S 1323: CURTAILING PUC EXPANSION OF REGULATORY CONTROL OVER IDAHO'S SMALL WATER COMPANIES

Key Takeaways:

- The PUC is investigating the regulated status of over 100 small water companies in Idaho.
- S 1323 simply codifies case law (and PUC guidance) and clarifies definitions.
- The PUC is concerned about S 1323 as it could limit its jurisdictional expansion plans.
- PUC regulation will drive rates up and drive small water delivery entities into the arms of the large multi-national water suppliers.

RESPONSE TO PUBLIC UTILITIES COMMISSION'S "ANALYSIS" OF S 1323

For years, water providers in Idaho have been relying on long-established Idaho law as described in the Idaho Public Utilities Commission's ("PUC") guidance[1] posted on the PUC's website as part of the PUC's "Water Company Information Packet." That guidance expressly states that providers serving only one customer are not regulated public utilities. The PUC now seemingly seeks to disavow that long-held position. S 1323 simply seeks to codify the existing guidance, which clarifies the meaning of the underlying statute and is consistent with settled Idaho Supreme Court precedent. The "single entity" exception embodied in S 1323—which the PUC now attacks—is not new. This bill makes it clear that under Section 61-125 of the Idaho Code providing water to only one customer does not create a public utility. This rule has been recognized since the Supreme Court's 1924 decision in *Humbird Lumber Co. v. PUC*, 39

[1] *See* PUC, *"Types of Water Utilities and who regulates them,"* https://puc.idaho.gov/FileRoom/PublicFiles/water/swc/SWC%20Types%20of%20Water%20utilities.pdf. The document is still available to the public and the regulated community on the PUC's website, though it has recently been relegated from its previous, prominent location within the Commission's "Water Company Information Packet" to an obscure "FileRoom" domain.

Idaho 505, 228 P. 271, 273 (1924) ("The furnishing of water to one person or corporation, under a contract, does not constitute a delivery of water to the public"). But now the PUC is attempting to abandon the "single entity" rule established by the Supreme Court nearly a century ago. **This approach appears to be a part of the PUC's strategy to vastly expand the number of water providers it regulates—launching investigations into the regulated status of over 100 water suppliers across the state.** In any case, the PUC's analysis of S 1323 is incorrect with respect to the current state of the law as well as what the bill's proposed amendments would do.

Section 61-104

S 1323 proposes to amend Section 61-104 to add to the list of exempt entities the very same entities identified by the PUC in its Water Companies Information Packet guidance document—homeowners associations ("HOA"), cooperative associations, and formal water districts. These entities were included in the amendment to ensure that they remain exempt. Even though the PUC expressly identified these entities as exempt, the PUC now questions whether the law should recognize an exemption for the very same entities that the PUC has historically identified as exempt to the public. It is unclear from the PUC's memo if the PUC is now claiming that these entities are now subject to PUC regulation.

First, however, the PUC admits that an HOA is exempt from regulation as a public utility, and it does not take issue with S 1323's addition of "homeowners association" to Section 61-104. However, the PUC takes issue with adding "cooperative association" and "formal water district" to the Section 61-104 exemption, even though the PUC identified these entities as exempt in its guidance.

S 1323 proposes adding "cooperative associations" to the exemption in Section 61-104 to better clarify that *any* form of cooperative association—not just a "cooperative corporation," as the PUC argues—is exempt as a non-profit organization. The PUC claims that adding "cooperative association" is redundant. But the definitions it cites are from entirely different provisions of the Code that are not part of the Title governing the PUC. Significantly, one of the statutes that the PUC cites refers to cooperative *corporations*—not cooperative *associations*. Idaho Code § 30-30-103(6). Corporations and associations are simply not the same kind of legal entity. The second statute the PUC cites relates only to electric and gas cooperative associations, and that statute does not reference water associations. Idaho Code § 63-3501. This is not redundancy but added clarity. In any event the PUC does not contend that cooperative associations are now regulated or should be regulated.

The PUC claims that "formal water district" needs more clarification, asserting that they don't know what a "formal" water district is, even though the language in S 1323 came directly from the PUC. Obviously, a formal water district would be one formed under Idaho law. The PUC cites one such type of district by reference to IDWR's website—those formed by IDWR under Title 42, Chapter 6 of the Idaho Code ("Distribution of Water Among Appropriators"). There are also "water districts" as defined under Chapter 32 of Title 42 ("Water and Sewer Districts"), and they also are currently not subject to PUC regulation. The text of Section 61-104 referring to formal water districts helps make it clear that any formally created water district remains exempt.

Section 61-125: "Profit" and "Compensation"

The proposed amendment to IC 61-125 is necessary to align Section 61-125 with Section 61-104 and clarify the scope of the PUC's jurisdiction. As written, Section 61-125's reference to

"compensation" could be read by an overzealous regulator to conflict with or override the "not for profit" exemption in Section 61-104. This exemption includes any utility not organized or operated for profit, but Section 61-125's reference to "compensation" might be read to include entities that receive payment for the water they provide, regardless of whether they operate for profit. The proposed change would align the 61-104 exemption for entities that are not organized or operated for profit with Section 61-125's definition of "water corporation"; it would not change the exemption. Indeed, the PUC acknowledges (for now) that receiving compensation for delivery of water does not make an entity that is organized and operated at cost and not for profit into a regulated public utility. Thus, this clarification would not open the door for "corporate gamesmanship" as the PUC argues. The PUC cites seventeen regulated water companies and acknowledges that ten of them are operating at a loss. This admission begs the question of why the PUC finds it necessary to regulate as many water companies as it does now, much less dozens more.[2] If the vast majority of these entities are not operating at a profit, it is hard to imagine how they would be charging exorbitant rates.

Section 61-125: "Single Entity" Exemption

The proposed amendment to Section 61-125 to codify the long-standing single entity rule draws most of the PUC's ire. That ire is misplaced. If the PUC wants to regulate deliveries by contract to a single entity, it is the PUC which should propose legislation to give it that authority – authority it hasn't had for nearly 100 years. Of course, the PUC's own guidance admits that it doesn't regulate delivery to a single entity.

[2] It is worth noting that while the PUC states that it only regulates seventeen water corporations, the PUC is in fact currently investigating over 100 additional entities in an apparent attempt to vastly increase the number of regulated water utilities.

- PUC Guidance: The PUC contradicts its own longstanding guidance by claiming that a "single entity" exemption is not consistent with Idaho Code. It is ironic that the PUC attempts to distance itself from its own guidance here, given that it cites the Idaho Department of Water Resources' FAQ page (an agency guidance document) in its attempted attack on the proposed amendments' use of the phrase "formal water district." Agency guidance is routinely relied on by the public and the regulated community. *See F.C.C. v. Fox*, 556 U.S. 502, 515 (2009) (agencies must justify a new policy when a prior policy has "engendered serious reliance interests"). Water providers have been justified in relying on the PUC's posted guidance telling them what it takes to be a regulated water utility. **That the PUC now tries to ignore its own guidance at the same time it is attempting to expand its jurisdictional turf should raise an eyebrow.**
- Supreme Court Precedent: In *Humbird*, the Idaho Supreme Court held that a lumber company that supplied water to just one customer—a railroad—was not a "public utility" subject to regulation because the water provider did not serve the public. *Id.* at 273. Contrary to the PUC's arguments against S 1323, *Humbird*'s "one customer" rule remains good law and is consistent with the PUC's own guidance that water systems serving no more than one customer are not subject to regulation. The PUC attempts to overrule *Humbird*'s "one customer" exemption by relying on a misapplication of the Court's ruling in *Verska v. Saint Alphonsus Reg'l Med. Ctr.*, 151 Idaho 889, 265 P.3d 502 (2011), to *Stoehr v. Natatorium Co.*, 34 Idaho 217, 200 P. 132 (1921), a case cited by *Humbird*. The PUC argues that *Verska* prohibits the type of statutory interpretation the *Stoehr* court performed. But this argument fails for one simple reason: *Verska*'s holding does not affect

the Court's holding in *Stoehr* or *Humbird* in any way.[3] As the PUC admits, *Verska* held that a court cannot ignore the "literal words of a statute" and that "where statutory language is unambiguous," the text must control. *Verska* at 505–06. But the Court in *Stoehr* was not interpreting an "unambiguous" statute: Idaho's Public Utilities Law (then, as now) states that a public utility is one that serves the public. Idaho Code § 61-129. The PUC statutes don't define the term "public." See Idaho Code § 61-129. Therefore, the interpretation of what it means to deliver water to the public is ambiguous when applied to a single customer. The Supreme Court did not ignore the literal words of the statute, but instead interpreted the statute, as is the Court's duty. This leaves the question of whether an organization that only provides water to one customer is delivering to the "public" ripe for judicial determination. *Humbird* did just that. *Humbird* at 273 ("The furnishing of water to one person or corporation, under a contract, does not constitute delivery of water to the public or some portion thereof."). *Stoehr* reached a similar conclusion—determining that merely furnishing water on contract was not enough, standing alone, to turn a private use "public." *Stoehr* at 218. The PUC acknowledged this rule in *Re Kootenai Heights Water System, Inc.* Case No. KHW-W-05-01, 2007 WL 1467299 (Idaho P.U.C. 2007). In that decision, the PUC recognized that *Humbird* required "examining primary purpose for operation and **requiring more than one customer".** The "single entity" exemption proposed by S 1323 directly agrees with the Supreme Court's clear, and undisturbed, holdings in *Humbird* and *Stoehr,* as the PUC admitted in *Re Kootenai Heights Water System, Inc.* Case No. KHW-W-05-01

[3] The PUC is an administrative agency, not a judicial or legislative body, and its attempts to undercut or override the Supreme Court's decisions in *Humbird* and *Stoehr* do not affect the validity of the Supreme Court's holdings, though they do belie the PUC's agenda. In any event the PUC does not have the power or authority to nullify a Supreme Court decision.

- Section 61-129: The PUC's arguments regarding Section 61-129 are circular and self-defeating. If the PUC's interpretation were correct, the exemption for non-profit organizations in Section 61-104 would be entirely undone. The PUC argues that if a corporation is involved in any way with the provision of water, that water will be subject to the PUC's regulatory authority. If this were true, a non-profit entity (including any entity enumerated in Section 61-104) would be unable to provide water without being subject to PUC regulation. This clearly conflicts with Section 61-104. **The proposed addition of an express "single entity" exception does not cut off any regulatory authority the PUC actually possesses under the statute as it stands.** Indeed, S 1323 harmonizes the language of Section 61-129 by recognizing that the single entity exemption only applies when the delivery is to an entity that is otherwise exempt, like an HOA or other non-profit. It does not leave the gaping hole that the PUC implies, because the HOA or non-profit is not otherwise subject to the PUC regulation as matters now stand.
- "Harm and Exploitation": The PUC draws out a parade of horribles based on a faulty understanding of what the "single entity" exception would do. The PUC warns that under the proposed amendments, if a water corporation charged a single entity such as an HOA, for water, then this service would be stripped of regulatory oversight. However, the exemption for entities like HOAs (which the PUC does not take issue with) makes sense precisely because the PUC's regulatory oversight is unnecessary when a non-profit entity like an HOA is providing water. The provision of "fair and reasonable rates" is ensured by the HOA's (or similar entity's) power to contract with the water corporation. It is worth noting, however, that the PUC's hypothetical wherein Veolia creates a subsidiary to

serve the City of Boise is totally imaginary. Veolia itself already contracts with customers, not the City of Boise. If Boise were to provide water service, it would be exempt from regulation under Section 61-104 as a municipal corporation.

"Example Scenario":

The PUC's attempt to argue that homebuilder control of an HOA while the development is still being built is somehow unacceptable falls flat. First, it is untrue that homeowners in such a scenario are unprotected: HOA boards owe fiduciary duties to their associations, and Idaho Code Title 55, Chapter 32 sets out comprehensive requirements for HOA boards to follow. Second, if the PUC disagrees with the concept of developers holding seats on HOAs, its fight is not with S 1323 but with Idaho HOA law, which does not prohibit homebuilders who own property from sitting on HOA boards.[4] The PUC doesn't suggest changing Idaho HOA law but still seems intent on regulating HOAs. Most significantly, the PUC has no basis for concluding that the market will not ensure that rates remain competitive. The PUC cites not a single instance of a water company "gouging" or charging "any rate it wants." Nor would the free market reward any company who acted as the PUC theorizes. ***In fact, experience shows that PUC regulation will drive rates up and drive small water delivery entities into the arms of the large multi-national water suppliers.***

[4] H 657, which would have undercut this ability, is currently stalled in committee.