

NM PUBLIC
REGULATION
COMMISSION

BEFORE THE NEW MEXICO PUBLIC REGULATION COMMISSION

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**In the Matter of a Petition by
New Mexico Water Service Company for
a Declaratory Order**

Utility Case No. 08- 00177-UT

BRIEF IN SUPPORT OF PETITION FOR DECLARATORY ORDER

New Mexico Water Service Company ("NMWSC") hereby submits this Brief in Support of its Petition for Declaratory Order ("Petition") to address the meaning and intent of the Final Order entered by the Commission on May 23, 2006 in Case No. 05-00208 UT and Case No. 05-00305 UT consolidated ("Order") with regard to the ability of NMWSC to fully utilize the water rights held by NMWSC as utility property for use within its service area. NMWSC incorporates herein by reference the entirety of the Petition.

The issue before the Commission in Case No. 05-00208 with regard to water rights was limited solely to whether, in the context of NMWSC's acquisition of Independent Utility Company ("IUC"), the Commission should approve the severance of some of the water rights from utility ownership and control to be held by a non-regulated entity after the acquisition and sold back to the NMWSC under certain terms and conditions. The Commission found this approach was not acceptable and was inconsistent with previous Commission policy and precedent. The Commission approved the acquisition of IUC by NMWSC but required all of the utility water rights to remain with the utility and pass as utility property to NMWSC. The Commission did not find that once the acquisition occurred, NMWSC had to utilize the water rights only for the benefit of specified customers within a limited part of its service area. The facts and law do not support such an interpretation of the Commission's Order. Moreover, such

an interpretation would preclude NMWSC from expanding and improving its service and infrastructure for the benefit of existing customers.

I. The Commission determined that the water rights should pass with the utility and did not determine that those water rights would be perpetually restricted to a limited part of NMWSC's service area.

The issue posed to the Commission in the context of Utility Case No. 05-00208 was whether the Commission should approve, in the context of a utility acquisition, the severance of a utility asset, i.e. the water rights, from the utility and the retention of the water rights by a non-regulated entity for later sale to NMWSC, the new utility owner. The Commission determined that such severance was not appropriate and conflicted with Commission policy and precedent. The Commission ordered that the water rights remain with the utility to be utilized by the utility in its service area. The Commission did not limit the water rights to any particular part of the service area, the Sandia Knolls subdivision or otherwise. Rather, NMWSC holds the entirety of the water rights as a utility asset for use within the entirety of its service area. The utilization of the water rights is, of course, subject to the requirement that NMWSC ensure that all existing customers continue to receive adequate and reliable utility service, including a sufficient water supply. NMWSC will meet this obligation but that is a different matter from whether in the context of an acquisition the Commission can place restrictions on utility assets that did not otherwise exist.

To read the Commission's Order as placing restrictions on the water rights under NMWSC ownership would mean that the Commission placed additional restrictions on NMWSC's ownership which did not exist at the time of IUC ownership. Prior to the acquisition IUC, without prior Commission authorization, could expand its infrastructure to serve contiguous areas within its service area. Accordingly, in the context of the acquisition, the

Commission, consistent with its authority, could not have placed new or additional restrictions on the utility water rights that did not previously exist. Rather, the intent of the Commission was to maintain the status quo – i.e. the water rights were utility property to be held in their entirety by the utility and utilized within the utility’s service area. The plain language of the Commission’s Order indicates this was the meaning and intent of the Order which is consistent with Commission policy and precedent, with the service area and service obligations of NMWSC, and with the State Engineer permitted place of use for the water rights.

- A. The plain language of the Final Order and Recommended Decision and Commission policy makes clear that the Commission did not intend to restrict the use of the water rights to specific customers within a limited part of NMWSC service territory.**

In its Final Order the Commission rejected the request to sever water rights from the utility and the water rights passed with the utility for NMWSC to service existing and future customers. The plain language of the Order indicates this was the Commission’s intent. For example, the Recommended Decision provides that “The Commission finds that all water rights became dedicated to public service at the time the State Engineer declared them for the use of the water utility and they shall remain with the utility.” Recommended Decision at 56. This language demonstrates that the water rights were to transfer with the utility and the only limitation was that the water rights would be “dedicated to public service.” Use of the water rights to serve all areas of NMWSC service area inclusive of service of new customers is consistent with and was contemplated by the Order and is consistent with how the water rights could be and were used prior to the acquisition.

The Commission also found that “[t]he public convenience and necessity requires or will require the operation of IUC’s water facilities, including 340¹ acre-feet of water rights and systems by New Mexico Water.” Recommended Decision at 59. The language approving the acquisition and the transfer of the water rights, while rejecting the proposal that some of the water rights be severed from the utility under a “surplus” determination dictated by the Asset Purchase and Sale Agreement, only required the utility itself continue to hold those water rights for public service. Indeed, this is consistent with the manner in which the Commission regulates all water utilities – water rights are held by the utility to be utilized in the course of serving both existing and new customers based on an assessment by the utility as to how to manage its water supply and otherwise fulfill its utility obligations. The “surplus” determination in Case No. 05-00208 related solely to whether water rights could be severed from the utility. The Commission determined the water rights should not be severed and that they should remain a utility asset thereby allowing the utility, for planning purposes, to assess and meet obligations within its service territory. The Commission could not have intended to treat NMWSC differently than other similarly situated utilities in this regard. NMWSC as the holder of the water rights as a utility asset, is then tasked with the exercise of its managerial discretion to utilize that asset in a manner which fulfills all its utility obligations.

As noted in its Order, the Commission’s policy “in sale and acquisition cases is that water rights should remain with the utility to serve the utility’s customers.” Recommended Decision at 55. Significantly, the policy is that water rights be held by the utility for utility purposes – not that they be restricted to any particular place within a utility’s service territory. Indeed, the extension of the Commission’s policy to limit the use of water rights to any particular class of

¹ The 340 acre-feet represents the 325 acre-feet held under New Mexico State Engineer Permit S-1 and 15 acre-feet held under State Engineer Permit No. E-4728.

customers within a utility service area would impermissibly create a preferred customer class. The underpinning of the Commission's policy and precedent regarding requiring all water rights to remain under utility ownership is to ensure they are held by the utility to provide for sufficient and adequate service within all of a utility service area, not any particular portion of that area. *See, e.g.*, NMPRC Utility Case No. 2634, 1996 WL 594009 at *16-17; NMPRC Utility Case No. 2494, 1991 WL 694685, at *4-5.

The determination of "surplus" water rights in Case No. 05-00208 UT and Case No. 05-00305 UT consolidated, related only to the assessment of whether water rights could be severed from the utility as proposed by the Asset Purchase and Sale Agreement, not whether the entirety of the water rights asset, if held by the utility, should be limited to use within one part of its service territory. Accordingly, the Commission's Final Order could not, and did not, include any determination that the water rights transferred to NMWSC as a utility asset are somehow limited to only a portion of NMWSC service area. Such an interpretation of the Commission's Order not only would be inconsistent with the plain language of the Order and Commission policy, but it would conflict with NMWSC's extant service area and its obligations to serve therein as well as the permitted place of use of the water rights as regulated by the New Mexico State Engineer.

B. NMWSC's service area includes areas outside of and contiguous to Sandia Knolls and the Order intended the water rights pass with the utility for service within the entirety of its service area.

NMWSC, like most other water and wastewater utilities regulated by the Commission, operates pursuant to a plant, lines and system Certificate of Convenience and Necessity. Its service area thus includes all contiguous areas and all areas within a half mile of NMWSC facilities not served by another utility. *See* NMSA 1978, § 62-9-1; *Dona Ana Mutual Domestic Water Consumers Assoc. v. NMPRC*, 2006 NMSC 32, *14, *18. Indeed, NMWSC is obligated

to serve customers within its service area which includes areas subject to existing service as well as contiguous areas. *Id.*

In the operation of the former IUC system, NMWSC is currently serving customers within the Sandia Knolls subdivision and in areas contiguous to the Sandia Knolls system. *See* Affidavit of Paul Risso, ¶ 12. These customers are served consistent with the terms of New Mexico State Engineer permit S-1 et al. which provides for a place of use that includes Sandia Knolls and several hundred acres of surrounding areas, including a portion of Campbell Ranch. *Id.* ¶ 13. The entirety of Campbell Ranch, Phase I is within NMWSC's service as it is contiguous to the area in which NMWSC is currently serving customers and is within one half mile of NMWSC's existing infrastructure. *Id.* ¶ 14.

Accordingly, to interpret the Commission's Order to limit NMWSC's use of the water rights only to the Sandia Knolls subdivision would preclude NMWSC from serving existing customers and other customers within its established service territory. The utility's service area is much broader than Sandia Knolls and the Commission's Order could not have intended to limit the water rights to use only within a limited area of the service area. NMWSC must have the ability to fully utilize its utility property – in this case the water rights which the Commission directed should pass in their entirety to NMWSC as the new owner and operator of the utility. To interpret the Commission's Order otherwise would undermine the ability and obligations of NMWSC to serve within its service area.

Indeed, NMWSC is utilizing its managerial discretion to utilize the water rights in a way that will ensure significant benefit to existing customers. Although NMWSC has implemented significant improvements since acquiring IUC, the existing system requires additional improvements which would necessitate rate increases (perhaps as much as 25-30%) for existing

customers. Affidavit of Paul D. Risso, ¶ 11. The expansion of the system to serve Phase I, will provide significant benefits to existing customers as it will provide for an additional well allowing for redundancy of supply, much needed 1.5 million gallons of storage, provide the initial basis for upgrading the backbone of the existing system and fire hydrants within Sandia Knolls. Affidavit of Paul Risso, ¶ 15. The developer of Phase I would construct this necessary infrastructure and system improvements all at no cost to NMWSC utility or existing customers and obviate the need for a rate increase based on these improvements.

C. The Commission acknowledged that the New Mexico Office of the State Engineer is the proper arbiter of the determination of the place of use of water rights permitted by the State Engineer and the permitted place of use for the water rights is not limited to Sandia Knolls

As the Commission acknowledged, it is the New Mexico State Engineer, and not the Commission which ultimately determines the place of use of the water rights of a utility. *See, e.g.,* Order at 53 (“The amount of IUC’s current water rights was not a determination made by the Commission but rather by the State Engineer on application of IUC.”); *see also* NMSA, 1978 §72-2-1 (State Engineer shall have general supervisory authority over the waters of the state). The law is clear, it is the State Engineer which determines the place of use of water rights. *See, e.g.,* NMSA 1978, § 72-12-3 (A)(6). In this case, the existing place of use for the water rights in question is not limited to Sandia Knolls subdivision, (where only the well is located) but rather includes several hundred acres of surrounding areas including a portion of the area known as Campbell Ranch. *See* Affidavit of Paul Risso, ¶ 13; Exhibit B (permits for the water rights describing place of use). As noted, NMWSC is currently serving customers both within and in the area surrounding Sandia Knolls. Moreover, as evinced by the attached Exhibit B, the water rights are also permitted to be utilized in non-contiguous areas. In 1997/1998, the State Engineer granted transfer of a portion of the water rights (99 acre-feet) to a subdivision of over 2,000 acres

commonly referred to as Loma Ponderosa.² Thus, the State Engineer has already recognized the right of the utility to utilize the water rights not only outside of Sandia Knolls subdivision but outside the original permitted place of use and in non-contiguous areas.

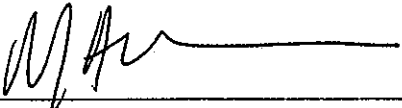
To the extent NMWSC's utility service area is not entirely coincident with the State Engineer currently permitted place of use for the water rights, NMWSC will apply to the State Engineer to expand the place of use of the water rights in order to maintain consistency between NMWSC's utility rights and obligations and its rights of use with regard to its utility water rights. To interpret the Commission's Order as limiting NMWSC's use of the water rights to Sandia Knolls would conflict with existing State Engineer permits and the Commission's own decision which appropriately direct that the State Engineer determines the place of use of water rights.

CONCLUSION

The Commission should address its Final Order in Case No. 05-00208 UT and Case No. 05-00305 consolidated, and issue an order which confirms that consistent with applicable law, policy and precedent the Commission did not place a new restriction on NMWSC to limit the use of utility water rights to only specified customers within its service area and that NMWSC may utilize its utility water rights to fulfill its obligations to serve existing and future customers within the entirety of its service area including Phase I of Campbell Ranch.

² NMWSC does not intend to provide utility service to the Loma Ponderosa subdivision which was never developed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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