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EXHIBIT CAW - 34

Appendix B – Accounting Rules for Government Contamination Loan Funds

APPENDIX B

RULES FOR THE ACCOUNTING OF GOVERNMENT CONTAMINATION LOAN FUNDS

These rules shall apply to all transactions involving government contamination loan funds (Govt. Loan Funds).

1. All government contamination loan funds shall be repaid by ratepayer contributions through surcharges similar to the accounting method used by the Commission for loans from the Safe Drinking Water State Revolving Fund as set forth in Water Division's Standard Practice U-13-W and summarized in the example below:¹

Assumptions:

Total Loan Amount:	\$154,500
Loan Proceeds to the Utility:	\$150,000
Administrative Fee:	\$ 4,500 ²
Term of Loan:	15 years with semi-annual payments

- a) Utility receives loan proceeds from government. Proceeds are recorded both in a cash account and, if authorized by the Commission, in a memorandum account. Set up the administrative fee as a prepaid asset to be amortized over life of loan.

	<u>Debit</u>	<u>Credit</u>
Cash Account	\$150,000	
Other Deferred Charges	4,500	
Other Deferred Credit- Govt. Loan		\$154,500

¹ Specific USOA account numbers will vary by utility.

² Any administrative fees taken out of loan proceeds shall be amortized over the life of the loan with the unamortized amount charged to Account 146 Other Deferred (Debits) Charges and excluded from rate base. The same process shall be followed for any administrative fees paid up-front by a utility that was not taken out of loan proceeds except that such fees may be included in rate base.

- b) Plant is constructed with Government loan proceeds. Plant is to be depreciated over life of loan.

Plant in Service (Accounts 301-341) \$150,000³

Cash Account \$150,000

- c) Monthly billing of customers for ordinary revenue of \$4,000 plus Government loan surcharge of \$1,850 (\$9.25 surcharge x 200 customers = \$1,850).

Accounts Receivable - Customers \$ 5,850

Water Revenue \$ 4,000

Govt. Loan Contamination Proceeds 1,850

- d) Monthly collections of customer receivables from 188 customers. Consists of \$3,760 of regular revenue and \$1,739 of Government Loan surcharge revenue.

Cash Account \$ 5,850

Accounts Receivable - Customers⁴ \$ 5,850

- e) Government loan surcharge collections are transferred monthly to an account with a fiscal agent.

Special Deposits - Fiscal Agent \$ 1,850

Cash Account \$ 1,850

- f) Semi-annual payment of principal and interest to Government Agency by fiscal agent and \$150 semi-annual amortization of administrative fees (\$4,500 divided by 30 semi-annual payments (15 years time 2 semi-annual payments equals \$150).

Interest Expense - Govt. Loan \$ 7,725

Other Deferred Credit-

Govt. Loan 2,325

³ Intent is that the entire \$150,000 loan proceeds shall be offset by Account 265.2 - Surcharge - Government Loan Contamination Proceeds for Class A water utilities, and Account 271.2 for Class B, C and D water utilities.

⁴ To the extent that any portion of the surcharge is deemed uncollectible those amounts shall be recoverable from ratepayers as an adjustment to the quantity surcharge.

Special Deposits – Fiscal Agent		\$ 10,050
Govt. Loan Amortization Expense	\$ 150	
Deferred Charges		\$ 150

g) Credit of interest earned on surcharge collections deposited with fiscal agent.

Special Deposits – Fiscal Agent	\$ 100	
Non-Utility Income – Interest		\$ 100

h) Annual amortization of 15 year Government plant (\$150,000 divided by 15 years = \$10,000). Amortize in lieu of booking depreciation.

Govt. Loan Amortization Expense	\$ 10,000	
Accumulated Amortization – Govt. Loan		\$ 10,000

Rule 1 is acceptable

2. No return shall be earned by Commission-regulated water utilities (Utilities) on plant to the extent that it is funded by government contamination loans repaid through ratepayer surcharges.

Rule 2 is acceptable

3. A rate surcharge shall be established which provides for a period of one year an amount of revenue approximately equal to the periodic payment which includes principal and interest. Any surplus surcharge revenue shall be refunded to ratepayers and any shortfall in debt service shall be recovered in rates. The annual adjustments to the surcharge shall be made through a Tier 2 Advice Letter filing.

Rule 3 is acceptable – although annual adjustments to this loan may not be necessary and could be made in each rate case cycle since other issue with the facility will likewise be addressed in each rate case.

4. No gain shall be recovered by utilities on the disposition of plant to the extent that it has been funded by government contamination loans repaid through ratepayer surcharges, except for gains from the sale of real property,

previously acquired with contamination proceeds but no longer used and not necessary, covered by § 790 of the Public Utilities Code.

Rule 4 is acceptable

5. Capital charges for a government contamination loan shall be offset by a quantity surcharge which shall last as long as the loan. The charges shall not be intermingled with other utility charges; special accounting requirements, including a refund condition and a shortfall provision, are necessary to ensure that there are no unintended windfalls or losses to utility owners.

Rule 5 is acceptable

6. Operating Expenses, Administrative and General Expenses, and Taxes associated with government contamination loan-funded plant, shall be allowed, if determined to be reasonable by this Commission. The reasonableness of these costs shall be determined in the general rate case that addresses the results of operations for the district or districts to which these expenses relate.

Rule 6 is acceptable – although this may be unnecessary in this case for O&M costs as they are addressed separately in the Settlement provisions

7. Any indirect benefits resulting from government contamination loan-funded plant such as reductions in operating expenses resulting from infrastructure improvements must be projected as cost savings in calculating the utility's revenue requirement.

This Rule is unnecessary in this case as cost savings is addressed separately in the Settlement provisions.

8. Unless the utility has received authorization from the funding agency, government contamination loan funds shall not be spent on expenses. Loan Funds that are expended for expenses authorized by the funding agency must not be included in the determination of the Results of Operations and the

forecast of future expenses in a general rate case. Within 30 days after a funding agency authorizes a utility to spend Loan Funds on expenses the utility must file a Tier 2 advice letter filing that sets forth an accounting treatment to exclude such expenses from the Results of Operations and forecast of future expenses in a general rate case.

Rule 8 is acceptable

9. In the event construction or study completion time limits are not established by the funding government agency, then the following provisions are reasonable and should apply:

- Construction of the project must start within one year after execution of the funding agreement;
- The project shall conclude within three years after execution of the funding agreement;
- Utilities must seek Commission approval for extensions of time limits at least two months prior to the expiration of those limits or risk loss of undelivered funding;
- Extension requests may be submitted by a Tier 2 advice letter;
- A minimum of three competitive bids shall be required unless justification is provided showing why the minimum could not be met;
- If the utility does not choose the lowest bid, it must provide a detailed justification explaining why it chose not to accept the lowest bid; and
- Utilities should be allowed to enter sole source contracts under special circumstances. If the utility chooses a sole-source contract, it must provide a detailed justification explaining why it did so.

This Rule is unnecessary and in fact could be harmful in this situation as the project addressed in this settlement is not the ordinary construction project for a water utility and in fact may take longer to design, build and bring to completion. Additionally, the timing of this project is already driven by other state requirements and orders and no further requirements are necessary. All bidding and other requirements as noted above are addressed already in separate agreements in this current proceeding and those agreements should not be countermanded by the Rules in this appendix.

10. Water utilities shall use a competitive bidding process specified by the funding government agency when awarding contracts for the construction of government loan-funded projects. If the funding government agency does not require specific competitive bidding process the utility shall use the competitive bidding process set forth in Rule 9 above.

Same comment as in Rule 9 above.

11. Water utilities may use Loan Funds for work done prior to the execution of the loan agreement only when the funding government agency has authorized this use. To the extent approval is given to use loan funds for work already performed such activity shall be accounted for pursuant to the accounting procedures set forth in this appendix for loan work not yet undertaken. At the time of the utility's next general rate case, the utility shall provide as part of its filing sufficient information for the Commission to review and determine the appropriate ratemaking treatment for any work performed that was not authorized by the funding agency.

This Rule is unnecessary as all financing for the project contemplated in A12-04-019 is addressed in the Settlement.

12. These rules apply to all tangible property funded with Loan Funds. In determining the proceeds in each of the following types of sales, the cost of disposal shall be deducted from the amount received in arriving at the final amount received. In cases of intangible property, such as the intellectual property of a study, the utility shall request the Commission to individually review the matter in the utility's general rate case or, sooner if requested, by separate application.

This Rule is acceptable

13. In order to ensure that the Commission has prior review and approval over all government loan-funded plant transactions, water utilities shall provide written notice to the Director of the Division of Water and Audits and the Director of the Division of Ratepayer Advocates 30 days prior to the disposition of loan-funded plant.

This Rule is acceptable

14. The following rule shall apply to the transfer or sale of an asset, district, or total utility to another Commission-regulated water utility. If the asset to be sold or transferred has been paid for with Loan Funds in whole or part, the utility transferring or selling the asset may not receive compensation for the portion of the asset that has been funded with Loan Funds except for gains from the sale of real property previously acquired with contamination proceeds but no longer used and not necessary, covered by § 790 of the Public Utilities Code, and the purchasing utility shall record a non-rate base asset as a separate component of Account 265.2. The asset should sell or transfer at fair market value, subject to § 790 of the Public Utilities Code.

This Rule is acceptable

15. When government loan-funded plant is sold to a publicly-owned water provider that will deploy the asset to provide water service to the public, the public interest integrity of the loan is preserved, and the rules governing the transaction from the selling utility's position would be the same as if the sale were to a Commission-regulated water utility.

This Rule is acceptable

16. When government loan-funded assets are sold to an entity other than a utility or public water provider, such as private unregulated companies or cities or counties exercising eminent domain powers for purposes other than acquiring

a municipal water system, the public interest integrity of the loan is not preserved. In these instances, the appropriate treatment is for the buyer to pay fair market value and for the selling utility to apply all proceeds received from the sale of the government loan-funded asset paid by ratepayer surcharges to the benefit of ratepayers, except as § 790 of the Public Utilities Code provides otherwise.

This Rule is acceptable

17. For plant wholly funded by Loan Funds, as well as for the partially funded portion of a plant, the utility must notify the Director of the Division of Water and Audits within 30 days after the utility signs a letter of commitment with the agency administering the loan and again within 30 days after completing the loan agreement execution with the responsible agency. For any portion of plant that is paid for by non-government loan funds, the utility must obtain Commission approval in its general rate case or through separate application.

This Rule is unnecessary as all provisions as to the financing of this project should be addressed together in a decision in this application.

18. All utilities that receive Loan Funds must provide the following information regarding its loan-funded plant in its Annual Report to the Commission: (1) Amount of Loan Funds received, (2) Amount of Loan Funds spent in the year covered by the Annual Report, (3) Amount of ratepayer surcharges billed and received, (4) Amount of loan repaid by ratepayer surcharges and (5) Description of plant constructed with Loan Funds.

This Rule is acceptable

19. When the "fair market value" asset valuation of a district or total utility is difficult or impossible to perform without the loan-funded plant, the government

loan-funded plant must be deducted from the “fair market value” of the total utility that has been determined by the valuation, except for the sale of real property previously acquired with contamination proceeds but no longer used and not necessary, covered by § 790 of the Public Utilities Code. Since the value of the loan-funded plant in the valuation has most likely been inflated, the selling utility should inflate the depreciated book value of the loan-funded plant using the Handy-Whitman index.⁵ This inflated value of loan-funded plant should be deducted from the “fair market value” of the utility. This “Adjusted Fair Market Value” would then be used to determine the reasonable purchase price of the asset.

This Rule is acceptable for plant that can't be “untangled” from other assets, however, it may be unnecessary as to plant that can be easily separated.

(END OF APPENDIX

⁵ The Handy-Whitman index is a widely recognized publication which reflects the costs of different types of utility construction.