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UTILITIES COMMISSION

Chas. F. McDevitt
Dean J. (Joe) Miller

July 31, 2008

VIA HAND DELIVERY

Jean Jewell, Secretary
Idaho Public Utilities Commission
472 W. Washington St.
Boise, Idaho 83720

Re: UWI-W-08-01

Dear Ms. Jewell:

Enclosed for filing in the above matter, please find the original and seven (7) copies of United Water's Reply to Petition for Clarification and Motion for Order of Dismissal Based on the Pleadings.

An additional copy of the documents and this letter is included for return to me with your file stamp thereon.

Very Truly Yours,

McDevitt & Miller LLP



Dean J. Miller

DJM/hh
Encls.

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Attorneys for United Water Idaho Inc.

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

McKAY CONSTRUCTION CO., INC.,
COMPLAINANT
and
SCHMIDT CONSTRUCTION CO., INC.,
COMPLAINANT
vs.
UNITED WATER IDAHO INC.
RESPONDENT

Case No. UWI-W-08-01

**REPLY TO PETITION FOR
CLARIFICATION and MOTION
FOR ORDER OF DISMISSAL
BASED ON THE PLEADINGS**

COMES NOW United Water Idaho Inc., ("United Water") and Responds to the Petition for Clarification by Complainants dated July 21, 2008, ("Petition") as follows, to wit:

In their Petition, McKay and Schmidt advance arguments which can be fairly summarized as follows:

- McKay & Schmidt are qualified to perform water line construction;
- Costs of training and monitoring contractors should be assigned to contractors or projects (developers) through an application fee or other form of direct charge;

REPLY TO PETITION FOR CLARIFICATION and MOTION FOR ORDER OF DISMISSAL BASED ON THE PLEADINGS-1

- Because administration of the *labor in lieu* program has rate impacts to retail customers, the Commission should not defer to United Water's business judgment.

In this Reply, United Water addresses each argument, in turn.

McKay & Schmidt Qualifications

United Water does not dispute McKay and Schmidt's qualifications as set forth in the Petition (pgs. 3—4). Individual qualifications, however, are not the issue in this case. At issue is the reasonableness of a generic policy capping the size of the qualified contractor pool, applied to all contractors in a non-discriminatory way. For the reasons set forth in United Water's Statement of Position, the policy is the result of a reasonable exercise of business judgment.

McKay points to a letter from United Water indicating that if McKay met the minimum insurance requirements it could be re-instated to the approved contractor list. (Petition Pg. 3). It should be noted, however, that letter was written in the year 2005. McKay, over more than a two year period, did not, to United Water's knowledge, take any steps to up-grade its insurance and there is certainly no evidence that McKay in any way relied to its detriment on the 2005 letter. Additionally, it is unreasonable to expect that United Water intended the statements in a 2005 letter to live in perpetuity, regardless of changes in circumstances.

McKay and Schmidt attach to their Petition letters from developers claiming there is demand for McKay and Schmidt's services. To United Water's knowledge, none of the letter authors have complained either to the Company or to the Commission that the supply of contractors was inadequate. In fact, none of the letter authors to date have contacted United Water regarding any upcoming main line extensions for service within United Water's

certificated service territory. The letters, prepared after litigation was commenced, appear self-serving.

Direct Charge

The Petition argues that United Water should develop an application fee or other direct charge to contractors or projects (developers) to recover costs that are not directly charged to specific projects. (Petition Pgs 5—7).

In theory this sounds simple, however it would involve the additional effort of creating a system for quantifying costs and devising a method, which currently does not exist, of allocating costs between new applicants, newly approved contractors, and those already in the pool. The Company's efforts to review applications of unsuccessful contractors would in theory be chargeable (and hopefully collectible) from contractors who would be doing no work for United Water. Newly approved contractors may or may not actually win any bids to perform on projects against which review costs could be charged, as suggested in the Petition. Should a newly approved contractor actually perform on one or more projects, the training and oversight required could extend over some time and over various projects, further complicating the tracking, charging and managing of these costs. United Water would also have to develop a method to charge contractors or projects the cost of the Company's annual review of all contractors' performance. These costs are typically incurred at the end of the year long after most projects are closed. The Company would then have to contend with the inevitable protests from contractors or developers who receive these charges. Because, as previously stated, United Water does not currently have a system and method in place to quantify and allocate these costs, a period of time, possibly a full year, would be required to accumulate actual cost data in order to be able to accurately charge developers a rate for these services. United Water is left to wonder

how it should set charges in the near term without any historical or other basis on which to establish those charges.

This, again, illustrates the wisdom of allowing company managers a certain level of discretion in the operation of its business. United Water chose a cap rather than a fee because the cap has the advantages of simplicity of administration, even-handed and non-discriminatory application, avoidance of individual cost allocations, and potential disputes. Contrary to the repeated, but unsupported, assertions in the Petition the decision to choose a cap rather than a fee was not arbitrary.

As explained in the Statement of Position, there was a factual basis for United Water's conclusion that a pool of ten contractors is adequate to provide a choice of suppliers to developers at competitive prices. Attached hereto is Exhibit A which accompanied United Water's Statement of Position. It illustrates that developers are, in fact, choosing from multiple contractors and there are a sufficient number of contractors to meet developer demands. United Water has not received from any developer a complaint that the number of contractors is inadequate. Additionally, as is well known, the residential construction market is currently experiencing a marked downturn compared to the years 2005 and 2006, as is also illustrated by Exhibit A. In 2008, as of April 30, the number of developer projects was 15, down from 80 and 83 in 2005 and 2006, respectively. As of the date of this Reply, the number of projects in various states of construction is 19, an increase of only 4 since April, indicating that new development construction in United Water's service area has almost completely stalled. Thus, for the foreseeable future, the level of demand for contractors from developers is likely to be significantly less than in years when a pool of ten contractors was adequate to meet demand.

The Petition's repeated characterization of the decision to cap the qualified contractor pool as "arbitrary" is unfounded. In fact, as demonstrated above, and in United Water's Statement of Position, the decision was based on a reasoned analysis of market conditions. A management decision supported by a factual basis is not arbitrary.

Scope of Business Judgment Deference

Contrary to the characterization in the Petition (Pg.6), it is not United Water's position that review of the decision to cap the contractor pool is outside the Commission's jurisdiction. Rather, United Water believes this is an area in which the Commission, in the exercise of its discretion, may appropriately defer to United Water's business judgment. This is based on the fundamental premise the public utility commissions do not operate the businesses they regulate. As the Commission recently said with respect to another water company:

It is not the Commission's intent to micro-manage the operating expenditures of Ponderosa. As the owner and operator of Ponderosa, Mr. Cobott shall use his own discretion to prudently allocate the funds generated by rates in a manner that benefits the ongoing operation of the Company. (*In The Matter of Ponderosa Terrace Estates Water Company*, Order No. 29086).

The Petition too narrowly defines the scope of Commission deference by asserting that in any matter having a possible effect on rates no deference is due¹. The Commission has not so narrowly construed the extent of its deference. For example, in Case No. UWI-W-96-7, Order No. 27616, the Commission deferred to the Company's decision to lease rather than own motor vehicles even where the decision had a direct impact on customer rates.

In a related argument the Petition asserts that United Water unfairly used its monopoly status to limit vendor access to its system thus justifying Commission intervention. In fact, of all the regulated utilities operating in southwest Idaho, United Water's policy on competitive

¹ Whether McKay and Schmidt have standing to serve as advocates for the general body of ratepayers is a question we leave unaddressed.

bidding is the most liberal. To United Water's knowledge, Idaho Power, Intermountain Gas and Qwest all employ sole source contractors and do not allow competitive bidding on developer projects at all.

Conclusion

As discussed herein, and in the Company's Statement of Position, the decision to cap the contractor pool at ten was based on a factual analysis of the current demand for and supply of contractor services. The decision was not arbitrary and was within the range of reasonable decisions available to management.

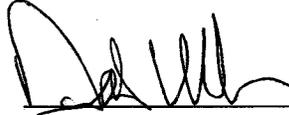
Accordingly, United Water respectfully moves the Commission for the entry of an Order dismissing the Complaints based on the pleadings and papers filed herein. By way of summary, United Water believes the Commission's Record for Decision would consist of the following:

- Letter Complaint of McKay Construction dated February 19, 2008;
- Letter Complaint of Schmidt Construction dated February 20, 2008;
- Commission Summons dated April 14, 2008;
- Answer of United Water dated May 6, 2008;
- United Water Statement of Position dated May 6, 2008;
- Reply of Schmidt Construction dated May 16, 2008;
- Reply of McKay Construction dated June 10, 2008.
- McKay and Schmidt Petition for Clarification dated July 23, 2008.
- The Reply and Motion incorporate herewith.

DATED this 7 day of July, 2008.

Respectfully submitted,

MCDEVITT & MILLER LLP



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Boise, ID 83702
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Counsel for United Water Idaho Inc.

CERTIFICATE OF SERVICE

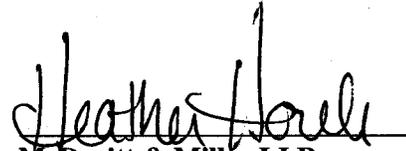
I hereby certify that on the 21st day of July, 2008, I caused to be served, via the method(s) indicated below, true and correct copies of the foregoing document, upon:

Jean Jewell, Secretary
Idaho Public Utilities Commission
472 West Washington Street
P.O. Box 83720
Boise, ID 83720-0074
jjewell@puc.state.id.us

Hand Delivered
U.S. Mail
Fax
Fed. Express
Email

Peter Richardson
Richardson O'Leary
515 N. 27th Street
Boise, ID 83702

Hand Delivered
U.S. Mail
Fax
Fed. Express
Email


McDevitt & Miller LLP

Contractor	# of Projects	Feet Installed	Project Totals
2004			
Contractor A	7	9160	\$340,184
Contractor B	1	2400	\$74,687
Contractor C	8	3715	\$292,558
Contractor D	20	33480	\$1,214,659
Contractor E	3	7255	\$254,040
Contractor F	14	16000	\$736,374
Contractor G	12	20929	\$754,218
Contractor H	4	33530	\$1,565,006
Contractor I	4	12435	\$441,607
2005			
Contractor A	5	16360	\$932,794
Contractor B	2	3255	\$181,280
Contractor C	10	8930	\$644,560
Contractor D	19	43079	\$1,783,491
Contractor E	25	27640	\$1,431,610
Contractor F	13	28800	\$1,178,624
Contractor G	2	4835	\$168,261
Contractor H	4	7775	\$314,765
2006			
Contractor A	6	8555	\$525,548
Contractor B	3	7445	\$383,509
Contractor C	8	7215	\$460,685
Contractor D	11	12960	\$756,813
Contractor E	17	44060	\$2,258,110
Contractor F	19	26255	\$1,690,135
Contractor G	9	24390	\$1,182,555
Contractor H	5	24780	\$1,292,892
Contractor I	2	11570	\$555,431
Contractor J	3	4030	\$325,144
2007			
Contractor A	5	4455	\$283,182
Contractor B	2	2765	\$207,488
Contractor C	5	2520	\$184,826
Contractor D	6	6165	\$385,754
Contractor E	18	62265	\$3,060,661
Contractor F	11	31230	\$2,133,433
Contractor G	9	14455	\$825,891
Contractor H	4	6815	\$340,365
Contractor I	3	5175	\$455,225
Contractor J	3	2355	\$267,649
2008			
Contractor A	1	2520	\$108,692
Contractor B	2	1760	\$98,919
Contractor C	0	0	\$0
Contractor D	1	890	\$37,653
Contractor E	2	810	\$44,757
Contractor F	2	2605	\$161,120
Contractor G	3	4875	\$276,454
Contractor H	3	15805	\$729,099
Contractor I	1	560	\$26,321
Contractor J	0	0	\$0