

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA



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Order Instituting Rulemaking on the )  
Commission's Own Motion into Addressing )  
the Commission's Water Action Plan Objective )  
of Setting Rates that Balance Investment, )  
Conservation, and Affordability for the )  
Multi-District Water Utilities of: California- )  
American Water Company (U210W), )  
California Water Service Company (U60W) )  
Del Oro Water Company, Inc. (U61W) )  
Golden State Water Company (U133W), and )  
San Gabriel Valley Water Company (U337W) )

R.11-11-008  
(Filed November 10, 2011)

OPENING COMMENTS OF  
SAN GABRIEL VALLEY WATER COMPANY (U337W)  
IN RESPONSE TO ORDER INSTITUTING RULEMAKING

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March 1, 2012

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In accordance with Rule 6.2 of the Commission's Rules of Practice and Procedure and the directions provided in the above-captioned Order Instituting Rulemaking (the "OIR"), San Gabriel Valley Water Company ("San Gabriel") submits the following opening comments.

**I. Introduction**

San Gabriel provides public utility water service in two geographically separated operating and ratemaking divisions in Southern California. San Gabriel's Los Angeles County division provides water service to a population of approximately 272,000 in 15 cities and in unincorporated areas of Los Angeles County. About forty miles to the east, San Gabriel's Fontana Water Company division provides water service to a population of approximately 210,000 in the cities of Fontana, Rialto, and Rancho Cucamonga and in unincorporated areas of San Bernardino County.

Because the questions posed to the water utilities in this proceeding are rather broad, San Gabriel will first address the issues in a general context before answering the specific questions as they relate to the company.

## **II. Background**

This OIR considers the Commission's Water Action Plan objective of setting rates that balance investment, conservation, and affordability. The OIR raises such diverse and competing issues as affordability of water and rate subsidies, water district consolidation guidelines, rate shock and rate stabilization, conservation of water and power, and impacts on land development. Related issues include consistency and efficiency of utility regulation, water quality, reliability of water service, and the growing need to replace aging infrastructure.

The Commission has a longstanding history of setting water rates to achieve the following objectives:

- Effective water rate regulation adheres to stated policies (e.g., the Water Action Plan) and clearly promotes those policies.
- Water rates should be based on the cost of service and provide utilities the ability to attract capital at a reasonable cost to fund necessary investments in utility plant.
- Water rates should be affordable for water required for essential needs such as consumption and sanitation.
- Water rates should be designed to discourage wasteful use.
- Water rates should be designed so customers can understand why and how they are being charged.
- Water rates should be designed to promote stability and predictability, and avoid sharp fluctuation.
- Efficient water rate regulation minimizes the costs of providing water service, including the costs of complying with the regulation.

Various mechanisms being evaluated in this OIR could promote or discourage these ratemaking objectives in unique ways. For example:

1. Water District Consolidation

Water district consolidation runs counter to some of the above ratemaking objectives.

The main beneficiaries of water district consolidation are customers in small water districts, where high fixed costs must be spread over a small customer base. However, water district consolidation can lead to less equitable treatment of ratepayers when it causes cross-subsidies between customers of previously-independent rate-setting districts.

2. Rate Subsidies and High Cost Funds

All Class A water utilities offer rates that provide low-income residential customers with affordable water service. A problem occurs in a water district with a high percentage of customers who qualify for the low-income rates. That situation imposes an even greater burden on the non-qualifying customers who must subsidize the low-income program.

Another type of rate subsidy encourages large industrial customers to remain a customer of the water utility. Such incentives can be justified when a high-volume industrial customer considers leaving the area or using a private well, thereby causing the remaining customers to bear a greater share of fixed costs and pay higher rates because of the lost sales.

3. Rate Case Plan

While this OIR does not explicitly review the Rate Case Plan (“RCP”), the RCP impacts many of the same issues in this OIR. Under the RCP, Class A water utilities must file a general rate case every three years. Rates are adopted for a single future test year, with lesser indexed rate increases allowed in the two intervening escalation years. Most multi-district water utilities are now being required to file a companywide general rate case, even while maintaining separate rates for individual ratemaking districts.

Rate shock is a major byproduct of the RCP as rate increases at the beginning of the single test year reflect reasonable and necessary expenditures that are not fully reflected in rates during the two preceding escalation years. Using two or three test years in a general

rate case would avoid large rate increases in the test year followed by much smaller rate increases in the two subsequent years.

Another major byproduct of the RCP is the consolidation of multiple districts in a single general rate case which dilutes the focus on individual issues of each ratemaking district and causes an uneven and burdensome workload for the water utilities, Division of Ratepayer Advocates (“DRA”), and the Commission. Evaluating the rates for multiple ratemaking districts in the same proceeding would generate customer confusion and even resentment that the Commission is not responsive to the needs of the individual ratemaking districts.

### **III. San Gabriel’s Response to Questions**

San Gabriel provides the following comments to the specific questions posed in the OIR:

***Question 1** – Identify current mechanisms utilized to subsidize rates and prevent rate shock, such as low income rates and rate support funds. Are these current mechanisms adequate to address ratepayer needs in general? Do these current mechanisms achieve an appropriate balance between utility investments, conservation and affordability of rates?*

San Gabriel offers low-income rates (California Alternative Rates for Water) in both divisions. While supporting the goal of rate affordability, low income rates have no material impact on rate shock.

San Gabriel’s Fontana Water Company division, a service area with significant growth and development potential, applies Facilities Fees for all new connections. These revenues are recorded as Contributions in Aid of Construction, thereby moderating the effect of major utility plant additions. The Commission has expressly directed San Gabriel to apply the Facilities Fees to offset the company’s \$45 million cost to design and build a new surface water treatment plant, thereby greatly minimizing the cost of that plant to customers in that division. In its pending application (A.11-06-005) for a recycled water project, the company proposes to use Facilities Fees to offset the cost of constructing recycled water distribution facilities.

**Question 2** – *Should the Commission modify the existing 1992 consolidation guidelines, as described in D.05-09-004? If so, what specific modifications are warranted and what are the justifications for those modifications?*

No. In D.05-09-004, the Commission established four criteria (proximity, rate comparability, water supply, and operation) that were jointly developed by the Division of Ratepayer Advocates and Class A water companies. These four criteria were to be considered in establishing a *prima facie* case for district rate consolidations. When these guidelines are not met, the applicant is required to bear the burden of showing that the advantages of consolidation outweigh the disadvantages.

These criteria are adequate. District consolidations should be evaluated on a case-by-case basis and should always be voluntary. If the Commission desires a larger water utility to “rescue” a smaller, unsustainable water utility, it should provide sufficient incentives and remove any disincentives necessary to achieve a specific consolidation.

**Question 3** – *To the extent a new district consolidation mechanism is necessary, identify and discuss significant characteristics of water districts that should be included in an analysis of whether consolidation is appropriate. Examples of significant characteristics include: infrastructure, geography, topology, hydrology, climate, water quality, nature of water supply, rate differences and average water usage.*

This question can only be answered within the context of the reasons that justify a new district consolidation. San Gabriel believes such a reason would be where customers are subject to grossly disproportionate rate impacts because of their location.

For example, where a water utility has both very small ratemaking districts (i.e., equivalent to Class B, C, or D companies) with high water rates and very large ratemaking districts with lower water rates, it might be appropriate to combine them for ratemaking purposes. This would make rates more affordable in the small ratemaking districts while causing only nominal increases in the larger water districts.

The Commission should consider incentives to promote the takeover of willing smaller water utilities where the consolidation with a larger investor-owned water utility provides customers of the smaller utility with significant benefits such as access to capital for infrastructure, professional expertise, and economies of scale that cannot be realized because of the existing size.

**Question 4** - *What advantages and disadvantages, if any, would result from implementing a "High-Cost" fund? How could such a "High-Cost" fund operate?*

There are numerous ways to design a "High-Cost" fund and any advantages and disadvantages of such fund would depend on its specific design.

**Question 5** - *What requirements and conditions, if any, should be included in any new district consolidation mechanism or "High-Cost" fund?*

For district consolidation mechanisms or "High-Cost" funds within a single water utility, San Gabriel recommends that any requirement or condition be tailored for the specific situation. For district consolidation mechanisms or "High-Cost" funds that extend beyond a single utility, San Gabriel recommends that such mechanisms not be promoted except in the most exigent circumstances.

Where there is rate consolidation within a single multi-district water utility, a complete consolidation is not always necessary or desirable. For example, water and power costs could be charged only to the individual district while the remaining costs could be consolidated and spread over one or more other districts for ratemaking purposes. A consolidation of this sort might simplify the rate design procedure so long as the consolidation satisfies the four Commission criteria.

**Question 6** - *What impacts would increase consolidation of water utility districts or the establishment of a "High-Cost" fund have on: (A) land development in the districts and (B) ongoing water and energy conservation efforts, including those mandated by Federal and State laws such as the Water Conservation Act of 2009? Is it possible to effectively mitigate these impacts?*

The impacts would be extraordinarily difficult to measure or mitigate except in response to a district's unique circumstances.

**Question 7** – *What impact, if any, would Public Utilities Code Section 701.10 or other statutory requirements have on the ability of multi-district water utilities to establish a “High-Cost” fund or to increase consolidation?*

Public Utilities Code §701.10 sets state policy for the establishment of water rates and charges. Briefly, water rates must (a) afford the utility an opportunity to earn a reasonable return on its investment, (b) minimize the long-term costs of water service (c) promote water conservation, (d) provide for equity between present and future ratepayers, (e) promote long-term rate stability, and (f) to the extent consistent with the foregoing, recover fixed costs with fixed revenues. It is foreseeable the present customers of large ratemaking districts would object to water rate increases intended to establish a “High-Cost” fund or subsidize consolidation with a small water system elsewhere. Section 701.10 requires the Commission to “minimize the long-term cost of service” and, therefore, could be read as a restriction on establishing a “High-Cost” fund.

**Question 8** – *Identify any additional impacts that would result from increased consolidation of water utility districts or the establishment of a “High-Cost” fund.*

Ratepayer acceptance seems to be the major hurdle in any consolidation of water districts or the establishment of a “High-Cost” fund. Change is not easy, especially when the benefits of a rate consolidation or a “High-Cost” fund are not equitable.

#### **IV. Conclusion**

This proceeding provides an opportunity to improve existing ratemaking procedures to better serve the objectives specified in the Commission's Water Action Plan. San Gabriel appreciates this opportunity to offer its comments on these very important issues.

Respectfully submitted,

/s/ ROBERT W. NICHOLSON

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Attorney for San Gabriel Valley Water  
Company

March 1, 2012

**VERIFICATION**

I, Robert W. Nicholson, am President of San Gabriel Valley Water Company, a Respondent in the foregoing Rulemaking and am authorized to make this verification on its behalf. The statements in the foregoing document are true of my own knowledge, except as to matters which are therein stated upon information or belief, and that as to those matters, I believe them to be true.

I declare under penalty of perjury that the foregoing is true and correct.

Executed at El Monte, California, on March 1, 2012.

**/S/ ROBERT W. NICHOLSON**

Robert W. Nicholson

President