregulated affiliates and thereby, ensuring the utility’s financial stability and the reliability of its service. (See Beach Andrew N., Gunter J. Elert, Brook C. Hutton, and Miles H. Mitchell. Maryland Commission Staff Analysis of Ring-Fencing Measures For Investor-Owner Electric and Gas Utilities. The National Regulatory Research Institute-Volume 3, December 2005 at 7). A non-consolidation opinion is not a ring-fencing measure per se, but focuses on the effect of ring-fencing. A non-consolidation opinion demonstrates that a utility has enough ring-fencing provisions to protect it from being pulled into a holding company bankruptcy. (D.07-05-061, footnote 22.)

consolidation opinion that demonstrates the adequacy of the ring-fencing measures.

Joint Applicants' briefs generally challenge DRA for focusing too much on the potential for harm to CalPeco should exigent financial circumstances arise. While Joint Applicants' are correct that it is impossible to guarantee, with absolute assurance, the financial security of any entity into the unknowable future, we do not agree that DRA is amiss for seriously considering the impact of exigent circumstances. At a minimum, recent financial history urges caution. However, we do not find it unreasonable that Joint Applicants oppose imposition of a first priority condition. Algonquin and Emera own regulated utilities in Canada and in four other states in this country and argue that, legally and practically, they cannot put CalPeco in first place before those other entities. As Joint Applicants observe, the Commission recognized this reality in D.02-12-068, when it approved the change of control of CalAm but declined to impose a first priority condition. Joint Applicants further contend that their situation is similar to PacifiCorp's acquisition by MidAmerican, where the Commission found an acceptable safety net in MidAmerican's promise to "obtain sufficient cash from its operations, regular infusions of equity capital from [MidAmerican's holding company], and steady increases in short-term debt."<sup>42</sup> Joint Applicants point to the Regulatory Commitments for similar promises by Algonquin and Emera.

Regarding equity infusions, Joint Applicants full commitment now states:

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<sup>42</sup> D.06-02-033 at 26.

Emera and Algonquin will provide sufficient initial equity to fund fifty percent (50%) of the purchase price for CalPeco. CalPeco shall seek to obtain the balance of the required capital necessary for the purchase price through stand-alone debt issued by CalPeco. Algonquin and Emera are prepared to make this initial equity investment and invest any additional equity in CalPeco based on their understanding that the Commission shall grant CalPeco timely recovery in rates (i) for the reasonable expenses it will make or undertake, respectively, to provide electric service; and (ii) for CalPeco to earn a reasonable return of and on CalPeco's investment in rate base. On this basis Emera and Algonquin are committed to ensure that CalPeco maintains sufficient funds to operate and has sufficient capital available for necessary capital investments. CalPeco, Algonquin, and Emera acknowledge that dividends or similar distributions by CalPeco may be restricted as necessary to maintain minimum equity levels that are reasonable in relation to any equity ratio requirements.<sup>43</sup>

An earlier version did not commit Algonquin and Emera to provide equity beyond the initial capital infusion; the change was made after hearings, at least in part in response to DRA's criticism. DRA's opening brief argues that the amended commitment remains deficient. DRA faults the amended version because it "put[s] the onus on CalPeco to maintain the necessary funding to operate" and also, as DRA reads the commitment, because it means that rate recovery must be assured before any capital infusions are made.<sup>44</sup> DRA further contends that the commitment effectively defines capital as additional equity, only, and therefore "is too limiting."<sup>45</sup> DRA refers to the Commission's discussion of capital in D.02-01-039, an interim decision in the Commission's

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<sup>43</sup> Appendix B, Regulatory Commitments, Section 1(g).

<sup>44</sup> DRA Opening Brief at 20.

<sup>45</sup> DRA Opening Brief at 21.

2002 investigation into, among other things, the meaning of the first priority condition in the context of the holding company structures for the major California energy utilities. There, the Commission examined the holding companies' policies in the context of the electricity crisis. Findings 5 and 6 of D.02-01-039 provide:

5. The term "capital," where not otherwise limited or qualified, encompasses all of the following: the money and property with which a company carries on its corporate business; a company's assets, regardless of source, utilized for the conduct of the corporate business and for the purpose of deriving gains and profits; and a company's working capital.

6. The term "capital" is not limited in the first priority condition to mean only "equity capital," infrastructure investment, or any other term that does not include, simply, money or working cash.<sup>46</sup>

We conclude that DRA overstates its case on this point. While we agree with DRA that the definition of capital should be understood, plainly, to include money or working cash, the following, very broad clause in Regulatory Commitment 1(g) is reasonably read to encompass working capital as well as capital expenditure: "... Emera and Algonquin are committed to ensure that CalPeco maintains sufficient funds to operate and has sufficient capital available for necessary capital investments."

DRA's other interpretations of Regulatory Commitment 1(g) also fail to persuade. Rather, the language reflects two established, general principles: (1) a regulated utility should be self-supporting where possible, and (2) under the

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<sup>46</sup> *Investigation into Pacific Gas and Electric Company, Southern California Edison Company and San Diego Gas & Electric Company and their respective holding companies, D.02-01-039 (2002)*

decades old regulatory compact, rate recovery can be expected for all reasonable expenditures made in the provision of safe and reliable utility service. We do not think the amended commitment can fairly be read to suggest that Algonquin or Emera plan to abandon CalPeco if an unusual or extreme need for cash should arise. Even before Joint Applicant's revised this commitment to extend it to additional equity infusions, their witness testified:

[I]f there were an extraordinary event – a storm of some profound magnitude that required some kind of capital infusion to protect the asset, then I would assume that CalPeco would either seek to obtain those funds or they'd be forthcoming from the parent to protect the asset.<sup>47</sup>

In addition, DRA argues that CalPeco's small size may increase its cost of debt. As DRA notes, this claim is frequently heard in ratemaking proceedings at the Commission, though it is not accurate in all instances. DRA has not shown, however, how a parental guarantee will benefit ratepayers by ensuring a lower debt rating for CalPeco, particularly when such a guarantee is at odds with standard ring-fencing measures. While the actual cost of debt cannot be known in advance, Joint Applicants' witness testimony further explains their representation that it should be competitive with NV Energy's debt:

Our discussion with the capital markets and lenders in the capital markets have led us on behalf of CalPeco to conclude that the cost of debt that will be sought by CalPeco will be competitive with the cost of debt which is currently outstanding on behalf of NVE.

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<sup>47</sup> Tr. at 85.

It is through looking at the ratios – the debt-to-energy ratios, looking at interest coverage ratios – that leads us to conclude that the rating that CalPeco will enjoy will be competitive, if not perhaps better in some respects, than NV Energy who has obviously a much broader business offering.<sup>48</sup>

A parental debt guarantee also serves to undermine the separateness which ring-fencing establishes. DRA does not discuss this issue. Its ring-fencing concerns focus on what DRA's terms the "two way" rather than "one way" nature of the measures that Joint Applicants propose. According to DRA, while the ring-fencing proposals do protect CalPeco from the bankruptcy of its upstream owners, they unreasonably protect Algonquin and Emera from providing any assistance in the case of CalPeco's financial distress. However, the testimony of DRA's witness suggests that DRA's concern really is that CalPeco's owners provide additional capital if needed – and subject to the definitional clarification discussed above, Joint Applicants have addressed that. Asked what Joint Applicants should do to mitigate problems with their ring-fencing proposal, DRA's witness testified that "... the Commission could order the parent company to infuse money into CalPeco if there's future financial hardship."<sup>49</sup>

With respect to the comparative adequacy of the ring-fencing measures that Joint Applicants' propose, we observe the measures offer value, though they are structured differently than those that MidAmerican developed in the context of the PacifiCorp acquisition. The PacifiCorp ring-fencing includes provision for an independent director at PacifiCorp; before any amendment can be made to

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<sup>48</sup> Tr. at 91-92.

<sup>49</sup> Tr. at 138.

the ring-fencing, the independent director must approve the amendment and there must be rating agency confirmation that the amendment will not result in a credit downgrade.<sup>50</sup> In Regulatory Commitment 1(e), Joint Applicants propose that no ring-fencing changes be made without Commission approval, which provides a high degree of oversight and ratepayer protection. Moreover, we retain regulatory jurisdiction to proactively require revisions to the ring-fencing measures, given appropriate notice and opportunity to be heard. On balance then, we find the ring-fencing measures adequate – at least at this time – and need not require Joint Applicants to undertake the additional expense of obtaining a nonconsolidation opinion.

#### **5.4.2. Emera Minimum Hold Condition; Internal Transfer Approval**

Algonquin commits to own at least 50% of CalPeco for at least ten years. Emera makes no such commitment, though according to Ex. 3, the first of several status update letters letter submitted prior to hearing, upon closing Emera now plans to acquire a 9.9% interest in Algonquin in addition to its indirect interest in

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<sup>50</sup> See D.06-02-033 at 25 and Appendix D: Adopted Conditions, 11.

The National Regulatory Research Institute publication quoted above in footnote 41 discusses a number of ring-fencing measures designed to protect the financial viability of a utility, including: (1) capital structure requirements, (2) dividend restrictions, (3) unregulated investment restrictions, (4) prohibition on utility asset sales, (5) collateralization requirements, (6) working capital restrictions, (7) prohibitions on inter-company loans, (8) maintenance of stand-alone bonds, and (9) independence of board members. (The National Regulatory Research Institute-Volume 3, December 2005 at 5.)

We observe that statute and our regulatory policies effectively impose several of the enumerated measures (for example, utility sales restrictions and capital structure requirements).

CalPeco. However, the Emera Minimum Hold Condition, a condition to the closing contained in the Purchase Agreement specifies that “[n]o Final Regulatory Order shall have imposed an affirmative obligation on Emera to continue to own its interest in [CalPeco] for any specific period of time following the Closing Date.”<sup>51</sup> Joint Applicants represent that Emera’s disinclination to be bound to hold its interest in CalPeco for any specific period should not be construed as “any intent to ‘flip’ or otherwise shortly sell” its interest in CalPeco but “is simply a matter of maintaining corporate flexibility.”<sup>52</sup> In response to DRA’s cross-examination at hearing, Joint Applicants’ witness testified: “I believe we have the ultimate track record of maintaining and holding our investments. I think we are the poster children for the buy-and-hold strategy for the assets that we ... own.”<sup>53</sup> Emera’s position on this issue basically reflects a “different philosophy” than Algonquin’s, he testified, and would wrongly be construed to mean anything else.<sup>54</sup>

DRA links its concern about the Emera Minimum Hold Condition to a second proposal, termed the Internal Transfer Approval. As described in the transfer application, the Internal Transfer Approval would permit “either Algonquin or Emera to transfer to the other all or any portion of its ownership interest in CalPeco, and without the need for an additional approval by this Commission.”<sup>55</sup> In Ex. 3, Joint Applicants clarify that they do not intend that this

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<sup>51</sup> Transfer Application, Ex. 8, Article VIII, 8.2(h).

<sup>52</sup> Transfer Application at 69.

<sup>53</sup> Tr. at 87.

<sup>54</sup> Tr. at 87.

<sup>55</sup> Transfer Application at 70.

authority override Algonquin's commitment to retain its investment in CalPeco for at least ten years. Ex. 3 also indicates that Joint Applicants would not object to the conditioning of the Internal Transfer Approval upon a requirement that any decrease in Emera's interest in CalPeco occur concurrently with a proportional increase of Emera's ownership interest in Algonquin. Joint Applicants' witness explained that the companies want the Internal Transfer Approval "for convenience and investment flexibility."<sup>56</sup> However much they might like to have it, the Internal Transfer Approval is not a deal breaker. Joint Applicants' witness also testified: "[I]f it would increase the Commission's comfort, we would be comfortable with filing, if necessary, for any of those transfers an 854(a) application for your approval."<sup>57</sup>

DRA contends that the Internal Transfer Approval is not only a bad idea that effectively would permit Emera to abandon CalPeco, posing risks for ratepayers, but more critically, that it is contrary to law. DRA observes that (1) § 851 and § 854 require Commission approval before any transfer of assets or change of control, and that lacking such approval, a transaction is void, and (2) that any attempt by this Commission to pre-approve such transactions, even if lawful, cannot bind future Commissions.

We agree with DRA that these two requests are inter-related. We do not agree that we should impose a minimum hold condition upon Emera. We desire stability for regulated utilities, but we also recognize that § 851 and § 854 provide legal means for approval of reasonable requests for changes in ownership and

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<sup>56</sup> Tr. at 33.

<sup>57</sup> Tr. at 34.

control. The record does not establish that the proposed transfer is unreasonable unless we impose a minimum hold condition upon Emera. We are less sanguine about the internal transfer authority sought. Whether or not it is lawful (the briefs do not adequately discuss whether the Commission effectively may pre-approve transactions that otherwise would require the filing and review of § 851 and/or § 854 applications), Joint Applicants have not established the Internal Transfer Approval is free of risk to ratepayers. By filing the transfer application as they did, Joint Applicants clearly reached their own determination that Emera and Algonquin should partner in the way proposed. Should they wish to change the financial arrangement at some time in the future, they must file a new application that explains why the proposed change would not be adverse to the public interest.

#### **5.5. Impact on Quality of Management**

DRA favorably acknowledges Emera's more than 130-year history of owning and operating electric utility facilities, including electric distribution and transmission systems. But because Algonquin's own, direct expertise is with electric generation facilities and small water and sewer systems, DRA registers concern that without Emera's long-term involvement, the transfer will result in weakened management. Joint Applicants have made a sufficient showing that CalPeco will have competent, professional management, including a competent initial board of directors, whose credentials are listed in Ex. 23 to the transfer application.

#### **5.6. Impact on Utility Employees**

As mentioned above in Section 5.2, Local 1245 submitted a letter in support of the transaction shortly after Joint Applicants filed the transfer application. DRA challenges Local 1245's support (though it did not call a union

representative or any other employee at hearing), contending that CalPeco has not proposed to offer affected employees continued employment under precisely the same terms and conditions that Sierra now offers. While the witness testimony is not entirely clear on this point, it suggests that the terms for retirement vesting may change for one or more employees who are not vested at present. Regulatory Commitment 4(c) merely states: “CalPeco will recognize the service and seniority of the former employees of Sierra who accept CalPeco’s offer of employment for all non-pension purposes including vacation, sick pay benefits and for non-pension post retirement benefits such as retiree health benefits.” It appears Local 1245 has not expressed pension concerns and DRA has not discredited Local 1245’s letter of support. We find that Joint Applicants have made a sufficient showing that CalPeco will treat employees fairly.

### **5.7. Impact on California and Local Communities**

Joint Applicants focus on service improvements, local hiring as needed, and an increased local presence under CalPeco, all of which can only yield some benefit to the state and local community. DRA’s contends that the likelihood of future rate increases render any change uneconomical. We will carefully consider the reasonableness of any rate increase requests in a future rate case filing, weighing evidence on actual costs and actual benefits in that forum. The record on these issues in the transfer application does not establish ratepayer harm.

### **5.8. Impact on Commission Jurisdiction**

Joint Applicants represent that Sierra not only undertook to fully apprise potential bidders of California’s jurisdictional requirements but that CalPeco and its owners accept the Commission’s jurisdiction and commit to comply with the

Commission's orders and with state law. Witness testimony and the Regulatory Commitments confirm the latter, generally, and DRA does not contest this aspect of the proposed transfer. We agree that Joint Applicants have made a sufficient showing that the transfer will not undermine or interfere with the Commission's jurisdiction regarding access to books and records of its owners or with respect to regulatory policies such as the RPS and the GHG EPS. However, though the issue is raised in the Assigned Commissioner's scoping memo, the record does not fully address the Commission's ability to call officers and employees of CalPeco's jurisdictionally foreign, upstream owners to testify in California regarding matters pertinent to CalPeco. To avoid the possibility of future confusion, any approval of the proposed transaction must be conditioned upon access to such officers and employees as the Commission, itself, may determine to be necessary, consistent with established principles of due process and fundamental fairness.

### **5.9. Impact on Competition**

Joint Applicants contend, and DRA does not contest, that the proposed transaction will have no adverse impact on energy markets in California. As Joint Applicants note, the proposed transaction is not a merger of two existing utilities, which might raise market power concerns. Joint Applicants also report that Algonquin, as the 50.001% owner of CalPeco, and Sierra will make the filings with the Federal Trade Commission required under the federal law known as Hart-Scott-Rodino. The record on this issue shows no ratepayer harm.

### **5.10. Other Operating Agreements**

We discuss above two of the seven Operating Agreements that are integral to the proposed transfer – the Power Purchase Agreement (Section 5.2), including inclusion of supply from Valmy (Section 5.3.4) and the Transition

Services Agreement (Section 5.3.2). The remaining five, uncontested agreements comprise the following:

- Emergency Backup Service Agreement (Ex. 11 to the transfer application);
- Interconnection Agreement (Ex. 16 to the transfer application);
- System Coordination Agreement (Ex. 15 to the transfer application);
- Borderline Customer Agreement (Ex. 13 to the transfer application); and
- Distribution Capacity Agreement (Ex. 14 to the transfer application).

The Emergency Backup Service Agreement governs CalPeco's proposed provision to Sierra of capacity and energy from the Kings Beach facility for emergency backup service.

The Interconnection Agreement provides how Sierra and CalPeco propose to ensure continued interconnection and coordinated operations between the California Utility's Commission-jurisdictional facilities and Sierra's transmission assets in California, which are subject to jurisdiction by FERC. In particular, if FERC accepts Sierra's request to file the agreement under Section 205 of the Federal Power Act, Joint Applicants ask the Commission to authorize CalPeco to recover any payments it must make to Sierra under the agreement, subject only to ongoing Commission review of the reasonableness of CalPeco's administration of the agreement.

The System Coordination Agreement provides how CalPeco and Sierra propose to coordinate non FERC-jurisdictional, operational matters related to the integrated nature of the California service territory and Sierra's distribution system in Nevada.

The Borderline Customer Agreement provides how CalPeco and Sierra propose to sell wholesale power in order to permit each utility to serve, in the

most cost effective way with existing resources, certain customers located near the California-Nevada border. Under the agreement, each utility will apply to FERC for authority to sell power at the rates set forth in the agreement. Joint Applicants ask the Commission to authorize CalPeco to recover payments to Sierra in rates, subject only to ongoing Commission review of the reasonableness of CalPeco's administration of the agreement. Joint Applicants ask the Commission to authorize CalPeco to account for any revenues it receives from Sierra as an offset against its ECAC purchased power costs.

The Distribution Capacity Agreement governs how CalPeco proposes to make capacity on the California Utility's distribution system available to Sierra so that Sierra can cost-effectively serve certain of its Nevada customers located near the California-Nevada border, recognizing that Sierra currently uses electric distribution facilities within California to receive power from Nevada and then to flow that power back to those customers. Joint Applicants' analysis (see Appendix 4 to today's decision) describes why these distribution facilities of the California Utility are "local distribution" facilities subject to the exclusive jurisdiction of the Commission under FERC's seven-factor test. Joint Applicants ask the Commission to retain jurisdiction over the facilities after the closing and authorize CalPeco to provide distribution to Sierra based on the rates and terms in the agreement.

Each of these Operating Agreements has been drafted to permit CalPeco and Sierra to continue to provide electric power, post-closing, to their respective customers in the same way and at the same price as occurs at present.

### **5.11. Conclusion**

Subject to the conditions specifically identified above and in the related Ordering Paragraphs, the transfer application is not adverse to the public interest

and should be approved. Joint Applicants' have established that the transfer will not harm ratepayers; in fact, certain service improvements are likely in the near term, at no cost to ratepayers. To the extent service improvements trigger higher costs that result in a request for an increase in rates in 2012 and beyond, CalPeco is on notice that we will carefully scrutinize its 2012 general rate case showing. As is standard in a general rate case, CalPeco will have the burden of proof to establish the reasonableness of its request.

## **6. Ancillary Agreements to the TDPUD Settlement: Discussion**

As mentioned in Section 3, Joint Applicants' settlement with TDPUD requires Commission approval of the two ancillary agreements filed as exhibits to A.10-04-032, the Fringe Agreement (Ex. A to that application) and the Reliability Support Agreement (Ex. B). TDPUD initially filed a protest to the transfer application, claiming that it would be harmed by the proposed transfer unless steps were taken to avoid that harm. Joint Applicants and TDPUD reached a settlement that resolved TDPUD's concerns and the two ancillary agreements implement that settlement. DRA does not specifically contest either agreement.

### **6.1. Fringe Agreement**

The Fringe Agreement memorializes certain informal, cooperative arrangements between TDPUD and Sierra that have permitted them to serve customers located on or near the border of their contiguous service territories without building uneconomic and duplicative electric distribution facilities. The cooperation has been and continues to be necessary given the terrain and the location of the service territory boundary, which bisects certain roads and residential neighborhoods. The Fringe Agreement obligates Sierra to assign its

rights and responsibilities to CalPeco upon the closing of the proposed transaction. The agreement also memorializes Sierra's, and subsequently CalPeco's, right to rate recovery from those fringe customers served by the California-jurisdictional utility. Since these costs are included within Sierra's revenue requirement calculations at present, the Fringe Agreement will not change revenue requirement.

## **6.2. Reliability Support Agreement**

The Reliability Support Agreement obligates CalPeco, upon closing, to continue to participate in the arrangement that Sierra and TDPUD have negotiated to provide their customers with an alternative path for delivery of electric power, should backup be needed because of an outage on either utility's primary delivery paths. A.10-04-032 describes, in detail, the physical configuration and specific facilities involved. The agreement provides that neither entity will charge for use of any of its distribution facilities for backup delivery. Joint Applicants explain: "It is anticipated that the circumstances in which the use of either of these backup facilities under the [Reliability Support Agreement] will be provided will be rare and largely the result of unpredictable line outages."<sup>58</sup> As with the Distribution Capacity Agreement discussed in Section 5.10, approval of the Reliability Support Agreement relies upon a Commission determination that local distribution facilities are involved (see Appendix 4 to today's decision).

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<sup>58</sup> A.10-04-032 at 8.

### **6.3. Conclusion**

Each agreement essentially memorializes the status quo and permits CalPeco to stand in the shoes of Sierra vis a vis TDPUD, to the mutual benefit of both CalPeco and TDPUD. Joint Applicants have established good reason for the authority sought by A.10-04-032. Accordingly, that application should be approved, as more particularly set out in the Ordering Paragraphs of today's decision.

### **7. Compliance with the California Environmental Quality Act (CEQA)**

The sole remaining issue is whether, as Joint Applicants assert, the proposed transfer qualifies for an exemption from CEQA. Under CEQA and Rule 2.4 of the Commission's Rules of Practice and Procedure, we are required to consider the environmental consequences of projects that are subject to our discretionary approval.<sup>59</sup>

We acknowledge that in some cases it is possible that a change of ownership and/or control may alter an approved project, result in new projects, or change facility operations in ways that have an environmental impact. However, as the transfer application states, the proposed change of control will not result in a change in operation or change in the use of existing assets and facilities. Nor do Joint Applicants seek approval of new construction or request approval for any future utility infrastructure. In accordance with today's decision and except as otherwise authorized herein, CalPeco will continue to operate the California Utility in the manner the Commission has approved for Sierra.

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<sup>59</sup> See, Public Resources Code § 21080.

## **8. Comments on Proposed Decision**

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Joint Applicants and DRA filed comments on October 4, 2010 and Joint Applicants filed reply comments on October 11, 2010.

Joint Applicants agree to comply with each of the three conditions on the transfer that the proposed decision recommends. Joint Applicants also suggest several minor modifications to the decision text, findings, conclusions, and ordering paragraphs to provide further clarity, or in a few instances, to make corrections. The suggestions are well taken and we revise the proposed decision accordingly.

DRA opposes the proposed decision and reiterates the major arguments in its briefs. DRA's contentions do not establish factual or legal error, however. DRA proposes that the Commission impose one, additional condition on the transfer by requiring that Sierra take back the California Utility if CalPeco is unable to fulfill the other conditions. This proposal goes beyond the scope of comments recognized by Rule 14.3(c). Since we have no record upon which to evaluate the proposal, we accord it no weight.

We make other, minor revisions to the proposed decision to correct typographical errors. To cure an inadvertent omission and support the relevant ordering paragraph, we include a brief discussion of the reason the transfer does not require review under CEQA, together with an associated finding and conclusion.

## **9. Assignment of Proceeding**

Dian M. Grueneich is the assigned Commissioner and Jean Vieth is the assigned ALJ in this proceeding.

### **Findings of Fact**

1. The proposed transfer from Sierra to CalPeco has been structured as a sale of all California-jurisdictional assets, rather than a merger or sale of stock, because the California Utility is not organized, legally, as a separate entity from Sierra. Sierra's California Utility consists of its California-jurisdictional service territory and all distribution assets, as well as the King's Beach Generating Station, a 12-MW diesel-fired generator located in King's Beach near Lake Tahoe.

2. Sierra wishes to sell the California Utility to enable its owner, NV Energy, to focus on Nevada operations, which now serve nearly 1.2 million customers located throughout most of that state, given recent load growth. The California Utility's operations represent less than 4% of NV Energy's customer base. The sale would permit NV Energy to consolidate all of its operations under a single, state regulatory agency and respond to a single set of regulatory directives

3. CalPeco is a newly created, California limited liability company. Appendix 2 reflects the organizational ownership chain. CalPeco's ultimate, indirect owners are two publicly traded Canadian companies, Algonquin, which will hold 50.001% stake in CalPeco, and Emera, which will hold 49.999%.

4. The proposed transfer fits the mutual business objectives of CalPeco's owners, Algonquin and Emera, to expand ownership and operation of regulated utility assets, with a view to long-term acquisition and, in some instances, the potential for investment in renewable energy.

5. As qualified in Finding 33, CalPeco's owners do not contest the Commission's jurisdiction. Because Joint Applicants have fully disclosed the

existence of California Pacific Utility Ventures, LLC, as well as Emera and Algonquin and their immediate subsidiaries in the chain of control of CalPeco, have presented witnesses from Algonquin and Emera at hearing, have offered Regulatory Commitments that include promises by Algonquin and Emera, and have placed issues concerning these entities directly before the Commission for decision, our ability to fully consider this transfer has not been circumscribed.

6. Sierra's 2008 annual California revenues were approximately \$72 million and CalPeco had no California revenues.

7. The record contains no evidence that the transfer will result in operational change and no new facilities are proposed.

8. Appendix 3 lists all Regulatory Commitments by CalPeco and its owners; subject to clarification of Regulatory Commitment 1(g) as described in Finding 25, the Regulatory Commitments are reasonable, will not result in harm to ratepayers, and may yield some ratepayer benefits.

9. The sales price which is estimated to range between approximately \$132 and \$137 million, will be calculated more precisely based upon various factors including outstanding accounts payables and accounts receivables at closing; however, the Regulatory Commitments prohibit CalPeco from seeking to recover in rates either the premium paid for the assets of the California Utility or any transactions costs.

10. The proposed transfer will continue safe and reliable service and generally, will maintain the quality of service customers experience today. Service for customers in the remote Loyalton/Portola area should improve given CalPeco's promises to undertake the reliability measures discussed in the body of this decision. Some customers may experience other service improvements, also discussed in the body of this decision.

11. Post-closing CalPeco will collect from customers the same total revenues that Sierra is authorized to charge and collect, at the same rate levels now applicable to individual customers.

12. O&M and administrative costs, which arguably might benefit the most from any economies of scale, comprise in the aggregate about 10% of the California Utility's total revenue requirement. Over half of these costs should be quite stable (given similar compensation packages for the same work force and continued use of the same trucks and other vehicles), which leaves only about \$3 to \$4 million potentially subject to cost escalation in a 2012 general rate case. For the purposes of illustration, only, a 15% escalation of that \$3 to \$4 million would result in a revenue requirement increase of \$450,000 to \$600,000, which is less than 1% of total revenue requirement.

13. CalPeco expects to be able to economically install electronic capabilities for billing and for scheduling service, based upon Algonquin's past success in this area.

14. CalPeco expects the reopening of the customer service counter in South Lake Tahoe to be cost-effective.

15. Under the Transition Service Agreement, which is one of the Operating Agreements, CalPeco has the reasonable option to ask Sierra to perform at cost for 24 months, with a 12-month extension, any of the services Sierra now provides to the California Utility.

16. The settlement with PSREC is not before the Commission in this docket and will have no impact on the rates of California customers, if at all, unless and until CalPeco seeks recovery for any expenditures associated with the PSREC settlement in the CalPeco 2012 general rate case and the Commission authorizes the recovery.

17. Sierra's coal-fired Valmy Power Plant commenced operations in the early 1980's and Sierra has no plans, at present, to make new ownership investments in Valmy.

18. Given the facts, prohibiting inclusion of Valmy power in the Power Purchase Agreement's supply mix for a term of five years will not further SB 1368's policy goals. The exclusion will affect costs for California customers (since power from Valmy is produced below Sierra's system average cost) but nothing else will change, as Sierra will continue to operate the highly-depreciated Valmy at the same capacity for the benefit of Nevada customers and any emissions that migrate into California now will continue to do so.

19. The rate consequences of prohibiting inclusion of Valmy power in the Power Purchase Agreement's supply mix will increase power costs by \$7.6 million starting in 2011, or put another way, increase the average residential rate in 2012 by 9.95% from \$0.12405 per kWh to \$.13639 per kWh.

20. Rejecting the transfer will obligate Sierra to continue to serve the California Utility, which also ensures the continued operation of Valmy.

21. Continued import of Valmy power under the Power Purchase Agreement simply preserves the status quo, operationally and economically, and therefore is not a covered procurement, within the context of SB 1368 and D.07-01-039 and is not subject to the Commission's EPS rules.

22. Beyond the Power Purchase Agreement's five-year term, Valmy should be viewed under the same rules that would apply were Sierra to continue to serve the California Utility. Thus, as long as Sierra makes no new ownership investment in Valmy, power from that plant may be included in the supply mix provided under any additional power purchase agreement, which Sierra and

CalPeco may enter upon the expiration of the initial, five-year Power Purchase Agreement.

23. While the cost consequences of the transfer in 2012 and beyond are uncertain, the evidence does not suggest cost consequences of a magnitude large enough to support a finding that proposed transfer will harm ratepayers and therefore, is adverse to the public interest.

24. Algonquin and Emera own regulated utilities in Canada and in four other states in the United States.

25. CalPeco's amended Regulatory Commitment 1(g), which promises infusions of necessary equity from CalPeco's indirect owners, is reasonably read to encompass working capital as well as capital expenditure.

26. A parental guarantee of debt serves to undermine the separateness which ring-fencing establishes.

27. The ring-fencing measures that Joint Applicants' propose offer value as discussed in the body of this decision.

28. The record does not establish that unless we impose a minimum hold condition upon Emera, the proposed transfer is unreasonable.

29. Joint Applicants have not established their Internal Transfer Authority is free of risk for ratepayers.

30. Joint Applicants have made a sufficient showing that CalPeco will have competent, professional management, including a competent initial board of directors.

31. Local 1245 supports the transfer and in other respects, Joint Applicants have made a sufficient showing that CalPeco will treat employees fairly.

32. Service improvements (even if minor), local hiring as needed, and an increased local presence for the utility can only yield some benefit to the state and local community; the record does not establish ratepayer harm.

33. With one exception, the record generally confirms that CalPeco and its owners accept the Commission's jurisdiction and commit to comply with the Commission's orders and with state law. To avoid the possibility of future confusion, any approval of the proposed transaction must be conditioned upon access to such officers and employees of CalPeco's jurisdictionally foreign, upstream owners as the Commission, itself, may determine to be necessary, consistent with established principles of due process and fundamental fairness.

34. The transfer application incorporates seven Operating Agreements, which comprise, in addition to the Power Purchase Agreement and Transition Services Agreement, these five: Emergency Backup Service Agreement, Interconnection Agreement, System Coordination Agreement, Borderline Customer Agreement, and Distribution Capacity Agreement. Each of these agreements has been drafted to permit CalPeco and Sierra to continue to provide electric power, post-closing, to their respective customers in the same way and at the same price as occurs at present.

35. Joint Applicants' settlement with TDPUD requires Commission approval of the two ancillary agreements filed as exhibits to A.10-04-032, the Fringe Agreement and the Reliability Support Agreement.

36. The Fringe Agreement memorializes certain informal, cooperative arrangements between TDPUD and Sierra that have permitted them to serve customers located on or near the border of their contiguous service territories without building uneconomic and duplicative electric distribution facilities. The

agreement obligates Sierra to assign its rights and responsibilities to CalPeco upon closing and will not change revenue requirement.

37. The Reliability Support Agreement obligates CalPeco, upon closing, to continue to participate in the arrangement that Sierra and TDPUD have negotiated to provide their customers, at no additional charge, with an alternative path for delivery of electric power, should backup be needed because of an outage on either utility's primary delivery paths.

38. The Fringe Agreement and the Reliability Support Agreement essentially memorialize the status quo and permit CalPeco to stand in the shoes of Sierra vis a vis TDPUD, to the mutual benefit of both CalPeco and TDPUD. Joint Applicants have established good reason for the authority sought by A.10-04-032.

39. With respect to the Distribution Capacity Agreement (in A.09-10-028) and the Reliability Support Agreement (in A.10-04-032), the Commission should determine that local distribution facilities are involved and assert jurisdiction over them.

40. The proposed transfer of control will have no significant effect upon the environment, because after the transfer CalPeco will continue to operate the California Utility in the manner the Commission has approved for Sierra, except as modified by today's decision.

### **Conclusions of Law**

1. The proposed transfer from Sierra to CalPeco should be reviewed under § 854, which generally governs mergers and similar transfers of control, rather than § 851, which typically governs sales of assets. More particularly, the transfer should be reviewed under § 854(a).

2. Neither D.01-09-057 nor D.06-02-033 established a positive benefits test for transactions such as the proposed Sierra/CalPeco transfer.

3. The following principles apply to a transfer proposed under § 854(a):

- (a) to ensure that a transfer is not adverse to the public interest, the Commission must be able to evaluate evidence on the important impacts of that transfer – whatever they might be – and find no harm to ratepayers;
- (b) some of the criteria enumerated in §§ 854(b) and (c) mirror criteria identified by past Commission decisions as relevant to a public interest assessment under § 854(a), and depending upon the nature of the transfer at issue, may well be relevant and even necessary to the specific public interest assessment required; and
- (c) only where §§ 854(b) and (c) expressly apply, must the Commission make all of the findings those subsections require.

4. No party has introduced facts to describe any alternative for the Commission to consider under § 854(d).

5. The requested financing authority is governed by is § 816 and § 818, which concern issuance of stocks, bonds, etc., and § 851, which as relevant here, concerns the encumbrance of utility assets.

6. Pursuant to § 15061(b)(3) of the CEQA guidelines, inasmuch as it can be seen with certainty that the project will have no significant impact upon the environment, the transfer application qualifies for an exemption from CEQA and the Commission need not perform any further environmental review.

7. The reach of today's decision necessarily extends to the direct and indirect owners of CalPeco; specifically, any approval of the proposed transaction must be conditioned upon access to such officers and employees of CalPeco's jurisdictionally foreign, upstream owners as the Commission, itself, may determine to be necessary, consistent with established principles of due process and fundamental fairness.

8. A general rate case is the forum for review of the reasonableness of actual costs incurred and actual benefits associated with those costs.

9. No finding or conclusions of law in this decision supports a reasonableness finding or authorizes rate recovery in a future general rate case.

10. D.07-01-039 provides no direct guidance regarding whether the supply mix under the Power Purchase Agreement may or may not include electric power from Valmy.

11. The Commission has not imposed a first priority condition on the owners of a California-jurisdictional utility that also own utilities in other regulatory jurisdictions.

12. The Commission retains regulatory jurisdiction to proactively require revisions to the ring-fencing measures included in the Regulatory Commitments, given appropriate notice and opportunity to be heard.

13. Section 851 and § 854 provide legal means for approval of reasonable requests for changes in ownership and control of public utilities regulated by this Commission.

14. Should any of CalPeco's direct or indirect owners wish to change arrangements governing their ownership and control of CalPeco, they must file a new application under § 854 that explains why the change proposed would not be adverse to the public interest.

15. Subject to the condition on the Power Purchase Agreement's inclusion of power from Valmy, CalPeco should be authorized to enter into the Power Purchase Agreement, the Interconnection Agreement and the Borderline Customer Agreement under the terms and conditions therein, which we deem to be reasonable. Accordingly, the costs incurred under each agreement will be deemed to be prudently incurred and CalPeco is authorized to recover those

costs, subject to review for reasonableness of CalPeco's administration of each agreement.

16. The Distribution Capacity Agreement (in A.09-10-028) and the Reliability Support Agreement (in A.10-04-032) involve local distribution facilities subject to the jurisdiction of this Commission.

17. The proposed transfer qualifies for an exemption from CEQA pursuant to the CEQA guidelines § 1506(b)(3) and so additional environmental review is not required.

18. This decision should be effective immediately to minimize business uncertainty for the parties and all affected by the transfer of Sierra's California Utility to CalPeco.

## **O R D E R**

### **IT IS ORDERED** that:

1. As conditioned by this Ordering Paragraph, the transfer from Sierra Pacific Power Company (Sierra) to California Pacific Electric Company, LLC (CalPeco) is not adverse to the public interest. Accordingly, subject to the Regulatory Commitments attached to this Order as Appendix 3 and subject to the following conditions, Application 09-10-028 is granted, the seven Operating Agreements are approved, and Sierra may transfer to CalPeco, Sierra's California-jurisdictional electric distribution facilities and the Kings Beach Generating Station, together with those Certificates of Public Convenience and Necessity held by Sierra that are required for CalPeco to serve California customers:

- (a) Power from Sierra's Valmy Power Plant (Valmy) may be included in the supply provided under the five-year term of the Power Purchase Agreement (one of the Operating Agreements) and any extension of that term as long as Sierra makes no new ownership investment in Valmy,

within the context of the Emissions Performance Standard rules adopted by Decision 07-01-039, and any subsequent modifications of that decision.

- (b) The Internal Transfer Authority is not approved and any change of ownership affecting CalPeco's upstream owners must be sought by application filed pursuant to Public Utilities Code Section 854.
- (c) Liberty Electric Co., Algonquin Power & Utilities Corp., Emera US Holdings, Inc., and Emera Incorporated must each notify the Director of the Commission's Energy Division in writing within 30 days of the effective date of this decision of its agreement to provide its officers and employees to testify in California regarding matters pertinent to CalPeco, as the Commission, itself, may determine to be necessary, consistent with established principles of due process and fundamental fairness.

2. The California Public Utilities Commission affirmatively asserts jurisdiction over the Distribution Capacity Agreement (one of the Operating Agreements) and the local distribution facilities described therein.

3. The financing authority requested by California Pacific Electric Company, LLC pursuant to Public Utilities Code Sections 816, 818, and 851 is granted.

4. The ratemaking adjustments requested by California Pacific Electric Company, LLC to recognize the provision of power under the Purchase Power Agreement and accordingly, reallocate certain components of general rates to Energy Cost Adjustment Clause rates without increasing total revenues, are approved.

5. Application 09-10-028 qualifies for an exemption from the California Environmental Quality Act and the Commission need not perform any further environmental review.

6. California Pacific Electric Company, LLC (CalPeco) shall file tariffs consistent with this Order no less than 15 days prior to the anticipated closing of the transfer from Sierra Pacific Power Company to CalPeco. The tariffs shall be effective upon the closing, subject to confirmation of compliance by the Director of the Commission's Energy Division or her designee.

7. Effective upon the closing of the transfer, the responsibilities of Sierra Pacific Power Company as a public utility in California shall terminate.

8. Sierra Pacific Power Company (Sierra) and California Pacific Electric Company, LLC (CalPeco) shall notify the Director of the Commission's Energy Division in writing of the transfer from Sierra to CalPeco within 30 days of the date of the transfer. A true copy of the instruments of transfer shall be attached to the notification.

9. The authority for the transfer from Sierra Pacific Power Company to California Pacific Electric Company, LLC shall expire if not exercised within one year from the effective date of this Order.

10. Application 10-04-032 is granted and Sierra Pacific Power Company (Sierra) may enter into the Fringe Agreement and the Reliability Support Agreement as requested in that application. During the period prior to the closing of the transfer from Sierra to California Pacific Electric Company, LLC (CalPeco), Sierra is authorized to account for the expenses it incurs and the revenues it receives to serve customers under the Fringe Agreement, pursuant to the terms therein. Upon closing, CalPeco is authorized to accept assignment of the Fringe Agreement from Sierra and to account for the expenses it incurs and the revenues it receives to serve customers under the Fringe Agreement, pursuant to the terms therein. CalPeco also may enter into the Reliability Support Agreement. The California Public Utilities Commission affirmatively

asserts jurisdiction over the Reliability Support Agreement and the local distribution facilities described therein.

11. Application (A.) 09-10-028 and A.10-04-032 are closed.

This order is effective today.

Dated October 14, 2010, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
DIAN M. GRUENEICH  
JOHN A. BOHN  
TIMOTHY ALAN SIMON  
NANCY E. RYAN  
Commissioners

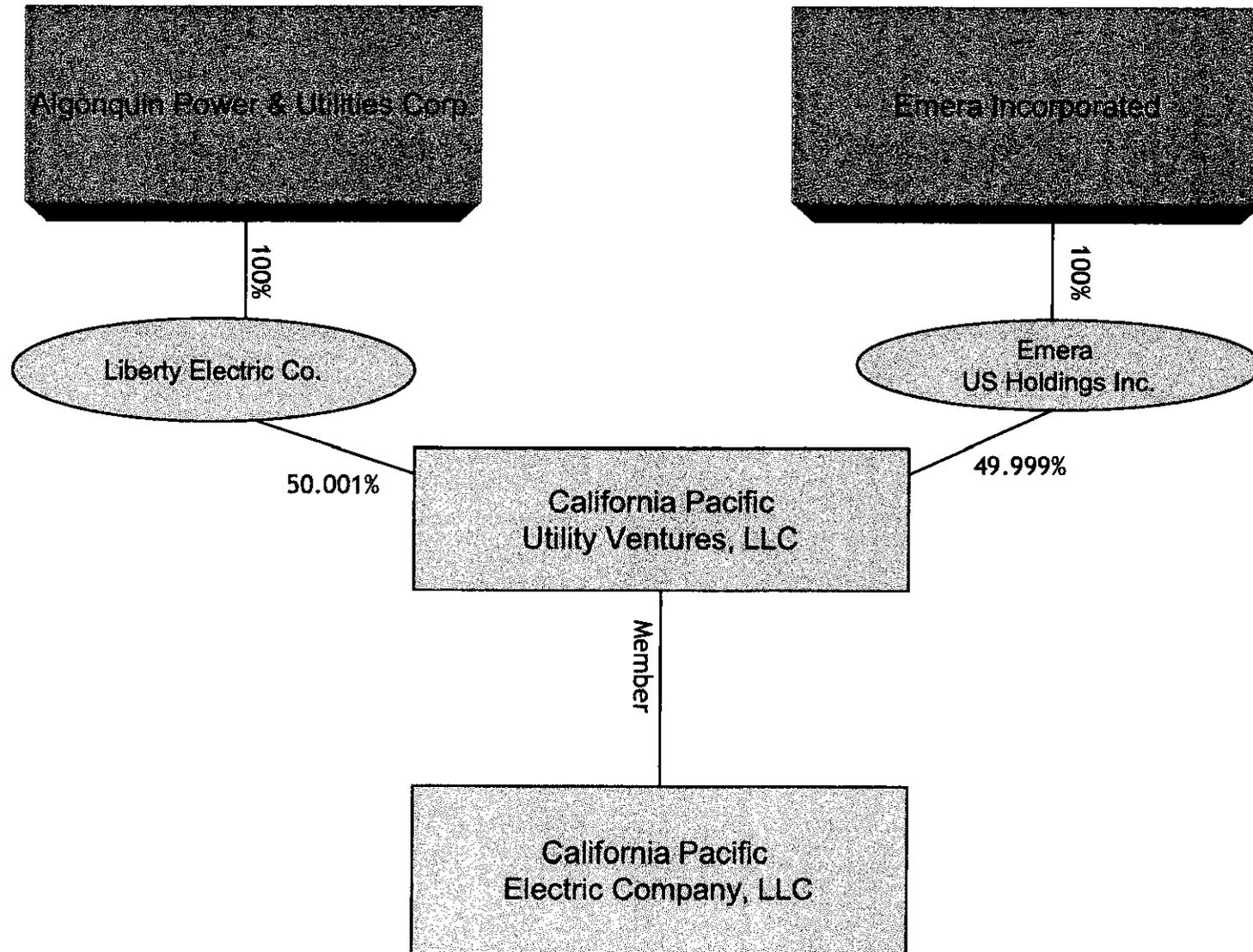
## APPENDIX 1

### LIST OF ABBREVIATIONS AND ACRONYMS

A.	Application
Algonquin	Algonquin Power Income Fund
CalAm	California American Water Company
CalPeco	California Pacific Electric Company, LLC
CEQA	California Environmental Quality Act
D.	Decision
DRA	Division of Ratepayer Advocates
ECAC	Energy Cost Adjustment Clause
Emera	Emera Incorporated
EPS	Emissions Performance Standard
Ex.	Exhibit
FERC	Federal Energy Regulatory Commission
GHG	greenhouse gas
kWh	kilowatt hour
King's Beach facility	King's Beach Generating Station
Local 1245	International Brotherhood of Electrical Workers Local Union 1245
MidAmerican MW	MidAmerican Energy Holdings Company megawatt
NV Energy	NV Energy Inc.
O&M	Operations and Maintenance
PSREC	Plumas-Sierra Rural Electric Cooperative
RPS	Renewable Portfolio Standard
Sierra	Sierra Pacific Power Company
TDPUD	Truckee-Donner Public Utilities District
Valmy	Valmy Power Plant

**(END OF APPENDIX 1)**

## CalPeco Ownership Structure



## APPENDIX 3

### Regulatory Commitments

#### 1. Separateness.

- (a) The California Utility<sup>1</sup> shall be held in a separate legal subsidiary (CalPeco) with no other operations. The only other California business activity currently undertaken by Algonquin Power & Utilities Corp. (“Algonquin”) and/or by Emera Incorporated (“Emera”) and/or their respective affiliates is a non-utility cogeneration power plant in the Fresno area (“Sanger Cogeneration”), which is owned and operated by Algonquin. Sanger Cogeneration sells power only at wholesale. It owns no electric distribution or transmission lines and it serves no retail electric customers. Sanger Cogeneration shall have no ownership or other interest in CalPeco. There shall be no overlapping of employees or responsibilities between the operations of Sanger Cogeneration and CalPeco.
- (b) Although each of Algonquin and Emera is an experienced owner/operator of regulated utilities and actively involved in developing and operating electric generating assets, including renewable generation sources, neither Algonquin nor Emera owns utility assets in the State of California subject to public utility regulation. In the event that either Algonquin or Emera were to acquire any other regulated utility in addition to CalPeco:
  1. The assets of such other public utility would be held in a legal entity separate from CalPeco;
  2. Algonquin or Emera, as the case may be, would segregate the capitalization, financing, and working cash for such other utility and CalPeco in totally separate money pools;
  3. There would be no cross ownership or other interests between such other utility and CalPeco; and
  4. The operations of such other utility and CalPeco would be totally discrete.
- (c) CalPeco will not provide financing or guarantees for, extend credit to, or pledge utility assets in support of either Algonquin or Emera or any of their respective affiliates. Algonquin and Emera each shall finance and fund their respective other business activities independently of CalPeco. The assets of CalPeco shall be used solely and exclusively for the purpose of providing electric distribution services to its customers and securing any debt financing obtained by CalPeco.

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<sup>1</sup> Capitalized terms used in the Regulatory Commitments and not otherwise defined in the Regulatory Commitments have the meanings ascribed to such terms in the Joint Application.

- (d) To the extent that Algonquin or Emera shall finance its non-utility or any business activities other than CalPeco's provision of public utility service, any such financing shall provide the financing parties no recourse to CalPeco's assets.
- (e) CalPeco shall not alter the "ring fencing" provisions set forth in sections 1(a)-1(d) above without first requesting and obtaining approval from the Commission to make any such change.
- (f) CalPeco shall not transfer any physical assets used to provide services to its customers to either Algonquin or Emera or any of their respective affiliates without first obtaining the necessary approvals from the Commission and shall in no event request approval to transfer any physical assets if such transfer would impair CalPeco's ability to fulfill its public utility obligations to serve, or to operate in a prudent and efficient manner.
- (g) Emera and Algonquin will provide sufficient initial equity to fund fifty percent (50%) of the purchase price for CalPeco. CalPeco shall seek to obtain the balance of the required capital necessary for the purchase price through stand-alone debt issued by CalPeco. Algonquin and Emera are prepared to make this initial equity investment and invest any additional equity in CalPeco based on their understanding that the Commission shall grant CalPeco timely recovery in rates (i) for the reasonable expenses it will make or undertake, respectively, to provide electric service; and (ii) for CalPeco to earn a reasonable return of and on CalPeco's investment in rate base. On this basis Emera and Algonquin are committed to ensure that CalPeco maintains sufficient funds to operate and has sufficient capital available for necessary capital investments. CalPeco, Algonquin and Emera acknowledge that dividends or similar distributions by CalPeco may be restricted as necessary to maintain minimum equity levels that are reasonable in relation to any equity ratio requirements.
- (h) CalPeco shall hold all of its assets in its own name, and will maintain adequate capital and number of employees in light of its business purposes. CalPeco shall maintain the current level of employees for a period of at least three (3) years.

## **2. Books and Records.**

- (a) CalPeco shall maintain separate books and records, systems of accounts, financial statements and bank accounts and shall in all events maintain its books and records in full compliance with Commission, and to the extent applicable, FERC, rules and regulations. All financial books and records of CalPeco will be kept in the California operations office, and, together with any records of any Emera and/or Algonquin affiliate that are relevant to CalPeco (wherever held), will be made available for review by the Commission upon request. Algonquin and Emera will make available to the Commission upon request its books and records and the books and records of any of their respective affiliates that allocate overhead or have operational or financial dealings with CalPeco, including any Algonquin or Emera affiliate that is a recipient of any funds (including dividends

or similar distributions) from CalPeco. Algonquin, Emera and CalPeco have reviewed the Commission's regulations and decisions on affiliate transactions and commit to comply fully with such rules and regulations.

- (b) Neither Algonquin nor Emera nor any of their respective affiliates conducts any other business within the geographic proximity of the California Utility. Accordingly, Algonquin and Emera (and their respective affiliates) do not anticipate that CalPeco and either Algonquin and/or Emera (and/or their respective affiliates) will be providing any operations-related services to one another. It is, however, contemplated that Algonquin or Emera (or their respective affiliates) may provide management, administrative, and regulatory services to CalPeco with respect to the California Utility. In the event that Algonquin and/or Emera (and/or or their respective affiliates) provide services to CalPeco or CalPeco provides services to Algonquin and/or Emera (and/or their respective affiliates), CalPeco will develop and file with the Commission such shared services agreements and such agreements will comply with applicable affiliate rules and regulations of the Commission.

### **3. Operating Commitments.**

- (a) Credit extended by Algonquin or Emera, jointly or individually, to CalPeco will be at rates and upon terms no less advantageous than those otherwise available to CalPeco from unaffiliated third parties for similar transactions.
- (b) CalPeco will conduct business in the same or similar manner as it has under Sierra's ownership concerning functions such as power delivery, contracting and management, system operation and maintenance activities, safety and service reliability, customer service functions, and billing operations. With respect to regulatory relations, CalPeco will maintain a manager level representative (having such authority as may be required by the Commission) physically present in an office located within the California Utility's service territory with primary responsibility for maintaining Sierra's positive relationships with, and responding to requests for information from, the Commission and other regulatory agencies. CalPeco will also engage competent and respected area consultants such as the Davis Wright Tremaine law firm to provide CalPeco with San Francisco-based support and presence with respect to the maintenance of such positive relationship.
- (c) For an initial period extending through the filing of the next general rate case for the California Utility, CalPeco will maintain and accept all tariffs of the California Utility existing at the Closing or approved by the Commission in response to filings made by Sierra prior to the Closing and as requested to be modified in this proceeding with respect to (i) the reallocation of certain amounts of revenue recovery from general rate to ECAC rate recovery and (ii) the ECAC tariff as explained and requested at pages 30-37 of the Joint Application (but shall not be required to accept a reduction or roll-back in such rates pursuant to the

Required Regulatory Approvals).<sup>2</sup> In this § 854(a) proceeding, CalPeco is requesting no increase in rates or in the total revenue requirement; on the day after Closing, rates for the customers of the California Utility shall remain at the same rate levels as the day prior to Closing and the total revenue requirement shall remain the same.

- (d) CalPeco shall provide service to its customers in compliance with all rules, regulations and decisions issued by the Commission. Among other matters, CalPeco will not change any rate or any other terms and conditions of service for its customers without first having obtained the necessary Commission approvals and CalPeco shall comply with all existing statutes and Commission regulations regarding affiliated interest transactions.
- (e) CalPeco agrees to maintain the existing low-income programs as part of the pending request under § 854(a) to acquire the California Utility. CalPeco shall operate within the existing rate case cycles now in effect for Sierra, including for general rates and ECAC rates.
- (f) CalPeco and Sierra have entered into a settlement agreement with the Plumas-Sierra Rural Electric Cooperative (“PSREC”), City of Loyalton, City of Portola, Sierra County and Plumas County (“PSREC Settlement”). The PSREC Settlement is Exhibit Q to Exhibit 1 to the proceeding. The PSREC Settlement obligates Sierra and CalPeco to make certain payments to PSREC at specified times and subject to certain conditions. Among these is a payment of \$250,000 to be made to PSREC within fifteen days of Closing. Under the terms of the PSREC Settlement, in the event that the Commission were to ultimately approve CalPeco making an \$1 million investment in the Herlong Transmission Project (as defined in the PSREC Settlement) and to authorize CalPeco to recover rates on this investment, PSREC has agreed that it will credit the \$250,000 payment as an advance payment against CalPeco’s \$1 million investment. CalPeco and Sierra commit that if CalPeco never requests authority to make an investment in the PSREC Herlong Transmission Project or if CalPeco requests Commission authorization to invest in the Herlong Transmission Project and the Commission rejects such request in its entirety, that CalPeco and Sierra will retain 100% of the cost responsibility for the \$250,000 payment to PSREC (i.e., customers will be held harmless).
- (g) CalPeco shall adopt, maintain and strive to improve the high quality of service standards that Sierra presently provides its customers.

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<sup>2</sup> References to “Joint Application” herein are to the Joint Application of Sierra Pacific Power Company (U903E) and California Pacific Electric Company, LLC for Transfer of Control and Additional Requests Relating to Proposed Transaction filed with the Commission on October 16, 2009, as updated and supplemented by Joint Applicants’ letters to Administrative Law Judge Vieth dated April 7, 2010, June 11, 2010, and June 16, 2010.

- (h) Algonquin shall own at least fifty percent (50%) of CalPeco for a minimum period of ten (10) years.
- (i) CalPeco has requested that the Commission approve that either Algonquin or Emera be allowed to transfer to the other all or any portion of its ownership interest in CalPeco and without the need for any additional approval by the Commission (“Internal Transfer Approval”). The Internal Transfer Approval is described at page 70 and 71 of the Joint Application. In the event that the Commission were to grant the request for the Internal Transfer Approval, Emera and Algonquin will also commit to the following additional terms and conditions:
  - 1. Any reduction in the dollar amount of Emera's direct investment in CalPeco will be made up by an increase in a corresponding dollar amount of Emera's investment in Algonquin;
  - 2. Emera shall maintain its investment in Algonquin for a minimum period of three (3) years;
  - 3. Should Emera use the Internal Transfer Approval process to sell down all or any portion of its direct ownership in CalPeco, Emera nonetheless through its ownership in Algonquin would continue to be active in the oversight of CalPeco in a manner designed to enable CalPeco to continue to realize the benefits of Emera's financial and operating strengths and resources and in developing renewable projects; and
  - 4. Regardless of the authority that the Commission grants with respect to the Internal Transfer Approval with respect to changes of ownership interests in CalPeco between Algonquin and Emera, in no event shall Algonquin reduce for a minimum period of ten (10) years its ownership interest in CalPeco below the fifty percent (50%) interest committed to in Section 3(h) above.

**4. Employees and Management Team.**

- (a) CalPeco intends to the extent practicable to retain the same experienced operations team that has been responsible for operations of the California Utility under Sierra’s ownership. Any additional management team members which need to be recruited by CalPeco shall be experienced in electric utility operations.
- (b) CalPeco intends to maintain a local headquarters within the California Utility’s service territory, including maintaining a local management and customer service headquarters at a location within such service territory.
- (c) CalPeco intends to offer each of Sierra’s current administration and operations employees located within the service territory employment with CalPeco at the same locations with responsibilities and remuneration consistent with each of their existing roles. Accordingly, CalPeco shall make no material changes in the nature of the employment roles of the California Utility fulfilled by individuals

located within the service territory and intends, to the extent practical, to recruit within the California Utility service territory any additional operations staff necessary to replace functions currently performed by staff of Sierra located in Nevada. CalPeco will recognize the service and seniority of the former employees of Sierra who accept CalPeco's offer of employment for all non-pension purposes including vacation, sick pay benefits and for non-pension post retirement benefits such as retiree health benefits.

**5. Premium and Cost Synergies.**

- (a) CalPeco agrees that its rate recovery shall be calculated based on the regulatory value of the California Utility, as depreciated by Sierra, and totally independent of the purchase price to acquire the California Utility. CalPeco shall in no event seek to recover the excess of the purchase price over the regulatory book value of the utility assets (i.e., "premium") in rates. Any premium which CalPeco shall pay shall not be recorded in the accounts of CalPeco utilized in the establishment of rates and tariffs for the California Utility.
- (b) The cost levels CalPeco shall use to request rates in future general rate cases shall be based on the actual recorded cost levels of CalPeco and will incorporate any cost savings synergies arising in comparison to the baseline costs established in Sierra's 2008 rate case with respect to the California Utility.
- (c) CalPeco shall not seek to recover from ratepayers the "transaction costs" (e.g. investment banking and legal fees, and perimeter metering costs) associated with its acquisition of the California Utility. CalPeco recognizes that its incurrence of any such "transaction costs" is not related to the provision of electric service to the ratepayers of the California Utility and thus these costs are necessarily to be borne exclusively by its owners.

**6. California Regulatory Programs.**

- (a) Subject to the exemptions which are to be sought pursuant to the Required Regulatory Approvals as set out in the Power Purchase Agreement, CalPeco shall reaffirm Sierra's commitment to comply fully with the California RPS standards, the Commission's GHG Emissions Performance Standard, and the compliance requirements for operators of generating units imposed by the Commission's General Order 167.

**(END OF APPENDIX 3)**

## APPENDIX 4

### **Excerpt from Joint Application of Joint Applicants' Analysis of FERC "Seven Factor Test" Demonstrating that Distribution Capacity Agreement is Subject to This Commission's Jurisdiction**

Because (i) CalPeco will be providing Sierra capacity from the CalPeco distribution facilities for purposes of allowing Sierra to serve its retail customers in Nevada; (ii) Sierra will retain title to the power as it flows through the CalPeco facilities; and (iii) Sierra will be the load-serving distribution utility making the ultimate retail sales, CalPeco's provision of such distribution capacity service is "local distribution" service, appropriately subject to jurisdiction by this Commission. Under current law, while the FERC has exclusive jurisdiction over unbundled retail transmission service in interstate commerce, unbundled local distribution service is within the exclusive jurisdiction of the Commission.

Joint Applicants accordingly request that the Commission: (i) determine that all distribution facilities that will be transferred to CalPeco are properly considered to be "local distribution" facilities under the exclusive jurisdiction of the Commission, (ii) retain regulatory jurisdiction over such facilities after the Closing and assert jurisdiction over the Distribution Capacity Agreement and the transactions contemplated thereby, and (iii) authorize CalPeco to provide such distribution capacity services to Sierra based on the rates and other terms set forth in the agreement.<sup>1</sup>

#### **Background of Jurisdictional Issues**

Section 201 of the Federal Power Act<sup>2</sup> establishes exclusive federal jurisdiction for FERC to regulate the transmission of electricity in interstate commerce. Importantly, FERC's jurisdiction over interstate transmission does not extend to the regulation of local distribution services. The distinction between "FERC-jurisdictional transmission" facilities and "State-PUC local distribution" facilities has at times raised an issue as to whether particular facilities are subject to FERC or state regulatory jurisdiction.

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<sup>1</sup> CalPeco will be advising the FERC that the Joint Applicants have requested the Commission to assert jurisdiction over the Distribution Capacity Agreement.

<sup>2</sup> 16 U.S.C. § 824(b).

Traditionally, all retail sales of electricity were "bundled" with the delivery service for such sales, requiring the customer to pay an integrated charge that recovered the costs of both power procurement and delivery. FERC traditionally has not attempted to assert jurisdiction over the transmission or distribution component of any retail sales that are "bundled" with delivery of the electricity.

In Order No. 888, FERC required the "unbundling" of wholesale sales of electricity from the transmission service associated with those wholesale sales. FERC accordingly obligated transmission owners to offer a separate transmission service with specific requirements, including, the establishment of separate rates for transmission service and the offering of transmission service according to a standardized OATT.

Some states also began requiring that transmission and distribution providers, who previously sold a bundled retail product, to also "unbundle" the retail sale of power from the delivery component. The transmission service of these now unbundled transactions had previously been regulated by the states as part of a bundled retail product.

In Order No. 888, FERC held that such "transmission" service to such "unbundled" state retail customers would be subject to FERC's exclusive jurisdiction. FERC then had to determine the point at which the distribution facilities transitioned from providing interstate FERC-regulated transmission service to providing state-regulated "local distribution" service. In Order No. 888, FERC identified seven factors that it would consider in assessing whether the service CalPeco will provide under the Distribution Capacity Agreement constitutes service by "transmission" facilities or "local distribution" facilities.

#### **FERC's Seven Factor Test**

The seven factors FERC will consider on a case-by-case basis to determine whether particular facilities are local distribution facilities include: (i) local distribution facilities are normally in close proximity to retail customers; (ii) local distribution facilities are primarily radial in character; (iii) power flows into local distribution systems; it rarely, if ever, flows out; (iv) when power enters a local distribution system, it is not reconsigned or transported on to some other market; (v) power entering a local distribution system is consumed in a comparatively restricted geographical area; (vi) meters are based at the transmission/local

distribution interface to measure flows into the local distribution system; and (vii) local distribution systems will be of reduced voltage.<sup>3</sup>

FERC acknowledges that the application of its seven factors is necessarily judgmental, and that not all seven factors have to be satisfied for the facilities to be considered distribution. Importantly, FERC has adopted a policy to accord deference to a state's determination that particular facilities are "local distribution" facilities and are to be subject to the state's regulatory jurisdiction.<sup>4</sup>

Based on concerns raised by state commissions . . . ., we have further determined that it is appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs...

\* \* \*

We believe that [this] Commission should take advantage of state regulatory authorities' knowledge and expertise concerning the facilities of the utilities that they regulate.

\* \* \*

Moreover, we recognize that in some cases [this] Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities...

\* \* \*

If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule [this] Commission will defer to such classifications and/or cost allocations. In order to give such deference, we expect state regulators to specifically evaluate the seven indicators and any other relevant facts and to make recommendations consistent with the essential elements of the Rule.<sup>5</sup>

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<sup>3</sup> Order No. 888, FERC Stats. & Regs. ¶ 31,036 at 31,771.

<sup>4</sup> *Id.*, at 31,783.

<sup>5</sup> *Id.*, at 31,783-84.

Thus, Joint Applicants request that this Commission exercise its “knowledge and expertise” concerning the distribution facilities to be used in the Distribution Capacity Agreement, apply FERC’s seven factor test, determine that all CalPeco facilities are local distribution facilities, and assert its jurisdiction over the facilities and the Distribution Capacity Agreement.

**Application of the Seven Factor Test Demonstrates that Facilities to be Employed in the Distribution Capacity Agreement Should Remain Subject to this Commission’s Jurisdiction**

Factor 1 - Local distribution facilities are normally in close proximity to retail customers. Sierra’s California retail customers are concentrated in the South Lake Tahoe and North Lake Tahoe areas, with smaller clusters of customers in Portola, Loyalton, Truckee, Markleville, and Coleville/Walker. Virtually all of these customers are served by distribution facilities that are within 15 miles of these communities. Distribution facilities in the other areas are located even closer to the customers.

Factor 2 - Local distribution facilities are primarily radial in character. Absent an emergency situation in the Incline Village area, the California Utility distribution facilities are exclusively radial in nature. Power flows over the lines in only one direction, *i.e.*, toward the retail customers where it is consumed, and there is no generation in the area except for the 12 MW Kings Beach Generation Facility. South Lake Tahoe is served by radial lines from Sierra’s distribution system in Carson City, Nevada. Sierra’s transmission system in Truckee, California serves the North Lake Tahoe area. The remaining areas are also served by radial lines from the Sierra system.

Factor 3 - Power flows into local distribution systems; it rarely, if ever, flows out. Almost all of the power that will flow into CalPeco’s system will be consumed by customers within the CalPeco service territory.<sup>6</sup> The only material exception will be the power that Sierra will inject into CalPeco’s system for purposes of serving Sierra’s retail customers in Stateline, Incline Village and Verdi in accordance with the Distribution Capacity Agreement. CalPeco’s

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<sup>6</sup> As previously explained, CalPeco and Sierra have also executed the Borderline Customer Agreement for purposes of enabling both Parties to serve customers in their respective service territories and in proximity to the state border with existing facilities. Additionally, Sierra has been selling PG&E a small amount of wholesale power (just over 2 MW) in the Echo Summit, California area for purposes of enabling PG&E to serve its retail load in that area.

estimated total winter peak load of 120 MW is significantly larger than the estimated coincident peak load of approximately 23 MW that will flow to Sierra's Nevada customers in Incline Village, Stateline and Verdi.<sup>7</sup>

Factor 4 - When power enters a local distribution system, it is not reconsigned or transported on to some other market. The only distribution capacity that CalPeco will make available to a third party will be reflected in the Distribution Capacity Agreement and for the specific and limited purpose of enabling Sierra to most cost-effectively serve portions of its retail load in Stateline, Incline Village and Verdi. None of this power will flow into any market other than the isolated areas of Sierra's Nevada service territory referenced in Factor 3 above.

Factor 5 - Power entering a local distribution system is consumed in a comparatively restricted geographical area. The rationale given for Factor 1 applies equally to this factor.

Factor 6 - Meters are based at the transmission/local distribution interface to measure flows into the local distribution system. Perimeter metering will be installed and maintained to measure all flows into and out of CalPeco's distribution system.

Factor 7 - Local distribution systems will be of reduced voltage. Among the distribution assets that Sierra will be convey to CalPeco are 1400 miles of 12.5 kV, 14.4 kV, and 25.9 kV distribution circuits, 75 miles of 60kV distribution lines, and 19 miles of 120 kV distribution lines. The 120 kV and 60 kV lines connect CalPeco's distribution substations to Sierra's transmission and distribution systems. Two of the 120 kV lines connect CalPeco's South Lake Tahoe area with the Sierra distribution system at the Nevada/California state boundary, and the other 120 kV line connects the CalPeco North Lake Tahoe system to the Sierra transmission system at Truckee, California. There are also 60 kV lines in the North Lake Tahoe and South Lake Tahoe systems, and 14.4 kV distribution circuits will serve as interconnection points between the CalPeco and Sierra systems at Incline Village, Stateline, and Verdi.

There is no single definition of the physical or engineering characteristics of a "reduced voltage" distribution line. FERC has approved lines as high as 138 kV as local distribution

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<sup>7</sup> A small amount of power is expected to flow from the Kings Beach Generation Facility into western Incline Village on those occasions when Kings Beach is operated to provide reliability backup service to the north Lake Tahoe area in the event of a transmission or distribution outage. Under the Borderline Customer Agreement, power will flow from the CalPeco distribution system across the state line to Sierra's system to serve only three Nevada customers; the amount of power that moves across the state line is *de minimis*.

based on their function. Significantly, in one instance, FERC relied upon the determination of this Commission that the particular 138 kV facilities are local distribution facilities.<sup>8</sup> More recently, FERC also approved 115 kV lines as local distribution.<sup>9</sup>

The limited nature of three 120 kV lines to be transferred to CalPeco and the circumstances of their use, combined with the fact that the remaining lines are at a voltage of 60kV or below, should be considered to satisfy the seventh of FERC's factors. However, even if not all of the transferred lines are technically considered to be "reduced voltage," that result should not outweigh the six other factors clearly supporting the conclusion that the facilities are local distribution facilities that are properly subject to this Commission's jurisdiction.

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<sup>8</sup> *Pacific Gas and Electric Company, et al.*, 77 FERC ¶ 61,077 at 61,325 (1996).

<sup>9</sup> *Puget Sound Energy, Inc.*, 110 FERC ¶ 61,229 at 61,856 (2005).

Response No. PSC-004  
Attachment PSC-004 (LIB-D)

ALGONQUIN POWER & UTILITIES CORP.

# COST ALLOCATION MANUAL

Effective: January 1st, 2014

This document outlines the methods of direct charge and cost allocations: (i) between Algonquin Power & Utilities Corp. and its affiliates, Algonquin Power Company and Liberty Utilities (Canada) Corp.; (ii) between Liberty Utilities (Canada) Corp. and its regulated utility subsidiaries; (iii) between Liberty Utilities (Canada) Corp.'s service companies and its regulated utility subsidiaries; and (iv) between Liberty Utilities (Canada) Corp and Algonquin Power Company.

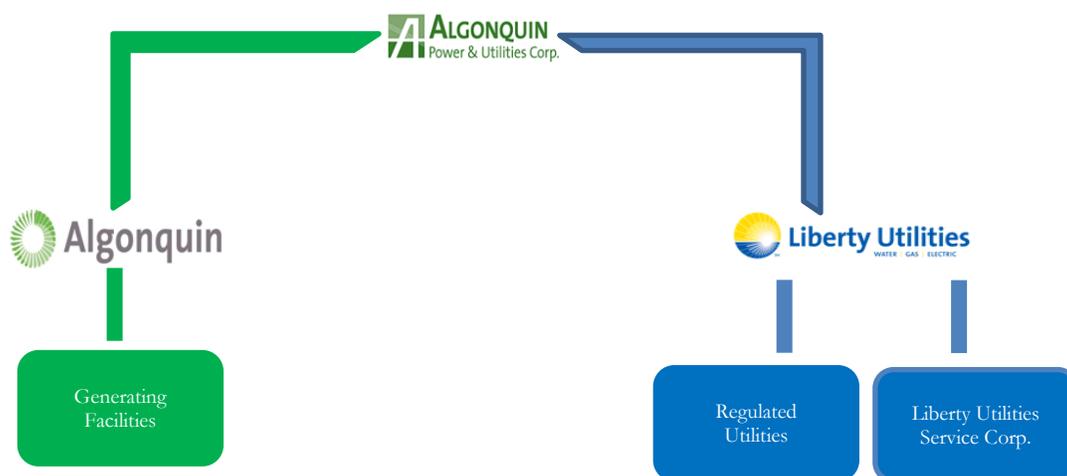
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## 1. INTRODUCTION

The purpose of this paper is to provide a detailed explanation of services provided by Algonquin Power & Utilities Corp (“APUC”), and its affiliates, Algonquin Power Company (“APCo”), Liberty Utilities (Canada) Corp. (“LUC”), and Liberty Utilities Service Corp. (“LUSC”) to the regulated utilities and to describe the Direct Charge and Cost Allocation Methodologies used by APUC, APCo, LUC, and LUSC. The following organization chart identifies the relationships between the separate entities.

**Figure 1: Algonquin Power & Utilities Corporate Structure**



This Cost Allocation Manual (“CAM”) has been completed in accordance and conformance with the NARUC Guidelines for Cost Allocations and Affiliate Transactions (“NARUC Guidelines”). More specifically, the founding principles of this Cost Allocation Manual are to a) directly charge as much as possible to the entity that procures any specific service, and b) to ensure that inappropriate subsidization of unregulated activities by regulated activities, and vice versa, does not occur. For ease of reference, the NARUC Guidelines are attached as Appendix 1.

Costs charged and allocated pursuant to this CAM shall include direct labor, direct materials, direct purchased services associated with the related asset or services, and overhead amounts. The direct charges are assigned as follows:

- a. Tariffed rates or other pricing mechanisms established by rate setting authorities shall be used to provide all regulated services;

- b. Services not covered by (a) shall be charged by the providing party to the receiving party at fully distributed cost; and
- c. Facilities and administrative services rendered to a rate-regulated subsidiary shall be charged on the following basis:
  - (i) the prevailing price for which the service is provided for sale to the general public by the providing party (i.e., the price charged to non-affiliates if such transactions with non-affiliates constitute a substantial portion of the providing party's total revenues from such transactions) or, if no such prevailing price exists, (ii) an amount not to exceed the fully distributed cost incurred by the providing party in providing such service to the receiving party.

## 2. THE APUC CORPORATE STRUCTURE

APUC's primary business is direct interest or equity ownership in renewable and thermal power generating facilities and regulated utilities. APUC owns a widely diversified portfolio of independent power production facilities and regulated utilities consisting of water distribution, wastewater treatment facilities, electric and gas utilities. While power production facilities are located in both Canada and the United States, regulated utility operations are exclusively in the United States. APUC is publicly traded on the Toronto Stock Exchange. Its structure as a publicly traded holding company provides substantial benefits to its regulated utilities through access to capital markets.

APUC is the ultimate corporate parent and affiliate that provides financial, strategic management, corporate governance, administrative and support services to LUC and its subsidiaries as well as to the numerous generation assets held by APCo. The services provided by APUC are necessary for LUC and its subsidiaries to have access to capital markets for capital projects and operations. These services are expensed at APUC and are performed for the benefit of APCo and LUC and their respective businesses.

APUC and its affiliates capitalize on APUC's expertise and access to the capital markets through the use of certain shared services, which maximizes economies of scale and minimizes redundancy. In short, it provides for maximum expertise at lower costs. Further, the use of shared expertise allows each of the entities to

receive a benefit they may not be able to achieve on a stand-alone basis such as strategic management advice and access to capital at more competitive rates.

### **3. SCOPE OF SERVICES AMONG AFFILIATES AND HOW THOSE COSTS ARE ALLOCATED**

#### **3.1. Labor Services and Cost Allocation from APUC to LUC and APCo**

APUC provides benefits to its affiliate companies by use of certain shared services. APUC charges labor rates for these shared services at cost, which is the dollar hourly rate per employee as recorded in APUC's payroll systems, grossed up for burdens such as payroll taxes, health benefits, retirement plans, other insurance provided to employees, and other employee benefits. These labor costs are charged directly based on timesheets to the extent possible. If labor is for the benefit of all subsidiaries then the allocation methodologies used for non-labor costs are applied.

APUC's non-labor services include Financing Services. As used herein Financing Services means the selling of units to public investors in order to generate the funding and capital necessary (be it short term or long term funding, including equity and debt) for LUC and APCo as well as providing legal services in connection with the issuance of public debt.

The capital and funds obtained from the sale of shares in APUC are used by LUC and APCo for current and future capital investments. The services provided by APUC are critical and necessary to LUC and APCo because without those services they would not have a readily available source of capital funding. Further, relatively small utilities may have difficulty attracting capital on a stand-alone basis.

The services provided by APUC specifically optimize the performance of the utilities, keeping rates low for customers while ensuring access to capital is available. If the utilities did not have access to the services provided by APUC, then they would be forced to incur associated costs for financing, capital investment, audits, taxes and other similar services on a stand-alone basis, which would substantially increase such costs. Simply put, without incurring these costs, APUC would not be able to invest capital in its subsidiaries, including the regulated utilities.

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In connection with the provision of Financing Services, APUC incurs the following types of costs: (i) strategic management costs (board of director, third-party legal services, accounting services, tax planning and filings, insurance, and required auditing); (ii) capital access costs (communications, investor relations, trustee fees, escrow and transfer agent fees); (iii) financial control costs (audit and tax expenses); and (iv) administrative (rent, depreciation, general office costs). See Appendix 2 for a more detailed discussion of the costs incurred by APUC.

Non-labor costs, including corporate capital, are pooled and allocated to LUC and APCo using the method summarized in Table 1. Each corporate cost type, or function, has been carefully reviewed to properly identify the factors driving those costs. Each function or cost type is typically driven by more than one factor each has been assigned an appropriate weighting. Table 1 includes brief commentary on the rationale for each cost driver and weighting, along with examples for each cost type.

**Table 1: Summary of Corporate Allocation Method of APUC Indirect Costs**

Type of Cost	Allocation Methodology	Rationale	Examples
Legal Costs	Net Plant 33.3% Number of Employees 33.3% O&M 33.3%	This function is driven by factors which include Net Plant, as typically the higher the value of plant, the more legal work it attracts; similarly, a greater number of employees are typically more indicative of larger facilities that require greater levels of attention; and O&M costs tend to be a third factor indicative of size and legal complexity.	Employee labor and related administration and programs; third party legal

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Tax Services	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by a variety of factors that influence the size and relative tax complexity, including Revenues, O&M and Net Plant. Tax activity can be driven by each of these factors.	Employee labor and related administration and programs, including Third party tax advice and services
Audit	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by a variety of factors that influence the size and complexity of Audit, including Revenues, O&M and Net Plant. Audit activity can be driven by each of these factors.	Employee labor and related administration and programs, including t Third party accounting and audit services
Investor Relations	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by factors which reflect the relative size and scope of each affiliate - Revenues, Net Plant and O&M costs.	Employee labor and related administration and programs, including third party Investor day communications and materials
Director Fees and Insurance	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by factors which reflect the relative size and scope of each affiliate - Revenues, Net Plant and O&M costs.	Board of Director fees, insurance and administration

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Licenses, Fees and Permits	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by factors which reflect the relative size and scope of each affiliate - Revenues, Net Plant and O&M costs.	Third party costs
Escrow and Transfer Agent Fees	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by factors which reflect the relative size and scope of each affiliate - Revenues, Net Plant and O&M costs.	Third party costs
Other Professional Services	Revenue 33.3% O&M 33.3% Net Plant 33.3%	This function is driven by factors which reflect the relative size and scope of each affiliate - Revenues, Net Plant and O&M costs.	Third party costs
Office Administration	Oakville Employees 50% Square Footage 50%	This function is driven by factors which are indicative of number of employees and square footage utilized by these employees.	Office space and utility costs. Employee labor and related administration

Notwithstanding the above, if a charge is related either solely to the regulated utility business, i.e., LUC, or to the power generation business, i.e., APCo, then all of those costs will be allocated to the business segment for which they are incurred (i.e. it is a direct charge).

Lastly, if a cost can be directly attributable to a specific entity, it will be directly charged to that entity. For an example of how an invoice would be allocated, please see Appendix 3.

Certain costs, which are incurred for the benefit of APUC's businesses, are not allocated to any subsidiary. These include costs such as donations, certain corporate travel, and certain overheads.

### **3.2. Labor Services and Cost Allocation From APCo To LUC**

From time to time, APCo may provide Engineering and Technical Labor to LUC or its utilities. These charges plus an allocation for corporate overheads such as rent, materials/supplies, etc. are capitalized and directly charged to the relevant utility.

From time to time, APCo employees may provide administrative support to LUC or its utilities. These charges are direct charged using time sheets.

## **4. SCOPE OF SERVICES PROVIDED BY LUC TO ITS SUBSIDIARIES, APUC AND APCO, AND HOW THOSE COSTS ARE ALLOCATED**

LUC provides its regulated utilities with the following services: accounting, administration, corporate finance, human resources (including training and development), information technology, rates and regulatory affairs, environment, health and safety, and security, customer service, procurement, risk management, legal, and utility planning. The following are examples of some of the services provided: (i) budgeting, forecasting, and financial reporting services including preparation of reports and preservation of records, cash management (including electronic fund transfers, cash receipts processing, managing short-term borrowings and investments with third parties); (ii) development of customer service policies and procedures; (iii) development of human resource policies and procedures; (iv) selection of information systems and equipment for accounting, engineering, administration, customer service, emergency restoration and other functions and implementation thereof; (v) development, placement and administration of insurance coverages and employee benefit programs, including group insurance and retirement annuities, property inspections and valuations for insurance; (vi) purchasing services including preparation and analysis of product specifications, requests for proposals and similar solicitations; and vendor and

vendor-product evaluations; (vii) energy procurement oversight and load forecasting; and (viii) development of regulatory strategy.

LUC will charge costs that can be directly attributable to a specific utility. These include direct labor and direct non-labor costs. However, the indirect LUC costs cannot be directly attributed to an individual utility. LUC allocates its indirect labor and indirect non-labor costs, including capital costs, to its regulated utilities using a Utility Four Factor Methodology. LUC uses the Utility Four Factor Methodology to allocate costs incurred for the benefit of all of its regulated assets (“System-Wide Costs”) to all of its utilities.

The Utility Four Factor Methodology allocates costs by relative size of the utilities. The methodology used by LUC involves four allocating factors, or drivers, (1) Utility Plant, (2) Total Customers, (3) Non-Labor Expenses, and (4) Labor, with each factor assigned an equal weight, as shown in Table 2 below.

**Table 2: Utility Four Factor Methodology Factors and Weightings**

<b>Factor</b>	<b>Weight</b>
Utility Plant	25%
Customer Count	25%
Non-Labor Expenses	25%
Labor	25%
<b>Total</b>	<b>100%</b>

LUC also uses the Utility Four Factor Methodology to allocate to its regulated utilities the system-wide indirect labor and indirect non-labor costs allocated to LUC from APUC.

Table 3 provides a simplified hypothetical example to demonstrate how the Utility Four Factor Methodology would be calculated based on ownership of only two hypothetical utilities.

**Table 3: Utility Four Factor Methodology Example**

Factor	Utility 1	Utility 2	Total All Utilities	Utility 1 % of Total	Factor Weight	Utility 1 Allocation
Utility Plant (\$)	727	371	1098	66%	25%	17%
Customer Count (#)	6000	1000	7000	86%	25%	21%
Labor (\$)	57	32	89	64%	25%	16%
Non-Labor Expenses (\$)	108	41	149	72%	25%	18%
<b>Total Allocation</b>						<b>72%</b>

As can be seen from these hypothetical numbers in Table 3, Utility 1 would be allocated 72% of the total Administrative/Overhead Costs incurred by LUC, based on its relative size and application of the Utility Four Factor Methodology. Utility 2 would be allocated the remaining 28%. LUC has developed and utilized this methodology to better allocate costs, recognizing that larger utilities require more time and management attention and incur greater costs than smaller ones.

LUC may also provide services to APUC and APCo. In these instances, LUC staff provide time sheets that depict the amount of time that is to be direct charged to either APUC or APCo.

In addition, LUC provides certain services that benefit the entire company, i.e., APCo and the utilities. These indirect costs are allocated using the following methodology shown in Table 4, which are designed to closely align the costs with the driver of the activity.

**Table 4: Summary of Corporate Allocation Method of LUC Indirect Costs**

Type of Cost	Allocation Methodology	Rationale	Examples
Risk Management	Net Plant 33.3% Revenue 33.3% O&M 33.3%	This function is driven by factors which reflect the relative size and complexity of Risk Management -	Software platform, fees and administration

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			Revenues, Net Plant and O&M costs.	
Information Technology	Number of Employees O&M	90% 10%	IT function is driven by factors which include number of employees and O&M. The larger the number of employees, the more support, software and IT infrastructure is required.	Enterprise wide support, architecture, etc. Third party fees
Human Resources	Number of Employees	100%	HR function is driven by number of employees. A greater number of employees requires additional HR support	HR policies, payroll processing, benefits, employee surveys
Training	Number of Employees	100%	Training is directly proportional to the number of employees per function	Courses, lectures, in house training sessions by third party providers
Facilities and Building Rent	Square Footage	100%	Office space occupied accurately reflects space requirements of each subsidiary	Corporate office building
Financial Reporting and Administration	Revenue O&M Net Plant	33.3% 33.3% 33.3%	This function is driven by factors which reflect the relative size and complexity of Financial Reporting and Admin. - Revenues, Net	Employee labor and related administration and third party fees

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			Plant and O&M costs.	
Environment, Health, Safety and Security	Number of Employees	100%	EHSS training, etc. is directly proportional to the number of employees per function	Enterprise wide programs, employee labor and related administration
Legal Costs	Net Plant Number of Employees O&M	33.3% 33.3% 33.3%	This function is driven by factors which include Net Plant, as typically the higher the value of plant, the more legal work it attracts; similarly, a greater number of employees are typically more indicative of larger facilities that require greater levels of attention; and O&M costs tend to be a third factor indicative of size and legal complexity.	Employee labor and related administration and programs, including third party legal
Treasury	Capital Expenditures O&M Net Plant	25% 50% 25%	Treasury activity is typically guided by the amount of necessary capex/plant for each utility, and operating costs/cashflow	Third party financing, employee labor and related administration and programs
Internal Audit	Net Plant O&M	25% 75%	This function is driven by factors which reflect the relative size and	Third party fees, employee labor and related administration

		complexity of Internal audit activity. Larger Plant and operating costs drive of a given facility drive more activity from IA.	and programs
Procurement	O&M 50% Capital Expenditures 50%	Procurement function is based on typical proportion of expenditures	Enterprise wide support and related administration
Communications	Number of Employees 100%	Communications cost is directly proportional to the number of employees	Enterprise wide support and related administration

## 5. LIBERTY UTILITIES SERVICE CORP.

All US utility employees are employed by Liberty Utilities Service Corp. (LUSC). All employees’ costs, such as salaries, benefits, insurances etc. are paid by LUSC and direct charged to the extent possible. Services provided from LUSC to each regulated utility shall be done on a time sheet basis to the extent possible. In instances where time sheeting may not be possible, the allocation factors shown in Table 5 are to be used.

**Table 5: Summary of Corporate Allocation Method of LUSC Indirect Costs**

Type of Cost	Allocation Methodology	Rationale	Examples
Customer Care and Billing	Customer count 100%	Customer count accurately reflects the resource requirements of the Customer Care and	Customer Care and Billing employees and related administrations

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			Billing group	
IT/Tech Support	Number of Employees	100%	Technical support requirements are related to the number of employees	Tech support staff, associated administration, and required software, hardware, etc.
Human Resources	Number of Employees	100%	HR function is driven by number of employees. A greater number of employees requires additional HR support	HR policies, payroll processing, benefits, employee surveys
Gas Control	Net Plant	100%	The greater the plant, the more control required	Gas Control labor, administration, and associated programs
Legal	Net Plant Number of Employees O&M	33.3% 33.3% 33.3%	Allocated based on the relative size of affiliate and employee count.	Employee labor and related administration and programs, including third party legal
Regulatory	Net Plant Number of Employees O&M	33.3% 33.3% 33.3%	Allocated based on the relative size of affiliate and employee count.	Utility-wide studies or third party costs beneficial to all utilities
Environment, Health, Safety and Security	Number of Employees	100%	EHSS training, etc. is directly proportional to the number of employees	Utility-wide programs, employee labor and related administration
Procurement	O&M Capital Expenditures	50% 50%	Based on typical proportion of expenditures	Utility-wide support and related administration

Please note the allocation methodology can be adjusted based on the number of participating utilities. For example, Customer Service representatives who serve only the New Hampshire utilities will only have their costs allocated based on the number of customers within New Hampshire. Labor cost associated with energy procurement is directly billed to the utilities using timesheets.

### **6. CORPORATE CAPITAL**

From time to time, APUC or LUC makes capital investments for the benefit of all the utilities or facilities it owns (examples include corporate headquarters, IT systems, etc.). All the capital investments will be kept at corporate level and charged monthly in the form of corporate capital rents to the regulated utilities. All costs associated to service the investment will be allocated to each utility based on that department's allocation where the capital investment is made. For example, if the capital investment is made in HR then the allocation methodology used for HR to allocate non-capital indirect costs as shown in Table 4 will be used to allocate the rent associated with the corporate capital expenditures, including the cost of capital, depreciation, property tax, operation and maintenance costs and all other cost associated with it. .

## 7. APPENDICES

### ***APPENDIX 1 - NARUC GUIDELINES FOR COST ALLOCATIONS***

#### **Guidelines for Cost Allocations and Affiliate Transactions:**

The following Guidelines for Cost Allocations and Affiliate Transactions (Guidelines) are intended to provide guidance to jurisdictional regulatory authorities and regulated utilities and their affiliates in the development of procedures and recording of transactions for services and products between a regulated entity and affiliates. The prevailing premise of these Guidelines is that allocation methods should not result in subsidization of non-regulated services or products by regulated entities unless authorized by the jurisdictional regulatory authority. These Guidelines are not intended to be rules or regulations prescribing how cost allocations and affiliate transactions are to be handled. They are intended to provide a framework for regulated entities and regulatory authorities in the development of their own policies and procedures for cost allocations and affiliated transactions. Variation in regulatory environment may justify different cost allocation methods than those embodied in the Guidelines.

The Guidelines acknowledge and reference the use of several different practices and methods. It is intended that there be latitude in the application of these guidelines, subject to regulatory oversight. The implementation and compliance with these cost allocations and affiliate transaction guidelines, by regulated utilities under the authority of jurisdictional regulatory commissions, is subject to Federal and state law. Each state or Federal regulatory commission may have unique situations and circumstances that govern affiliate transactions, cost allocations, and/or service or product pricing standards. For example, The Public Utility Holding Company Act of 1935 requires registered holding company systems to price "at cost" the sale of goods and services and the undertaking of construction contracts between affiliate companies.

The Guidelines were developed by the NARUC Staff Subcommittee on Accounts in compliance with the Resolution passed on March 3, 1998 entitled "Resolution Regarding Cost Allocation for the Energy Industry" which directed the Staff Subcommittee on Accounts together with the Staff Subcommittees on Strategic Issues and Gas to prepare for NARUC's consideration, "Guidelines for Energy Cost Allocations." In addition, input was requested from other industry parties. Various levels of input were obtained in the development of the Guidelines from

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the Edison Electric Institute, American Gas Association, Securities and Exchange Commission, the Federal Energy Regulatory Commission, Rural Utilities Service and the National Rural Electric Cooperatives Association as well as staff of various state public utility commissions.

In some instances, non-structural safeguards as contained in these guidelines may not be sufficient to prevent market power problems in strategic markets such as the generation market. Problems arise when a firm has the ability to raise prices above market for a sustained period and/or impede output of a product or service. Such concerns have led some states to develop codes of conduct to govern relationships between the regulated utility and its non-regulated affiliates. Consideration should be given to any "unique" advantages an incumbent utility would have over competitors in an emerging market such as the retail energy market. A code of conduct should be used in conjunction with guidelines on cost allocations and affiliate transactions.

### A. DEFINITIONS

1. Affiliates - companies that are related to each other due to common ownership or control.
2. Attestation Engagement - one in which a certified public accountant who is in the practice of public accounting is contracted to issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party.
3. Cost Allocation Manual (CAM) - an indexed compilation and documentation of a company's cost allocation policies and related procedures.
4. Cost Allocations - the methods or ratios used to apportion costs. A cost allocator can be based on the origin of costs, as in the case of cost drivers; cost-causative linkage of an indirect nature; or one or more overall factors (also known as general allocators).
5. Common Costs - costs associated with services or products that are of joint benefit between regulated and non-regulated business units.
6. Cost Driver - a measurable event or quantity which influences the level of costs incurred and which can be directly traced to the origin of the costs themselves.

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7. Direct Costs - costs which can be specifically identified with a particular service or product.
8. Fully Allocated costs - the sum of the direct costs plus an appropriate share of indirect costs.
9. Incremental pricing - pricing services or products on a basis of only the additional costs added by their operations while one or more pre-existing services or products support the fixed costs.
10. Indirect Costs - costs that cannot be identified with a particular service or product. This includes but not limited to overhead costs, administrative and general, and taxes.
11. Non-regulated - that which is not subject to regulation by regulatory authorities.
12. Prevailing Market Pricing - a generally accepted market value that can be substantiated by clearly comparable transactions, auction or appraisal.
13. Regulated - that which is subject to regulation by regulatory authorities.
14. Subsidization - the recovery of costs from one class of customers or business unit that are attributable to another.

## B. COST ALLOCATION PRINCIPLES

The following allocation principles should be used whenever products or services are provided between a regulated utility and its non-regulated affiliate or division.

1. To the maximum extent practicable, in consideration of administrative costs, costs should be collected and classified on a direct basis for each asset, service or product provided.
2. The general method for charging indirect costs should be on a fully allocated cost basis. Under appropriate circumstances, regulatory authorities may consider incremental cost, prevailing market pricing or other methods for allocating costs and pricing transactions among affiliates.

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3. To the extent possible, all direct and allocated costs between regulated and non-regulated services and products should be traceable on the books of the applicable regulated utility to the applicable Uniform System of Accounts. Documentation should be made available to the appropriate regulatory authority upon request regarding transactions between the regulated utility and its affiliates.
4. The allocation methods should apply to the regulated entity's affiliates in order to prevent subsidization from, and ensure equitable cost sharing among the regulated entity and its affiliates, and vice versa.
5. All costs should be classified to services or products which, by their very nature, are either regulated, non-regulated, or common to both.
6. The primary cost driver of common costs, or a relevant proxy in the absence of a primary cost driver, should be identified and used to allocate the cost between regulated and non-regulated services or products.
7. The indirect costs of each business unit, including the allocated costs of shared services, should be spread to the services or products to which they relate using relevant cost allocators.

### C. COST ALLOCATION MANUAL (NOT TARIFFED)

Each entity that provides both regulated and non-regulated services or products should maintain a cost allocation manual (CAM) or its equivalent and notify the jurisdictional regulatory authorities of the CAM's existence. The determination of what, if any, information should be held confidential should be based on the statutes and rules of the regulatory agency that requires the information. Any entity required to provide notification of a CAM(s) should make arrangements as necessary and appropriate to ensure competitively sensitive information derived therefrom be kept confidential by the regulator. At a minimum, the CAM should contain the following:

1. An organization chart of the holding company, depicting all affiliates, and regulated entities.
2. A description of all assets, services and products provided to and from the regulated entity and each of its affiliates.

3. A description of all assets, services and products provided by the regulated entity to non-affiliates.
4. A description of the cost allocators and methods used by the regulated entity and the cost allocators and methods used by its affiliates related to the regulated services and products provided to the regulated entity.

#### D. AFFILIATE TRANSACTIONS (NOT TARIFFED)

The affiliate transactions pricing guidelines are based on two assumptions. First, affiliate transactions raise the concern of self-dealing where market forces do not necessarily drive prices. Second, utilities have a natural business incentive to shift costs from non-regulated competitive operations to regulated monopoly operations since recovery is more certain with captive ratepayers. Too much flexibility will lead to subsidization. However, if the affiliate transaction pricing guidelines are too rigid, economic transactions may be discouraged.

The objective of the affiliate transactions' guidelines is to lessen the possibility of subsidization in order to protect monopoly ratepayers and to help establish and preserve competition in the electric generation and the electric and gas supply markets. It provides ample flexibility to accommodate exceptions where the outcome is in the best interest of the utility, its ratepayers and competition. As with any transactions, the burden of proof for any exception from the general rule rests with the proponent of the exception.

1. Generally, the price for services, products and the use of assets provided by a regulated entity to its non-regulated affiliates should be at the higher of fully allocated costs or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator.
2. Generally, the price for services, products and the use of assets provided by a non-regulated affiliate to a regulated affiliate should be at the lower of fully allocated cost or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator.
3. Generally, transfer of a capital asset from the utility to its non-regulated affiliate should be at the greater of prevailing market price or net book value, except as

otherwise required by law or regulation. Generally, transfer of assets from an affiliate to the utility should be at the lower of prevailing market price or net book value, except as otherwise required by law or regulation. To determine prevailing market value, an appraisal should be required at certain value thresholds as determined by regulators.

4. Entities should maintain all information underlying affiliate transactions with the affiliated utility for a minimum of three years, or as required by law or regulation.

### E. AUDIT REQUIREMENTS

1. An audit trail should exist with respect to all transactions between the regulated entity and its affiliates that relate to regulated services and products. The regulator should have complete access to all affiliate records necessary to ensure that cost allocations and affiliate transactions are conducted in accordance with the guidelines. Regulators should have complete access to affiliate records, consistent with state statutes, to ensure that the regulator has access to all relevant information necessary to evaluate whether subsidization exists. The auditors, not the audited utilities, should determine what information is relevant for a particular audit objective. Limitations on access would compromise the audit process and impair audit independence.

2. Each regulated entity's cost allocation documentation should be made available to the company's internal auditors for periodic review of the allocation policy and process and to any jurisdictional regulatory authority when appropriate and upon request.

3. Any jurisdictional regulatory authority may request an independent attestation engagement of the CAM. The cost of any independent attestation engagement associated with the CAM, should be shared between regulated and non-regulated operations consistent with the allocation of similar common costs.

4. Any audit of the CAM should not otherwise limit or restrict the authority of state regulatory authorities to have access to the books and records of and audit the operations of jurisdictional utilities.

5. Any entity required to provide access to its books and records should make arrangements as necessary and appropriate to ensure that competitively sensitive information derived therefrom be kept confidential by the regulator.

## F. REPORTING REQUIREMENTS

1. The regulated entity should report annually the dollar amount of non-tariffed transactions associated with the provision of each service or product and the use or sale of each asset for the following:

- a. Those provided to each non-regulated affiliate.
- b. Those received from each non-regulated affiliate.
- c. Those provided to non-affiliated entities.

2. Any additional information needed to assure compliance with these Guidelines, such as cost of service data necessary to evaluate subsidization issues, should be provided.

Source:

<http://www.naruc.org/Publications/Guidelines%20for%20Cost%20Allocations%20and%20Affiliate%20Transactions.pdf>

## ***APPENDIX 2 – DETAILED EXPLANATION OF APUC COSTS***

### **1. APUC STRATEGIC MANAGEMENT COSTS**

Strategic management decisions are critical for any public utility. The need for strategic management is even more pronounced for APUC as a publicly traded company, which depends on access to capital funding through public sales of units. APUC seeks to hire talented strategic managers that aid in running each facility owned by the company as efficiently and effectively as possible. This ensures the long term health of each utility and ensures that rates are kept as low as possible without compromising the level of service. It also facilitates each regulated utility's access to necessary capital funding at reduced costs. The costs included in Strategic Management Costs fall into the following categories.

#### a. Board of Directors

The Board of Directors provides strategic oversight on all company affairs including high level approvals of strategy, operation and maintenance budgets, capital budgets, etc. In addition, the Board of Directors provides corporate governance and ensures that capital and costs are incurred prudently, which ultimately protects ratepayers.

#### b. General Legal Services

General legal services involve legal matters not specific to any single facility, including review of audited financial statements, annual information filings, Sedar filings, review of contracts with credit facilities, incorporation, tax issues of a legal nature, market compliance, and other similar legal costs. These legal services are required in order for APUC to provide capital funding to individual utilities, without which the utilities could not provide adequate service. Additionally, the services ensure that APUC's subsidiaries remain compliant in all aspects of operations and prevents those entities from being exposed to unnecessary risks.

#### c. Professional Services

Professional Services including strategic plan reviews, capital market advisory services, ERP System maintenance, benefits consulting, and other similar professional services. By providing these services at a parent level, the subsidiaries are able to benefit from economies of scale. Additionally, some of these services improve APUC's access to capital which benefits all of its subsidiaries.

## 2. ACCESS TO CAPITAL MARKETS

One of APUC's primary functions is to ensure its subsidiaries have access to quality capital. APUC is listed on the Toronto Stock Exchange, a leading financial market. In order to allow its subsidiaries to have continued access to those capital markets, APUC incurs the following costs. These services and costs are a prerequisite to the subsidiaries continued access to those capital markets.

### a. License and Permit Fees

In connection with APUC's participation in the Toronto Stock Exchange, APUC incurs certain license and permit fees such as Sedar fees, annual filing fees, licensing fees, etc. These licensing and permit fees are required in order to sell units on the Toronto Stock Exchange, which in turn provides funding for utility operations.

### b. Escrow Fees

In connection with the payment of dividends to unit holders, APUC incurs escrow fees. Escrow fees are incurred to ensure continued access to capital and ensure continuing and ongoing investments by shareholders. Without such escrow fees, APUC's subsidiaries would not have a readily available source of capital funding.

### c. Unit Holder Communications

Unit holder communication costs are incurred to comply with filing and regulatory requirements of the Toronto Stock Exchange and meet the expectations of shareholders. These costs include items such as news releases and unit holder conference calls. In the absence of shareholder communication costs, investors would not invest in the units of APUC, and in turn, APUC would not have capital to invest in its subsidiaries. With such communications services, the subsidiaries would not have a readily available source of capital funding.

## 3. APUC FINANCIAL CONTROLS

Financial control costs incurred by APUC include costs for audit services and tax services. These costs are necessary to ensure that the subsidiaries are operating in a manner that meets audit standards and regulatory requirements, which have strong financial and operational controls, and financial transactions are recorded

accurately and prudently. Without these services, the regulated utilities would not have a readily available source of capital funding.

### a. Audit Fees

Audits are done on a yearly basis and reviews are performed quarterly on all facilities owned by APUC on an aggregate level. These corporate parent level audits reduce the cost of the stand-alone audits significantly for utilities which must perform its own separate audits. Where stand-alone audits are not required, ratepayers receive benefits of additional financial rigor, as well as access to capital, and financial soundness checks by third parties. Finally, during rate cases, the existence of audits provides staff and intervenors additional reliance on the company records, thus reducing overall rate case costs. The aggregate audit is necessary for the regulated utilities to have continued access to capital markets and unit holders.

### b. Tax Services

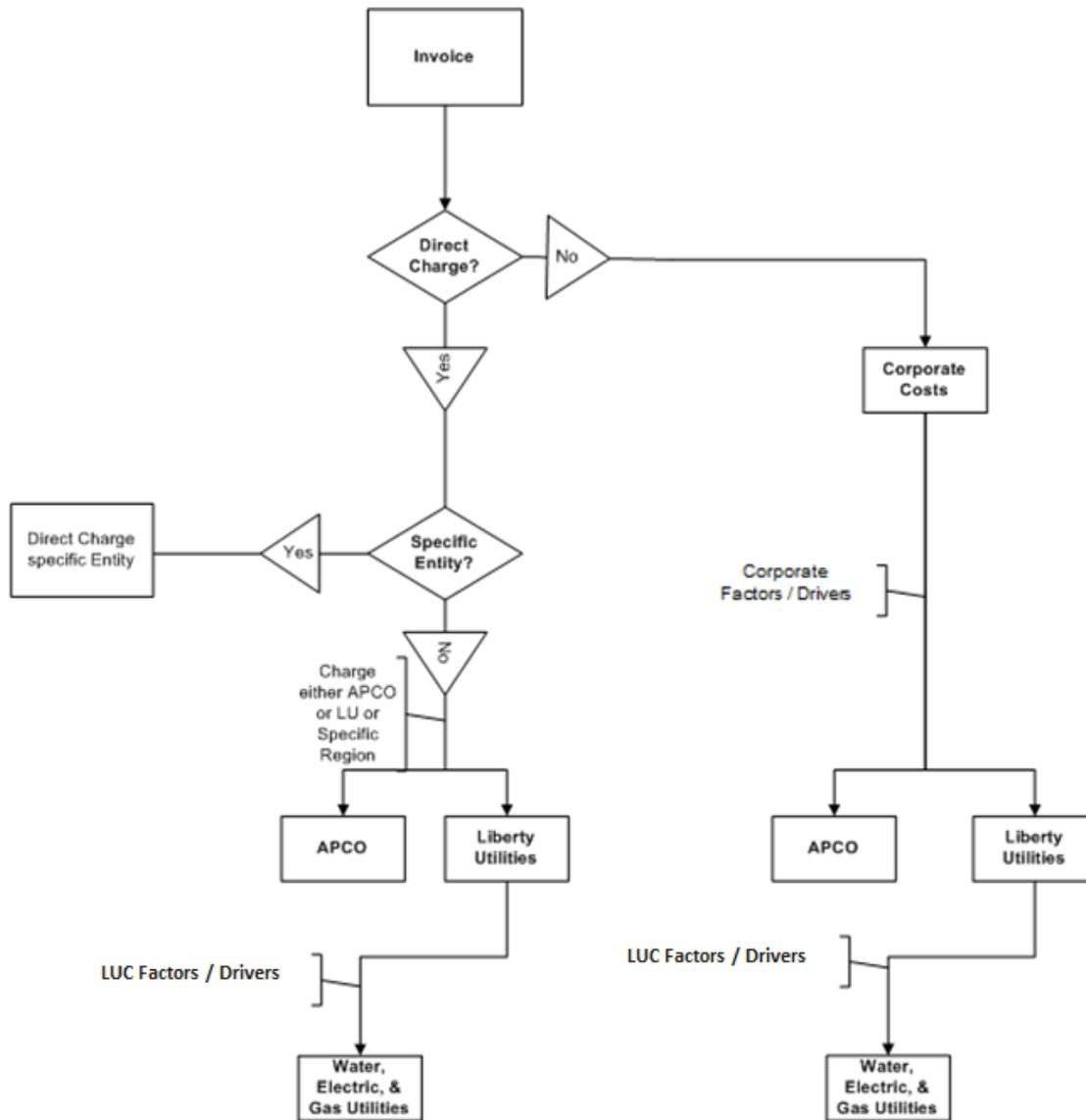
Taxes are paid on behalf of the regulated utilities at the parent level as part of a consolidated United States tax return. Tax services such as planning and filing are provided by third parties. Filing tax returns on a consolidated basis benefits each regulated utility by reducing the costs that otherwise would be incurred by such utility in filing its own separate tax return.

## 4. APUC ADMINISTRATIVE COSTS

Finally, administrative costs incurred by APUC such as rent, depreciation of office furniture, depreciation of computers, and general office costs are required to house all the services mentioned above. Without these administrative costs, the employees of APUC could not perform their work and provide the necessary services to the regulated utilities. These administrative costs also include training for corporate employees.

**APPENDIX 3 – LIFE OF AN INVOICE**

A hypothetical example is being provided of an invoice received by APUC for services to be allocated to its subsidiaries. The diagram below is intended to visually explain APUC’s allocation to APCo and Liberty Utilities.



PSC-005

Regarding: Liberty Board of Directors

Witness: Unknown

- a. Was the decision to purchase Western Water made solely by Liberty Utilities without consultation of any representatives of any parent (indirect or direct) company? Please explain.

**Response:** The Board of APUC was consulted and determined that the acquisition was desirable and in the best interest of APUC that Liberty Utilities consummate the transaction. In addition, APUC CEO and Director Ian Robertson serves as a director of Liberty and was involved in approving the transaction at the APUC and Liberty Utilities levels.

- b. Are there common members of the board of directors of Liberty Utilities and any parent (indirect or direct) of Liberty Utilities? If so, please specify and provide which other boards those members serve on.

**Response:** The common member of the boards of directors of Liberty Utilities Co. and any parent (direct and indirect) is Ian Robertson.

- c. Please provide the names and biographies of each of the board members of Liberty Utilities.

**Response:** The members of the board of directors for Liberty Utilities Co. are Ian Robertson, Richard Leehr and Greg Sorensen. Biographies for Mr. Robertson, Mr. Leehr and Mr. Sorensen are attached as Attachment PSC-005 (LIB-A).

Response No. PSC-005  
Attachment PSC-005 (LIB-A)



### **Ian Robertson, Chief Executive Officer**

Ian Robertson serves as Chief Executive Officer of Algonquin Power & Utilities Corp. (APUC). He is a founder and principal of Algonquin Power Corporation Inc., an independent power developer, which was formed in 1988 and is the predecessor organization to APUC.

Ian has over 25 years of experience in the development, financing, acquisition and operation of electric power generating projects both in North America and internationally. He is an electrical engineer and holds a Professional Engineering designation through his Bachelor of Applied Science awarded by the University of Waterloo and a Master of Business Administration from York University's Schulich School of Business. In addition, Ian was awarded a Chartered Financial Analyst designation in 2001. Ian received a Chartered

Director designation from McMaster University in 2008. Consistent with his commitment to continuing education, Ian is currently pursuing a Master of Laws at the University of Toronto, Law School.

In addition to his principal occupation as Chief Executive Officer of Algonquin Power & Utilities Corp., Ian has served as a director on a number of Boards of Directors for public companies in the electrical generation and oil and gas sectors, and is a member of the Board of Directors of the American Gas Association.



### **Dick Lehr, President, Pipelines & Transmission**

Dick Lehr is the President of Liberty Utilities (Pipeline & Transmission) Corp. based in Londonderry, New Hampshire. Previously he served as President of Liberty Energy Utilities – NH. Prior to joining Liberty, Dick served as a consultant for utilities developing northeast infrastructure projects drawing from the Marcellus/Utica shale region. He has also served in progressive, challenging senior executive capacities in the interstate gas pipeline industry over his 40 year career. More recently, Dick served as President of a natural gas pipeline company and was responsible for the revival, development, construction, and eventual operations that served the premium New York markets. Dick is a graduate of John Carroll University.

**Greg Sorensen, President, Liberty Utilities - Arizona**

Greg Sorensen is the President of Liberty Utilities Sub Corp. based in Avondale, Arizona. Previously he served as Director of Operations and Vice President Finance for the same organization. Prior to joining Liberty in 2005, Greg served as a Vice President Finance and Executive team member for an international call center company located in Tempe, Arizona. Greg also serves on the Board of Directors of the Water Utility Association of Arizona. Greg is a graduate of Wake Forest University.

PSC-006

Regarding: Algonquin not a formal applicant  
Witness: Unknown

Please explain why Algonquin has chosen not be a formal applicant in this docket, given that Liberty Utilities is a wholly-owned subsidiary of that company.

**Response:** Liberty believes it is inappropriate and unnecessary to add APUC as a joint applicant or as a party to this docket. APUC does not have a direct interest in the transaction, and will not have direct control over the Montana utility, Mountain Water, if the requested approval is granted. Liberty Utilities and Liberty WWC are appropriate joint applicants in this matter because they are parties to the Plan and Agreement of Merger. Given that the Commission's regulatory authority extends only to Mountain Water, it seems unlikely the Commission has any authority over any upstream entities. However, in keeping with Commission precedent, Liberty Utilities and Liberty WWC consented to Commission jurisdiction for the limited purpose of supporting the request for approval of the proposed merger. Liberty believes the current joint entities will be able to provide relevant information needed for the Commission's review of this matter. Liberty also believes that the Commission does not have jurisdiction directly over APUC and cannot properly require APUC to be a party to this proceeding.

PSC-007

Regarding: Allocated Value of Mountain Water  
Witness: Unknown

The purchase price of Western Water is stated to be \$327MM with \$250MM cash and assumption of \$77MM of debt obligations.

- a. What is the separate value of Mountain Water in the proposed sale and merger?

**Response:** Liberty Utilities' final offer as accepted by the Seller entities did not include a separate valuation for Mountain Water, but was based on an enterprise value for Park Water, Apple Valley and Mountain Water.

- b. Please provide all work papers supporting the valuation both in hard copy and electronic format.

**Response:** Liberty objects to this request because it seeks information which is not relevant to this matter and is protected from disclosure as it is confidential and contains proprietary trade secrets. Liberty's due diligence work papers are not relevant because they have no impact on Mountain Water's consumers. The documents are not tied to the service consumers will receive, the operations of Mountain Water, or the rates consumers will pay. Moreover, Liberty's internal valuation will not affect Mountain Water's rates or the level of service, as stated in Liberty's application because Liberty does not intend to seek an acquisition adjustment to the existing rate base. Regardless of these considerations, all future rate changes will be subject to the Commission's review and approval. Accordingly, this request seeks information that has no bearing on the Commission's decision in this matter, and as such seeks information that is irrelevant and not reasonably calculated to lead to the discovery of admissible information.

The requested information is also protected from disclosure because it is proprietary and contains confidential trade secrets. Liberty's due diligence efforts, including any financial analyses of potential investments, are based upon years of research and investment at a substantial cost to Liberty Utilities. The underlying financial and other analyses and overall bid strategy and methodologies that Liberty implements in responding to solicitations relating to the sale of regulated utilities are proprietary and contain confidential trade secrets. Moreover, compelling winning bidders to disclose their successful strategy will necessarily have a chilling effect on the participation in the market of future offerings of utility assets. Disclosure of such information, even under seal, would be harmful to the business interests of Liberty, because both its seller and the City are parties who could obtain these materials, and the Commission cannot provide certainty that information produced, even under protective order, would not be subject to disclosure on challenge by a party or outside interested party.

- c. What was the percentage of debt allocation, and separately, the equity allocation for Mountain Water? Please provide supporting work papers.

**Response:** The proposed transaction would have Liberty WWH merge with and into Western Water Holdings, and Liberty Utilities, as a consequence of such merger, to acquire the stock of Western Water Holdings. The result will have Liberty Utilities acquiring WWH, which is the parent to the entire Park operations, inclusive of all three operating utilities in the states of California and Montana. Thus, no allocation of debt and/or equity will be made by Liberty Utilities for Mountain Water.

The anticipated debt and equity required to close the proposed acquisition will be as follows:

Debt component: the debt component will consist of present third party debt plus debt raised by Liberty Utilities by its Private Placement Platform

Equity component: Equity for the acquisition will be provided by Liberty Utilities.

PSC-008

Regarding: Acquisition adjustment

Witness: Unknown

The application states in paragraph 16 page 5 that “The merger of Western Water Holdings and Liberty WWH also does not impact the operations of Mountain Water in the State of Montana, or the rates that Mountain Water has been authorized by the Commission to charge for water service.”

Does this mean that Liberty Utilities will not be seeking an acquisition adjustment for the purchase of Western Water above the regulated rate base of the company? Please explain.

**Response:** Yes, Liberty does not intend to seek an acquisition adjustment to the existing rate base of Mountain Water in a future rate case. Liberty will, of course, seek recovery of and on investment made in actual rate base assets in future rate cases.

PSC-009

Regarding: "No harm to consumer"

Witness: Unknown

The application is proposing the Commission adopt the "No-harm to consumers' standard" for the determination of approval of the application. Specifically to Montana, the last authorized regulated rate base for Montana was approximately \$35,651,607 with an additional \$534,224 from the main office allocated to Montana for a total rate base of \$36,185,831.

- a. Is Liberty Utilities taking the position that it will not seek a return on or return of any investment above the regulated rate base? Please explain.

**Response:** As described in response to PSC-008, Liberty will not seek an acquisition adjustment as a result of the transaction subject to approval of the Commission in this docket, but reserves the right to seek recovery of and on investment in regulated rate base assets after MWC's last rate case.

- b. Is Liberty Utilities aware that Montana characteristically does not allow acquisition adjustments in the determination of rate base or return on equity?

**Response:** Yes.

- c. Is Liberty Utilities aware that Montana uses an historical test year as the basis for establishing rates?

**Response:** Yes.

- d. Given a hypothetical \$40MM rate base for MWC, a 50/50 capital structure, and a 10% ROE, the approximate equity return would be \$2MM. What would be the yield on the investment in MWC based on the allocated value provided in a previous data request (PSC-007)?

**Response:** It is impossible for Liberty to accurately answer this hypothetical, based on a separate allocation to MWC. As indicated in the prior responses, there is no separate allocation of transaction price to Mountain Water.

- e. What is the current 30-year treasury rate?

**Response:** 2.592% (as of February 6, 2015).

PSC-010

Regarding: Allocation of expenses

Witness: Unknown

Presently there is no overhead (Main Office Expense) that is being charged by Western Water to Park Water or Mountain Water.

- a. Will there be an allocation of Western Water or other entity expenses to the overhead of Park Water? Please explain.

**Response:** There will be no allocation from Western Water. In the future, Liberty anticipates integrating Park Water's centralized services into Liberty Utilities. While the details of such integration cannot be determined until Liberty assumes operations, the goal of integration will be to provide economies of scale and efficiencies, and to minimize or eliminate duplication for the benefit of MWC customers.

- b. If Liberty Utilities integrates its cash management system, will there be an overhead cost associated with the use of the cash management system?

**Response:** Yes. Park Water or Mountain Water, depending on the ultimate structure, will, presumably, receive its allocation of corporate Treasury costs associated with the cash management system.

PSC-011

Regarding: Cash Management

Witness: Unknown

- a. Order No. 7149d stated that Mountain must file for Commission approval of a cash management plan incorporating best practices protecting Mountain's and its parent's credit from risks associated with participating in a shared money pool with such affiliates. Will that be the case with Liberty Utilities? Please explain.

**Response:** Yes. Liberty intends to integrate the Park Water utilities into its money pool. [For the purpose of this question, the response assumes that "cash management plan" is intended to incorporate the day-to-day money needs of a utility]. Liberty has not identified recognized industry "best practices," but has historically operated a shared money pool for all its utility affiliates, as approved by the respective regulators. This arrangement has not had a negative impact on the credit rating of the affiliates. Cash management is a centralized function at Liberty Utilities and is run through the Treasury Group. Treasury, through Liberty Utilities Co, will provide sufficient liquidity to assist all of its operating utilities, as it will the Park utilities in the future, in meeting their daily cash needs. As a result, the cash management system should have no discernible impact on credit ratings, to the extent Mountain Water receives a separate credit rating.

- b. Please provide a copy of Liberty's cash management plan.

**Response:** Cash management is a centralized function at Liberty Utilities and is run through the Treasury Group. Treasury, through Liberty Utilities Co, will provide sufficient liquidity to assist all of its operating utilities, including Mountain Water in the future, in meeting their daily cash needs. Any revenues received by MWC, as with all other utilities within the Liberty money pool, would be input into the money pool on a daily basis. The money pool is operated and managed by an independent third party financial institution and all transactions are carefully monitored, recorded and tracked, and are fully in compliance with all GAAP accounting standards.

PSC-012

Regarding: Carlyle/City/Clark Fork Coalition Letter Agreement

Witness: Unknown

Please address each of the issues in Paragraph 47 of Final Order 7149d. Please explain and provide supporting documentation that each of the conditions has been met.

**Response:** Liberty does not have any independent knowledge or information responsive to this request. Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-013

Regarding: Letter Agreement Order 7149d, paragraphs 79-80 – Rattlesnake Watershed  
Witness: Unknown

If the sale and transfer is approved, will the successor company continue to honor the Letter Agreement that the Rattlesnake Watershed will only be used for emergency backup water supply and that Missoula water would be kept in the Missoula area watershed? Please explain.

**Response:** Liberty assumes that this data request is referencing section 3 of the September 22, 2011 Letter Agreement between the City of Missoula, the Clark Fork Coalition and Carlyle Infrastructure Partners. Liberty will consent to inclusion of provisions consistent with the paragraph 3(a), 3(b) and 3(c) of that Letter Agreement relating to the Rattlesnake Watershed in the final order approving the transaction in this docket.

PSC-014

Regarding: Western Water Schedule 4.21(a)

Witness: Unknown

Please provide a copy of the loans and guarantees indicated in Schedule 4.21(a).

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-015

Regarding: Schedule 4.18(b)

Witness: Unknown

Please provide copies of each of the agreements 1-14.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-016

Regarding: Schedule 6.8(d)

Witness: Unknown

Please provide copy of agreement referred to in this Schedule.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-017

Regarding: Liberty Utilities' water utilities

Witness: Unknown

List the water distribution utility systems owned by Liberty Utilities along with their locations, numbers of customers, and the dates when Liberty assumed operation of the systems.

**Response:** The table below identifies all water utilities, and their sub-regions, owned and operated by Liberty utilities.

<u>Utility</u>	<u>Location</u>	<u>Customers</u>	<u>LU Ownership Date</u>
Black Mountain	Arizona	2,121	March 20, 2001
Gold Canyon	Arizona	6,548	July 9, 2001
Entrada Del Oro	Arizona	332	August 26, 2008
LPSCO	Arizona	39,918	February 25, 2003
Rio Rico	Arizona	8,454	December 2, 2005
Bella Vista	Arizona	8,812	April 18, 2002
Northern Sunrise	Arizona	336	July 7, 2004
Southern Sunrise	Arizona	760	July 7, 2004
Holiday Hills	Missouri	476	August 29, 2004
Timber Creek	Missouri	41	August 29, 2004
Ozark Mountain	Missouri	483	August 29, 2004
Noel	Missouri	663	March 4, 2011
KMB	Missouri	707	March 18, 2011
Fox River	Illinois	439	August 29, 2004
Holly Ranch	Texas	1,993	August 29, 2004
Big Eddy	Texas	1,054	August 29, 2004
Piney Shores	Texas	543	August 29, 2004
Hill Country	Texas	632	August 29, 2004
Tall Timbers	Texas	2,205	November 5, 2002
Woodmark	Texas	1,828	December 18, 2002
Seaside Resort	Texas	468	February 28, 2010
Pine Bluff	Arkansas	16,332	February 1, 2013
Whitehall Water	Arkansas	1,920	June 2014
Whitehall Sewer	Arkansas	1,821	June 2014

PSC-018

Regarding: Ring fencing requirements, p. 10 of application

Witness: Unknown

- a. An existing Mountain Water ring-fencing provision requires Mountain to notify the Commission 30 days in advance of any dividend declarations, or other transfer that exceeds 5% of Mountain's shareholder equity. Please explain why your provision (F) does not include the 30-day advance notice requirement.

**Response:** Liberty chose to include a provision in the Joint Application that is consistent with the commitments made, and approved, in California when it purchased the assets of the CalPeco Electric system. Liberty believes that its commitment to maintain the financial integrity of the Mountain Water utility through its Cash Management Plan sufficiently protects MWC and its customers. A more specific requirement, such as the 30 day requirement to notify the Commission, creates the increased potential for conflict with financial public disclosure provisions. Moreover, the advance notice is not necessary and may limit Liberty's ability to adequately manage and maintain the financial integrity of the utility, and would unnecessarily differentiate MWC from the other Liberty affiliates participating in the Cash Management Plan.

- b. Please explain why provision (J) of the existing Mountain ring-fencing provisions is not included in Liberty's proposed ring-fencing requirements. The existing provision (J) requires Mountain, if it wants to change its current cash management agreement with Park, to incorporate best practices for protecting Mountain's credit from the risks of such an agreement and to provide the Commission with 30 days' advance notice of any changes.

**Response:** Liberty anticipated disclosing its cash management system for the Commission's review in this docket. Liberty is willing to accept a requirement in the final order that it provide the Commission 30 days' advance notice of material changes to Liberty's current cash management system if the system is approved in this proceeding.

PSC-019

Regarding: Merger Agreement

Witness: Unknown

- a. Does the acronym “CIP” in the Agreement refer to Carlyle Infrastructure Partners?

**Response:** Yes, see §8.5(a) of the Merger Agreement.

- b. Provide the “Class A Joinder Agreement, pursuant to which CIP has agreed ... to provide certain indemnification obligations ...”

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- c. List all of the Transaction Documents referred to on p. 15 of the Agreement.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-020

Regarding: Due Diligence

Witness: Unknown

- a. Please provide the names, contact information, qualifications of representative, dates and locations physically reviewed by representatives of Liberty Utilities that physically visited the facilities of Park, Apple Valley and Mountain Water.

**Response:**

Matthew Garlick, Director of Operations (AZ/TX), Liberty Utilities: visited Park Water on August 5-6, 2014; visited Apple Valley on August 19, 2014; visited Mountain Water on September 1-3, 2014.

Brian Hamrick, Senior Project Manager, Liberty Utilities: visited Park Water on August 5-6, 2014; visited Apple Valley on August 19, 2014; visited Mountain Water on September 1-3, 2014.

Greg Sorensen, President, Liberty Utilities: visited Park Water on August 5-6, 2014; visited Apple Valley on August 19, 2014.

Other company representatives attended business meetings with Carlyle/Park on August 5-6 in Los Angeles but did not perform on-site visits with the express purpose of physically reviewing the three operations prior to the announcement of the transaction.

- b. Please provide all documents, presentations, notes and reports, written and electronic that were generated as a result of those visits.

**Response:** Liberty objects to this request because it seeks information which is not relevant to this matter and is protected from disclosure as confidential and contains proprietary trade secrets. Liberty's due diligence work papers are not relevant because they have no impact on Mountain Water's consumers. The documents are not tied to the service consumers will receive, the operations of Mountain Water, or the rates consumers will pay. Moreover, Liberty's internal valuation will not affect Mountain Water's rates or the level of service, as stated in Liberty's application because Liberty does not intend to seek an acquisition adjustment to the existing rate base. Regardless of these considerations, all future rate changes will be subject to the Commission's review and approval. Accordingly, this request seeks information that has no bearing on the Commission's decision in this matter, and as such seeks information that is irrelevant and not reasonably calculated to lead to the discovery of admissible information.

The requested information is also protected from disclosure because it is proprietary and contains confidential trade secrets. Liberty's due diligence efforts, including any

financial analyses of potential investments, are based upon years of research and investment at a substantial cost to Liberty Utilities. The underlying financial and other analyses and overall bid strategy and methodologies that Liberty implements in responding to solicitations relating to the sale of regulated utilities are proprietary and contain confidential trade secrets. Moreover, compelling winning bidders to disclose their successful strategy will necessarily have a chilling effect on the participation in the market of future offerings of utility assets. Disclosure of such information, even under seal, would be harmful to the business interests of Liberty, because both its seller and the City are parties who could obtain these materials, and the Commission cannot provide certainty that information produced, even under protective order, would not be subject to disclosure on challenge by a party or outside interested party.

PSC-021

Regarding: Plan and Agreement Merger Pg. 22 4.17 Labor and Employment Matters

Witness: unknown

- a. Please list all unfair labor practice complaints and a brief summary and disposition of those complaints for all regulated utilities of Liberty Utilities for the last 5 years. Identification of the affected employee(s) is not necessary and can be redacted.

**Response:** In 2014, an Arkansas employee of Liberty filed an EEOC discrimination claim in Arkansas, alleging violations of Title VII of the Civil Rights Act and the Americans with Disabilities Act. The parties reached an agreement in mediation and the claim was dismissed without any action against Liberty.

- b. Please do the same for Western Water Works and its direct and indirect subsidiaries.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-022

Regarding: Schedule 4.3(a)

Witness: Unknown

- a. Please provide copies of documentation referred to in 4.3(a) 4.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- b. Is the ownership interest in Park Water pledged to BNY Western Trust Company as well? Please explain.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-023

Regarding: Schedule 4.7(a)

Witness: Unknown

Please provide a list of costs expensed by MWC in this litigation.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-024

Regarding: Schedule 4.11

Witness: Unknown

- a. Please provide copies of documents referred to in 4.11 (iii) 1, 2, 3, 4

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- b. Please provide copies of documents referred to in 4.11 (iv) 1

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- c. Please provide copies of documents referred to in 4.11 (iv) 3 with regard to Decision No. 11-12-007 of the PUC of California.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- d. Please provide copies of documents referred to in 4.11(x) 5 and 7.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-025

Regarding: Schedule 4.11

Witness: Unknown

Please explain what is a provisional permit as referred to on page 48 of 64.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-026

Regarding: Schedule 4.19

Witness: Unknown

- a. What is the status of the property tax situation as referred to in number 1?

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- b. Have the tax returns referred to in number 2 been filed? Please supply copies of the Federal and Montana returns.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- c. Was there a gain or loss on the sale of Santa Paula Water Works, Ltd.? If so, what was that gain or loss?

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- d. Are the assets and liabilities of Santa Paula allocated to any of the subsidiaries or operating divisions of Park Water? Please explain.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

PSC-027

Regarding: Due Diligence

Witness: Unknown

- a. Please provide copies of all correspondence, presentations, minutes of meetings, and phone logs, electronic or paper, between Carlyle Infrastructure Partnership and Western Water discussing the sale of Western Water to Liberty Utilities. If there are video or audio recordings please provide those as well.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- b. Was Carlyle Infrastructure Partnership or Western Water approached first regarding the sale of Western Water? What company made the initial contact, Liberty Utilities or Algonquin?

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- c. Please provide copies of correspondence, presentations, minutes of meetings and phone logs, electronic or paper, regarding the initial contact for the sale and purchase of Western Water. If there are video or audio recordings please provide those as well.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- d. If there was a solicitation of bids for the purchase of Western Water, please provide the solicitation letter and names of companies providing proposals.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

- e. If there is an answer other than not applicable to (d) above, please provide the details of the other bids including worksheets supplied by the bidder, and supporting documentation as to why they were not chosen.

**Response:** Liberty understands WWH and MWC are providing the response to this request in their separate responses.

CERTIFICATE OF SERVICE

I hereby certify that on February 17, 2015, the foregoing Liberty Utilities Co. and Liberty WWH, Inc.'s Responses to Data Requests PSC-001 through PSC-027 was served via electronic and U.S. mail on:

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