Decision **PROPOSED DECISION OF ALJ LONG (Mailed 10/18/2005)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of Apple Valley Ranchos Water Company (U346W) for Authority to Increase Rates Charged for Water Service by $2,748,100 or 18.56% in 2006, $496,580 or 2.69% in 2007, and $1,075,879 or 5.46% in 2008.	Application 05-02-005 (Filed February 1, 2005)

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Jason Reiger, Attorney at Law, for Office of Ratepayer Advocates.

OPINION ADOPTING TEST YEAR 2006 REVENUE REQUIREMENTS FOR APPLE VALLEY RANCHOS WATER COMPANY

Table of Contents

Title **Page**

OPINION ADOPTING TEST YEAR 2006 REVENUE REQUIREMENTS FOR APPLE VALLEY RANCHOS WATER COMPANY 2

1. Summary 2
2. Background 2
3. Hearing and Record 3
4. Legal Authority 4
   - A. The Public Utilities Act 4
   - B. Burden of Proof 5
5. Issues 5
6. ORA's Recommendations 7
7. Escalation Rates 7
8. Comparison Exhibit 9
9. Cost of Capital 9
   - A. Apple Valley's Showing 9
   - B. ORA's Proposal 11
   - C. Discussion 12
10. Capital Additions 15
    - A. New Wells 15
    - B. Stipulation 18
    - C. Standpipe Replacements 20
11. Depreciation in Working Cash 21
12. Five-year Average 23
13. Low-Income Ratepayer Assistance 24
    - A. Discussion 27
      - 1. Eligibility 28
      - 2. Current Eligibility Criteria 29
      - 3. CARW Discount Balancing Account 30
      - 4. CARW Implementation Memorandum Account 31

Table of Contents

Title	Page
14. Unresolved Ratemaking Issues	32
A. Customers, Water Sales and Operating Revenues	32
B. Purchased Power	34
C. Customers Other Expenses	36
D. Insurance – Operating Expense	36
E. Insurance – Main Office	37
F. Gravity Irrigation Rate Design	38
G. Unaccounted for Water	40
H. Pump Efficiency Improvement	41
15. Infrastructure Improvement Act	42
16. Justification of Back-up Generators	43
17. Comments on the Proposed Decision	44
18. Assignment of Proceedings	44
Findings of Fact	44
Conclusions of Law	48
ORDER	49

Appendix A Summary of Earnings Test Year 2006

Appendix B Schedule No. 1 – General Metered Service
Schedule No. 2 – Gravity Irrigation Service
Schedule No. 4 – Non-Metered Fire Service
Schedule No. LC – Late Payment Charge
Schedule No. UF – Surcharge to Fund

Appendix C Comparison of Rates Test Year 2006

Appendix D Adopted Quantities

OPINION ADOPTING TEST YEAR 2006 REVENUE REQUIREMENTS FOR APPLE VALLEY RANCHOS WATER COMPANY

1. Summary

Apple Valley Ranchos Water Company seeks a significant rate increase in 2006 and approval of a method to adjust rates for Escalation Years 2007 and 2008. This decision adopts a test year revenue requirement of $ 16,539,400, an increase of 10.58%, for 2006 and approves the formulaic adjustment method for 2007 and 2008 consistent with the existing water company rate case plan, Decision (D.) 04-06-018. The rate of return for Test Year 2006 is 9.45% including a 10.15% return on equity. In addition, this decision adopts a low-income ratepayer assistance plan consistent with Pub. Util. Code § 739.8, granting a $5/month bill credit to Apple Valley customers who meet income eligibility requirements. (Citations to statute refer to the Public Utilities Code unless otherwise noted.) This proceeding is closed.

2. Background

On February 1, 2005, Apple Valley filed this general rate case pursuant to D.04-06-018 that adopted a rate case plan for Class A water companies such as Apple Valley. Apple Valley is a wholly-owned subsidiary of Park Water Company (Park).[1] Apple Valley requests that rates for Test Year 2006 increase by $2,748,100, or 18.56%, and indicates that subsequently, its rates are expected to increase in Escalation Years 2007 and 2008 by an estimated $496,580 (2.69%) and $1,075,879 (5.46%), respectively, pursuant to the method adopted in the rate case plan. Apple Valley says that the Escalation Years are shown for illustration and

[1] See *Apple Valley Ranchos Water Company - Main Office/Cost of Capital Report – Test Year 2006*, p. 1.

customer information purposes, and it will file advice letters to implement subsequent rate changes as allowed by D.04-06-018.

On March 22, 2005, a prehearing conference was held to determine parties, identify issues, consider the schedule, and address other matters. Public participation hearings were held on April 5, 2005, in Apple Valley's service territory. Evidentiary hearings were held June 6 - 8, 2005. Opening briefs were filed by Apple Valley and the Office of Ratepayer Advocates (ORA) on July 1, 2005, and reply briefs on July 8, 2005, in accordance with the schedule adopted in the March 29, 2005, *Scoping Memo and Ruling of the Assigned Commissioner and Administrative Law Judge* (scoping memo).

The scoping memo designated the assigned Administrative Law Judge (ALJ) as the principal hearing officer as defined in Rule 5(l) of the Commission's Rules of Practice and Procedure (Rules). It also determined that this is a ratesetting proceeding. Pursuant to Rule 5(k)(2), the principal hearing officer is the presiding officer for this proceeding. Accordingly, the proposed decision of the ALJ was issued pursuant to Rule 8.1(b).

By a ruling dated April 7, 2005, Apple Valley was required to serve additional testimony presenting an analysis of a low-income customer assistance program, omitted in the original application but required by D.03-08-069, and to supplement its testimony on cost of capital. Apple Valley served the additional and supplemental testimony on May 1, 2005.

3. Hearing and Record

Applicant proposed that this proceeding might include a hearing. The Commission preliminarily determined that this matter would require hearing. (Resolution ALJ 176-3147.) The scoping memo adopted a schedule that included formal hearing. (*See* Rules 6(a)(3) and 6.1(a).)

The record is composed of all filed and served documents, testimony and exhibits received at hearing, and the opening and reply briefs.

4. Legal Authority

A. The Public Utilities Act

Under § 451, public utilities may demand and receive only just and reasonable charges, and they must provide "adequate, efficient, just, and reasonable service" in a way that promotes the "safety, health, comfort, and convenience of [their] patrons, employees, and the public." Under § 454, public utilities must make a showing to the Commission that any proposed rate change is justified, and receive a finding by the Commission to that effect, before making such change. Under §§ 701 and 728, the Commission has the authority to determine what is just and reasonable, and to disallow costs not found to be just and reasonable.

Our legal obligation to the customers of Apple Valley is to ensure that Apple Valley provides adequate service at just and reasonable rates. As we use the term here, adequate service encompasses all aspects of the utility's service offering, including but not limited to safety, reliability, public information services, new customer connections, and customer service. In addition, a utility that provides adequate service must do so in compliance with laws, regulations, and public policies that govern public utility facilities and operations. In carrying out this obligation, we assess whether Apple Valley has justified the revenue increase proposals, disallow those proposals to the extent that they have not been justified, and may even order reductions in the revenues collected by Apple Valley if the evidence shows that is necessary.

B. Burden of Proof

There is a natural litigation advantage enjoyed by utilities in that we must rely in significant part on their evidence and experts; this advantage reinforces the importance of placing the burden of proof in ratemaking applications on the applicant utilities. Apple Valley has the sole obligation to provide a convincing and sufficient showing to meet the burden of proof, and any active participation of other parties can never change that obligation. This was described in D.87-12-067[2] as follows:

> The inescapable fact is that the ultimate burden of proof of reasonableness, whether it be in the context of test year estimates, prudence reviews outside a particular test year, or the like, never shifts from the utility seeking to pass its costs of operations onto ratepayers on the basis of the reasonableness of those costs.

And further:

> The longstanding and proper rule is set forth in D.90642 at 2 CPUC 89, 98-99 and requires that the utility meet its burden by clear and convincing evidence. To meet this burden we have specified that "… the applicant must produce evidence having the greatest probative force."

Nothing in this decision in any way alters or redefines the obligations of Apple Valley to meet the legal requirements on burden of proof.

5. Issues

Based on applicant's statement of proposed issues in the application, ORA's protest, plus parties' statements at the prehearing conference, the issues were identified in the scoping memo as:

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[2] CPUC 2d, 1, 21, and footnote 1 at p. 169.

a. Adoption of a just and reasonable rate of return, and return on equity, for 2006, 2007, and 2008.

b. Adoption of a reasonable forecast of Apple Valley's operating expenses and revenues for Test Year 2006, including Apple Valley's use of the "New Committee Method" to forecast revenues as authorized in D.04-06-018.[3]

c. Adoption of a reasonable rate design.

d. Adoption of a reasonable forecast and appropriate allocation of costs from any parent or other affiliated company included in Apple Valley's revenue requirement for Test Year 2006.

e. Adoption of a reasonable forecast of capital additions, plant in service, and working cash, to estimate Test Year 2006 rate base. Included in this is the appropriate allowance for depreciation in determining the working cash allowance.

f. Examine other issues that may affect Apple Valley's ability to provide efficient, safe, and reliable water service.

g. Determine Apple Valley's compliance with applicable Commission decisions, including but not limited to D.04-06-018, D.03-08-069, and other decisions generally applicable to water utilities, or specifically to Apple Valley and its affiliates. Specifically, the proceeding will examine Apple Valley's:

[3] *Mimeo.*, p. 20, Appendix, p. 6.

1. Implementation of the Infrastructure Improvement Act.[4]
2. Analysis of viability of a low-income rate assistance program.[5]
3. Justification for the inclusion of backup generators in rate base.[6]

6. ORA's Recommendations

During the course of the evidentiary hearings ORA modified a number of its recommendations, and it reached numerous agreements with Apple Valley on account forecasts, main replacements, and other items. As these agreements arose, they were noted in the transcript and are included in Ex. 20, the Joint Comparison Exhibit. We discuss several of these agreements in order to state the Commission's expectations either for implementation or for subsequent proceedings.

7. Escalation Rates

Escalation rates are necessary to derive a forecast for the test year that partly relies on historical data and, pursuant to the rate case plan, to adjust the

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[4] D.04-06-018, Attachment, p. 10. *See* §§ 789 – 790.1.

[5] D.03-08-069, p. 44, and Ordering Paragraph 5: "AVR (Apple Valley) shall gather demographic information about its customers for the purpose of determining the feasibility of offering reduced rate programs for its low-income customers and include those results and a recommendation for a low-income program in its next general rate case (GRC). If AVR determines that such a program is not feasible, it shall explain why."

[6] D.03-08-069, p. 25, and Ordering Paragraph 3: "AVR shall provide information in its next GRC to support the inclusion of backup generators in rate base. That additional information shall include, but not be limited to, the identity of each generator by horsepower, facility intended to backup, year purchased, rate base amount, actual time placed in service as a backup facility, and actual amount of time tested by year since acquired."

test year for the subsequent two escalation years. The escalated forecasts can include both operating expenses and rate base. (See D.04-06-018, pp. 10-15.) The rate case plan determined that a standard was necessary, and it adopted the use of "Estimates of Non-Labor and Wage Escalation Rates" and the "Summary of Compensation per Hour," both published by ORA. Further, any item not covered by these factors is to be escalated using the most recent 12-month "US Cities CPI-U" also published by ORA. Today's decision, the first for Apple Valley under the new rate case plan, will adhere to the plan's requirements unless a party shows good cause for a deviation.

In its application, Apple Valley used several factors for its estimates. For labor, it used the actual cost-of-living-adjustment in effect for 2005 to adjust 2004 recorded wages. It then used a forecast of a further 3% increase for 2006, the test year.[7] ORA proposed that in 2006 we adopt a 2.2% labor escalation factor, consistent with the March 31, 2005 estimates published by ORA.[8] ORA forecast a 0.0% change for 2006 non-labor expenses. For 2007, ORA forecast a labor escalation of 1.7% and 0.0% for non-labor. ORA proposed, and we will also adopt where appropriate, a 2.2% CPI-U escalation rate for 2006.[9] We will use the ORA rates of escalation – for labor, no-labor and rate base – as described in the rate case plan. There are some unique exceptions, including pension and benefits expenses, where we will consider the arguments on escalation rates raised by ORA. Otherwise, we adopt labor escalation rates of 2.2% and 1.7% for

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[7] Ex. 1, p. 20.

[8] Ex. ORA-1, pp. 3-2 & 3-3, and 4-1.

[9] See for example, Main Office Insurance at ORA Ex-1, p. 4-7.

2006 and 2007, respectively; non-labor escalation of zero for both 2006 and 2007; and CPI-U rates of 2.2% and 1.7% for 2006 and 2007.

Apple Valley and ORA used these rates in the Joint Comparison Exhibit.[10]

8. Comparison Exhibit

On July 8, 2005 Apple Valley and ORA jointly filed Ex. 20, a Joint Comparison Exhibit, summarizing the final estimates of both parties, inclusive of all stipulations and other item-by-item agreements. Thirty-one specific "resolved issues" are itemized.[11] Based on the whole record, the agreed-to forecasts are reasonable and are adopted in this decision. We have reviewed the exhibit and find it is consistent with the record, and we can reasonably rely on it for this decision.

9. Cost of Capital

Under the rate case plan, this decision adopts a capital structure and a cost of capital, including the authorized return on equity, for the test year 2006 as well as the two attrition years 2007 and 2008. Apple Valley's capital structure, long term debt financing and equity investment are all provided by its sole shareholder, Park, but we adopt for ratemaking purposes the most appropriate capital structure and cost of capital for Apple Valley.

A. Apple Valley's Showing

Apple Valley requests a capital structure of 42.33% debt and 57.67% equity for all three years, 2006 – 2008. Based on forecasts of its weighted average cost of borrowing it proposes debt costs of 8.49%, 8.41% and 8.35%, respectively, and a constant 11% return on equity for the three years. ORA accepted the capital

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[10] Ex. 20, p. 2, item 2.

[11] Ex. 20, pp. 2 - 5.

structure and weighted cost for long-term debt for the three years,[12] so the only disputed issue is the return on equity. We will adopt the agreed-upon capital structure and cost of debt because they reasonably reflect the actual capital structure and cost of debt for Park as applied to Apple Valley.

Apple Valley's consultants used the Discounted Cash Flow model to derive a water utility benchmark sample equity return of 10.4%. They also used three Risk Premium methodologies to derive a water utility benchmark sample equity return of 10.9% to 11.6%; and the CAPM model to derive a water utility benchmark sample equity return of 11.1%. Apple Valley also proposes to use gas utilities as a basis for justifying a range of 10.3% to 11.2%.[13] Additionally, Apple Valley proposes that there are specific high risks identifiable for water utilities generally and Park, and hence Apple Valley, that would support a range of return on equity of 11.3 to 12.5%. This includes a request for a 90 basis-point risk premium, despite the Commission's findings in D.03-08-069 that 30 basis points were sufficient. That decision was also highly "skeptical" of Apple Valley's analysis,[14] which relied on the same models offered for us to consider again in this proceeding. In that decision, Apple Valley was authorized a 30 basis point risk premium on the "lower second quarter (or 9.80%) of the 9.21% to 11.22%" range for return on equity, resulting in an authorized 10.10% return.

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[12] Ex. ORA-1, p. 13-3.

[13] Ex. 2, p. 35.

[14] D.03-08-069, pp. 29-40.

We find that Apple Valley has again proposed an inflated range for equity returns and further that several of the asserted "risks" are in fact discretionary choices made by Park, the alter-ego of Apple Valley. Apple Valley cites that Park does not publicly trade its stock, and this therefore limits its access to capital.[15] Park is an "S" Corporation[16], a choice made by Park for the convenience of its limited investors, and such a discretionary choice should not result in any increased costs to be borne by the ratepayers. We will not adopt a large risk premium caused by discretionary choices of closely held Park.

We also find that natural gas rates of return are not relevant for Apple Valley. The cost recovery and market risks are totally dissimilar. Apple Valley failed to provide any convincing evidence to support the relevance of gas utility returns, and thus it failed to meet its burden of proof on this portion of its cost of capital showing. We therefore reject Apple Valley's reliance on the returns of equity applicable to gas utilities.

The Commission has never endorsed a single method to forecast return on equity, preferring instead to consider the ranges provided by an array of methods. We will again consider Apple Valley's specific operations and risks, and an array of analyses, to find a just and reasonable return on equity for Apple Valley.

B. ORA's Proposal

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[15] Ex. 2, p. 34, and Ex. 4, un-numbered page 2, Jordan testimony.

[16] An S Corporation is taxed like a partnership or sole proprietorship rather than as a separate entity. Thus, the income is "passed through" to the shareholders for purposes of computing tax liability. Therefore, all shareholders' individual tax returns will report the inome or loss generated by an S Corporation.

ORA did a limited analysis on the return on equity, acknowledging that it did not perform a separate study for Apple Valley.[17] ORA reviewed the proposed capital structure and embedded cost of debt projected for 2006, 2007 and 2008, and accepted them as reasonable estimates.[18] ORA looked at its three most recent recommendations for other Class-A water companies[19] where, on average, ORA's studies recommended a return of 9.47%, about 2.08% less than the average requests of 11.55%. These cases all settled, but the average return included in the settlements was 10.02%. This was an average of 1.53% less than the rate proposed by the utilities.

ORA then focused on its most recent recommendation of 9.61% for California Water Service. It asserted the data underlying that recommendation are still current, and therefore recommended a rate of 9.61% plus a risk premium of 30 basis points (0.30%) for a final return on equity of 9.91%. The proposed risk premium would continue the premium adopted in Apple Valley's last rate case in D.03-08-069, where the Commission adopted a return on equity of 10.10% including the risk premium. The unadjusted rate was therefore 9.80%.

C. Discussion

Unlike the energy utilities that have annual cost of capital proceedings separate from their other ratemaking proceedings,[20] the Class A water utilities

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[17] Ex. ORA-1, p. 13-5.

[18] Ex. ORA-1, p. 13-1.

[19] Settlements pending in A. 04-09-005 for San Gabriel Water Company, A.04-04-040 for California-American Water, and A. 04-09-028, et al., for California Water Service Company. (Ex. ORA-1, Table 13-3.)

[20] *See*, for example, D. 04-12-047 in consolidated A.04-05-021 and A.04-05-023 for Southern California Edison Company and Pacific Gas & Electric Company, respectively.

have a review every three years as a component of the general rate case. One can argue whether there is more risk associated with a return subject to change annually (a volatility risk) or a return fixed for a longer period (an opportunity risk). But we do not see the same risks or degree of risk in water utilities that would warrant a more frequent review. The rate case plan for water utilities opted to review the equity return triennially.

Apple Valley has shown, with the limitations of their implied capital structure, that for 2001 through 2004, it earned a lower actual return on equity than was authorized, while its cost of debt and its equity ratio in the capital structure were (with one exception) lower than authorized.[21] A lower cost of debt and lower equity ratio would tend to increase the actual return on equity, all other factors being constant.

Apple Valley introduced rebuttal testimony in Ex. 8 that was "an update and corrections to ORA's Cost of Capital Report presented in A.04-09-028 … (and) an update of ORA's ROE [return on equity] estimate from A.04-04-040."[22] ORA accepted this exhibit as providing an update and correction. Apple Valley and ORA then offered a written stipulation in Ex. 10 which indicated that the ORA recommendation changed from 9.61% to 9.85%, before consideration of a risk premium.

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[21] Ex. 4, un-numbered page Table 1, Jordan testimony.

[22] Ex. 8, p. 1.

We will adopt the corrected ORA recommendation, inclusive of the risk premium, because the 10.15% return on equity (9.85% + 0.30%) most reasonably reflects the risks faced by Apple Valley.[23] We stress that the inclusion of a risk premium is not automatic, and in Apple Valley's next general rate case, it must continue to meet its full burden of proof for its proposed return on equity and any request for a risk premium addition.

2006 Adopted Cost of Capital			
		Cost	Weighted
Debt	42.33%	8.49%	3.59%
Equity	57.67%	10.15%	5.85%
Total	100.00%		9.45%

2007 Adopted Cost of Capital			
		Cost	Weighted
Debt	42.33%	8.41%	3.56%
Equity	57.67%	10.15%	5.85%
Total	100.00%		9.41%

2008 Adopted Cost of Capital			
		Cost	Weighted
Debt	42.33%	8.35%	3.53%
Equity	57.67%	10.15%	5.85%
Total	100.00%		9.39%

[23] ORA Opening Brief, p. 22.

10. Capital Additions

A. New Wells

Apple Valley forecast an increase in plant in service for 2006 and 2007 of approximately $6.7 million and $5.7 million, respectively.[24] Included in this total are three wells forecast to cost $2.285 million in 2005 (for inclusion in the beginning balance to determine test year 2006), $0.7 million in 2006, and $0.7 million in 2007, for a total cost of $3.485 million.[25] This was one of the largest and most contentious issues in the proceeding.

ORA objects to the proposed inclusion in rate base of these three wells, arguing that they will primarily serve new customers, and do not benefit current customers. ORA believes that a single well will serve 1,090 new customers, therefore, ORA proposes a connection fee of $1,000 based on a cost of $1.2 million per new well.[26] ORA describes the proposed connection fee in several conflicting ways: as a facility fee to be paid by "each new customer of a vacant lot"; as a "contribution" for individual lot owners; and as "advances subject to refund for developers" (p. 12-3). These three descriptions are not synonyms. A "fee" is a general term for a fixed charge for a service. A contribution is essentially a donation of cash or goods or services by a customer as a condition of service, but an "advance" is more likely to be refunded if certain conditions are met.

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[24] Calculated from data in Ex. 1, Table VIII-A.

[25] Ex. ORA-1, pp. 8-6 and 8-7, citing the response to Data request JXM-1.

[26] Ex. ORA-1, p. 12-3. ($1,200,000/well ÷ 1,090 customers = $1,100 per customer.)

General Order (GO) 103[27] includes the following:

I. Definitions
3.f. Service Connection. The term "service connection" shall be construed to mean the point of connection to the customer's piping or ditch with the meter, service pipe or ditch owned by the utility.

V. Extension of Service
2.a. Ownership of Service
(1) Charge for Service Connections. Except as noted in 2a(1)(A) or 2a(1)(B) below, the utility shall make no charge to a customer for making a service connection …

Apple Valley cannot assess a service charge without a deviation from the provisions of GO 103. ORA cites three such deviations, most recently in D.03-09-021 that authorized California Water Service to collect water supply special facility fees for five of its districts.[28] That deviation allows California Water Service to charge a fee on a per lot basis rather than on a sub-division or project development basis, as otherwise allowed in its Rule 15, Main Extensions.

Apple Valley also has a Commission-approved Rule 15 in its tariffs. Included in that rule, pursuant to GO 103, are the various terms and conditions where Apple Valley can charge a new customer or a commercial developer to extend service to their location. An extension under Rule 15.C.1.a does not encompass a charge for new wells: its language deals solely with in-ground extensions of pipelines, valves, etc., but not meters. "The costs of the extension

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[27] *Rules Governing Water Service Including Minimum Standards*, adopted June 12, 1956; Effective July 1, 1956, in D.53204, Case No. 5662; and subsequently modified most recently in D.94-02-043.

[28] See D.03-09-021, Attachment B, p.9, Section 5.09 which is the "Joint Recommendations of the Office of Ratepayer Advocates and California Water Service Company". These fees are not otherwise discussed in the decision.

shall include necessary service stubs or service pipes, fittings, gates and housing therefor, and meter boxes, but shall not include meters."[29]

ORA would extend the concept to include the wells that produce the water.

Another portion of the tariff's main extension rule, Rule 15.C.1.b,[30] also allows Apple Valley to charge developers an advance to pay for other additional equipment necessary to serve new customers:

> If special facilities consisting of items not covered by Section C.1.a. are required for the service requested and, when such facilities to be installed will supply both the main extension and other parts of the utility's system, at least 50 percent of the design capacity (in gallons, gpm, or other appropriate units) is required to supply the main extension, the cost of such special facilities may be included in the advance, subject to refund …

ORA would have the Commission direct Apple Valley to charge a fee on a per lot basis that is not necessarily charged in total to the initial developer, and the fee would explicitly include the cost of the wells as "special facilities." Thus, Apple Valley could charge a fee under Rule 15.C.1.b for necessary equipment not included in the charges under Rule 15.C.1.a.

Existing customers should be treated equitably when compared to new customers. Equitable treatment would justify including new wells in a special facilities charge to new customers if the effect of otherwise including the wells in rate base would result in existing customers paying higher rates that subsidize

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[29] Revised Cal. P.U.C. Sheet No. 393-W. For Apple Valley's tariffs, *See*: http://www.avrwater.com/pdf/avrtariffs/TOC.pdf.

[30] Portion of Rule 15.C.1.b. Revised Cal. P.U.C. Sheet No. 393-W.

the cost of connecting new customers. This is the justification for Apple Valley's Rule 15.C.1.d:[31]

> If, in the opinion of the utility it appears that a proposed main extension will not, within a reasonable period, develop sufficient revenue to make the extension self-supporting, or if for some other reason it appears to the utility that a main extension contract would place an excessive burden on customers, the utility may require nonrefundable contributions of plant facilities from developers in lieu of a main extension contract. (Emphasis added.)

Construing all the provisions of Apple Valley's Rule 15, we conclude that the cost of all necessary facilities to serve new customers, including wells, tanks and treatment facilities, when clearly attributable to new customers, should be recovered in the facilities charge, and not imposed on the existing customer base. We will adopt a stipulation discussed below to exclude 75% of $3.5 million in capital additions from rate base for 2006 and 2007; grant Apple Valley the necessary deviation from GO 103; and clarify that Rule 15 advances and contributions include such necessary facilities as wells, tanks or treatment facilities necessary to serve new customers.

B. Stipulation

During the evidentiary hearings, Apple Valley and ORA stipulated to a change in the fee structure that would allocate a large portion of the new wells' costs to new connections, larger than five connections per request. Apple Valley agreed to a 75-25 split, so that a connection fee would cover 75% of the forecast and only 25% would be included in rate base. A connection fee of $1,000 would

[31] Revised Cal. P.U.C. Sheet No. 394-W.

be imposed on developments of more than five houses and exclude single non-developer connections.[32]

We will accept the stipulation that only 25% of the proposed new wells will be added to the rate base for test year 2006 and for 2007 additions. Apple Valley is at risk for any shortfall. Apple Valley will modify its Rule 15, as necessary; charge a connection fee of $1,000; and may exclude single connections and developments under 5 units. To avoid gaming, we will add a provision that all connections by a single individual, or corporation or other entity, over a period of 18 months should be counted against the 5 unit exclusion. This will avoid piecemeal connection requests to evade the fees. If there are 6 or more connections within 18 months Apple Valley must assess $6,000 on the sixth connection and thereafter impose a $1,000 connection fee on all subsequent connections by that individual or entity. Apple Valley must track every exemption and make those records available to ORA in the next general rate case.

Apple Valley expressed concern that there was a notice deficiency that could delay implementation of the stipulation. We disagree. As long ago as D.88-01-050,[33] the Commission held "no additional notice was required when … the commission staff proposed a rate spread not contemplated by a local exchange carrier, which had properly notified its customers of its application for a rate increase." Allocating certain costs to a connection fee rather than rate base

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[32] Ex. 7, Attachment 2 shows the development of the 75% split to new connections and Attachment 4 showed the effect of a $1,000 fee. See also Transcript, pp. 309 - 310.

[33] D. 88-01-050 in Case 84-06-049, Richard L. Farrington et al. v. Citizens Utilities Company of California. (27 CPUC 2d, 308.)

is nothing more than a different rate spread. No further notice is required and there will be no delay to implementation.

C. Standpipe Replacements

ORA initially disputed Apple Valley's proposal for replacement of water standpipes (public access connections for fighting fires). The testimony showed that Apple Valley had a reasonable need to up-grade its system to ensure system reliability. Parties stipulated to an average of eighty (80) standpipes per year but to include the company forecasts of $170,000, $150,000 and $175,000 for 2005 through 2007, respectively.[34] The average cost is $2,050 per standpipe.

We approve this stipulation, but we require Apple Valley to refund the revenue requirement of any shortfall in the three-year 240 standpipe replacement total in its next general rate case. It is reasonable to impose this refund obligation to ensure that Apple Valley vigorously implements the replacement program. ORA initially questioned the timing and need for these up-graded facilities. This program is within the control of Apple Valley, and it should be prepared to carryout improvements seen as necessary to ensure system reliability. We will fund 240 standpipes, Apple Valley shall make any refund as a reduction to the revenue requirement in the next general rate case for test year 2008, and we expect either 240 installed standpipes or a refund.

[34] Ex. 20, p. 5 (incorrectly cites 90 standpipes), and Transcript, p. 208. Parties confirmed the agreement to be 80 standpipes on July 12, 2005.

11. Depreciation in Working Cash

Apple Valley presented its working cash calculation for inclusion in rate base consistent with the long-standing Standard Practice U-16. ORA proposed a departure to exclude depreciation expense from the working cash calculations.[35] ORA cites D.04-09-061 as adopting this adjustment.[36] ORA testified that it believes depreciation is "… not an out-of-pocket expense. Therefore, it should not be allowed in working cash."[37]

ORA appears to rely on the discussion where the Commission stated:

> We agree with ORA that cash working capital should not include depreciation since this expense does not require Pacific to make a cash outlay. However, Standard Practice U-16 is contradictory about whether depreciation should be included. It appears Pacific was in compliance with Standard Practice U-16 when it followed the numerical example described in the detailed methodology. Therefore, we clarify that for the current and future financial periods Pacific [Pacific Bell, now SBC] shall no longer include depreciation in its cash working capital calculations, regardless of whether the simplified or detailed method is employed. (D.04-09-061, p. 58.)

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[35] Ex. ORA-1, p. 10-1.

[36] D.04-09-061 dated September 23, 2004, in Rulemaking 01-09-001 *Order Instituting Rulemaking on the Commission's Own Motion to Assess and Revise the New Regulatory Framework for Pacific Bell and Verizon California Incorporated* and Investigation 01-09-002 *Order Instituting Investigation on the Commission's Own Motion to Assess and Revise the New Regulatory Framework for Pacific Bell and Verizon California Incorporated*.

[37] Transcript, p. 283, lines 23 - 25.

However, the quoted discussion in D.04-09-061, which would otherwise support ORA's contention, is not reflected in the Conclusions of Law, nor are there supporting Findings of Fact, or an Order that directs the respondents to implement ORA's proposal based on the discussion. Specifically, in D.04-09-061 the Commission's Conclusions of Law did not determine that the working cash was in error and did not conclude depreciation should be excluded. Conclusions of Law 36 through 38 in D.04-09-061 appear instead to adopt the applicant's position, not ORA's, and found Pacific in compliance with the standard practice.

> 36. The procedures set forth in Standard Practice U-16 guides the calculation of "cash working capital." Pacific followed these procedures.
>
> 37. The TURN/ORA proposal to set Pacific's working capital figure at zero is unreasonable because it removes cash working capital from rate base on the basis of alleged errors or complexities in the calculation.
>
> 38. Since we find no "special circumstances" that justify a deviation from Standard Practice U-16, <u>it is reasonable to adopt only the rate base changes concerning cash working capital proposed by Pacific</u> and described herein. Moreover, it is reasonable to modify the IEMR regulatory books for each of the years in this audit to reflect the changes as proposed by Pacific. (Emphasis added.)

Therefore we cannot rely on ORA's interpretation of D.04-09-061, and we decline to make the adjustment in the absence of precedent, or other persuasive argument by ORA. ORA otherwise found that Apple Valley complied with Standard Practice U-16 and correctly calculated working cash. We will therefore only adjust working cash to reflect the flow-through of other adopted adjustments, such as the exclusion from rate base of 75% of the capital expenditures on new wells, discussed above.

12. Five-year Average

One consistent difference for several forecast items is the use of a five-year average. Apple Valley proposed to use 2000 – 2004 where ORA has used the older 1999 – 2003 period. When forecasting using an historical trend, we believe that the most recent record, subject to an opportunity to review the accuracy and reasonableness of the latest year, is the most appropriate record period. ORA was not consistent in using 1999 – 2003. For example, it used the earlier five years for Customer – Other expenses, but used the later five years for Maintenance – Other.[38] Apple Valley had to prepare its application before closing the books for 2004. Thus it had to start with older 2003 data. This problem was specifically anticipated in the rate case plan:

> The temptation to wait for additional historical data, i.e., updates, upon which to base a forecasted test year cannot be indulged when we face a statutory requirement for getting rates in place by a specific date. Any rate case plan requires a data collection termination date; otherwise, no rate case with a forecasted test year would ever be completed. For this reason, our Rate Case Plans have always included a limitation on updates. In this RCP, we have set the general limitation date as the filing of the application for all parties. We will allow two exceptions to this limitation: (1) updates of recorded data, and (2) with the approval of the Principal Hearing Officer based on standards set out in the Appendix. (D.04-06-018, pp. 9-10.)

[38] Ex. 13, pp. 6-7, Apple Valley's rebuttal shows this and other examples.

Apple Valley reasonably up-dated its filing with 2004 recorded data in conformance with the rate case plan. Park (Apple Valley's parent) and ORA specifically considered this issue in the rulemaking leading to the rate case plan.

> Park contends that this information can be conveniently supplied in a February update to its January applications. Similarly, ORA seeks the right to use updated amounts in its reports, which follow the utility's application by a few months. (D.04-06-018, p. 9.)

We will adopt all forecasts that are up-dated to a 2000 – 2004 five year average and reject ORA's forecasts that rely on a 1999 – 2003 average. As a result, a number of unresolved issues in the Comparison Exhibit (Ex. 20) are now resolved.

1. Maintenance Other Expense (Ex. 20, p.7.)
2. Clearing Other Expense – Maintenance (Ex. 20, p.7.)
3. Outside Services – Maintenance (Ex. 20, p.8.)
4. Clearing other Expenses – Main Office (Ex. 20, p.8.)

13. Low-Income Ratepayer Assistance

Recently, San Gabriel Valley Water Company was authorized to implement a low-income ratepayer assistance program in D.05-05-015[39] where we found that a credit to the service charge could still promote water conservation because it left the quantity rate and rate steps unchanged. San Gabriel's California Alternative Rates for Water (CARW) was implemented as a result of earlier Commission directives[40] to develop a program consistent with § 739.8 to provide rate relief for low-income ratepayers:

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[39] A. 03-04-025 filed April 24, 2003.

[40] D.02-10-058, cited in D. 05-05-015 at p. 2.

> § 739.8. (a) Access to an adequate supply of healthful water is a basic necessity of human life, and shall be made available to all residents of California at an affordable cost.
>
> (b) The commission shall consider and may implement programs to provide rate relief for low-income ratepayers.
>
> (c) The commission shall consider and may implement programs to assist low-income ratepayers in order to provide appropriate incentives and capabilities to achieve water conservation goals.
>
> (d) In establishing the feasibility of rate relief and conservation incentives for low-income ratepayers, the commission may take into account variations in water needs caused by geography, climate and the ability of communities to support these programs.

The requirements of § 739.8 are an adaptation for water utilities of the provisions in §§ 739.1-739.5 for gas and electric utility customers that established California Alternate Rates for Energy (CARE) programs:

> § 739.1. (a) The commission shall establish a program of assistance to low-income electric and gas customers, the cost of which <u>shall not be borne solely by any single class</u> of customer. The program shall be referred to as the California Alternate Rates for Energy or CARE program. The commission shall ensure that the level of discount for low-income electric and gas customers correctly reflects the level of need. (Emphasis added.)

In the San Gabriel proceeding, the Commission recognized that "(w)hile we were unable to determine an equitable way to provide every low-income San Gabriel resident a discount for water, we are under no obligation to do so. Since two thirds of San Gabriel's customers are eligible for the discount, there is

no just or compelling reason to deny these low-income customers a discount."[41] The Commission found no reasonable means to extend the CARW assistance to sub-metered customers. San Gabriel estimated that for 5/8-inch service CARW customers the monthly bills will decrease $4.88, but for 5/8-inch service non-CARW customers, monthly bills will increase $2.32. The Commission found imposing this increase on non-CARW customers was reasonable in order to offer assistance to the majority of low-income customers.

Apple Valley was also ordered in D.03-08-069, in its last general rate case to propose the implementation of a low-income ratepayer assistance program in it next rate case. However, Apple Valley filed Ex. 5 only after the April 7, 2005 ruling required it to file such a proposal. Apple Valley concluded that it should not offer a low-income assistance program. It cites the costs for non-recipients and the fact that all eligible low-income customers are not served directly on an Apple Valley meter, because many are sub-metered.[42] The costs are estimated as follows: 5,801 out of 18, 557 residential customers (31%) are estimated to likely meet the low-income guidelines; a $5/month discount would cost $29,005 in revenues to be reallocated to non-recipients; thus the 12,756 non-recipient customers' bills would increase by $2.27 per month.[43]

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[41] D.05-05-015, p. 4.

[42] Ex. 5, p. 4.

[43] Data, *See* Ex. 5, pp. 4-6. Apple Valley used an old income limitation to estimate the number of eligible customers. (See transcript, p. 300.)

Apple Valley illustrated five options:

Discount	Monthly Reallocation	Non-Recipients Cost
15% Total Bill	$88,191	$6.91
10% Total Bill	$58,780	$4.61
5% Total Bill	$29,411	$2.31
$10/Month	$43,954	$3.45
$5/Month	$29,005	$2.27

Apple Valley proposed that the Commission should not adopt any the above five options for a CARW rate discount and recommended instead "that conservation programs be evaluated … (because lost water from) …leaky pipes and fixtures is a significant issue." Apple Valley suggests that Commission should open a rulemaking "to explore other funding mechanisms including the feasibility of a Federal Water Assistance Program or a State Wide Assistance Program under which each utility would provide funding to the program (similar to CARE)."

A. Discussion

A $5/month low-income assistance program for Apple Valley costs five cents less per non-CARW customer ($2.32 - $2.27) than the cost of San Gabriel's program, and it provides 12-cents more in discount ($5.00 - $4.88). These figures are based on only applying the cost recovery to other residential customers even though § 739.8 does not explicitly limit the reallocation to residential customers, and the analogous energy program in § 739.1 explicitly states the costs recovery for the program "shall not be borne solely by any single class."

As discussed below we will immediately adopt a $5 per month service charge discount for low-income ratepayers. We will not consider larger discounts at this time. We will instead focus on the $5 program, which is similar to the recently adopted San Gabriel program.

ORA recommended that we adopt the $5/month service charge discount and that Apple Valley should be allowed to track implementation costs for later recovery. ORA also indicated it intended its recommendation to be consistent with the San Gabriel program. We approve these recommendations and also adopt specific simple procedures for Apple Valley to ensure compliance.

As noted for San Gabriel, we presently cannot extend the low-income assistance to customers served by a master meter, and a landlord attentive to every dollar will see a $2.27 increase to the service charge (but not as a separate line item). Thus, in a small five-unit complex, were the landlord to pass through the service charge increase, the individual renter could see a $0.45 ($2.27 ÷ 5) per month rent increase. At a larger complex, the impact per consumer would be lower. This conjecture conservatively assumes all master-metered customers are otherwise eligible for the CARW discount. We reluctantly accept this potential adverse impact, but we will consider any improvements offered to us in subsequent proceedings.

1. Eligibility

The easiest way to reach the eligible customers is to automatically assign them based upon their current participation in an existing CARE program. Therefore, customers may demonstrate eligibility by showing proof of their enrollment in the Southern California Edison CARE program. Such proof can be a recent bill showing the customer is a CARE customer. Alternatively, the water customer may not have an account in his or her name with Edison, or for any reason does not want to provide a bill to Apple Valley. Therefore, Apple Valley must create a self-certification application substantially similar to Edison's (or another approved form as used by a California utility) and file that application form by advice letter for Commission approval.

2. Current Eligibility Criteria

The Commission authorized the Low-Income Rate Assistance Program (LIRA) by D.89-07-062 and D.89-09-044. LIRA became CARE, effective January 1, 1995, as a result of Senate Bill (SB) 491. The current effective rules for determining low-income eligibility are set forth in Resolution E-3524, dated February 19, 1998. The current eligibility criteria[44] for energy utilities were authorized in an April 26, 2005 letter from the Commission's Energy Division, in compliance with Resolution E-3524:

Household Size	Income Limitation
1 - 2	$24,200
3	$28,400
4	$34,200
5	$40,000
6	$45,800
Each Additional	$ 5,800+

We will apply these already existing eligibility income limits on the Apple Valley program adopted in this decision. The current eligibility criteria may affect Apple Valley's estimate of eligible customers because it did not consider the sliding scale for household size. We will use Apple Valley's household number and provide a balancing account as discussed below. Apple Valley shall use the updated income limits in accordance with the Energy Division's annual letters.

[44] In contrast to the old criteria used by Apple Valley (Transcript, p. 300). Resolution E-3524 sets forth a requirement for Energy Division to annually update the income limitations.

Apple Valley must publicize the availability of the low-income discount and explain to its customers how to apply, and the eligibility criteria. We will direct Apple Valley to propose customer notices to the Commission's Public Advisor for approval, and Apple Valley shall inform all customers of the program in every billing cycle for the first 12 months following the effective date of this decision.

3. CARW Discount Balancing Account

We will include in this proceeding's rate design the assumption that Apple Valley will incur the $29,005 annual revenue reallocation to provide a $5 per month discount to 5,801 customers. Our adopted rate design includes this reallocation, making Apple Valley whole for the forecast. It is very likely that the number of eligible customers, or the monthly value of actual discounts, will not match this estimate. Therefore, Apple Valley shall file an advice letter to establish a CARW Discount Balancing Account to record the over- or under-provisioning of the discount. For example, if only 5,000 monthly discounts are made in January 2006, then $4,005 (801 customer-shortfall @ $5 each) would be recorded as an over-collection to be refunded to non-recipient customers, or to offset the cost reallocation for subsequent year's discounts. Equally, Apple Valley may record for future recovery any under-collection should there be more discounts to low-income customers than we forecast in the test year. As with any balancing account, Apple Valley must meet its burden of poof that the balance is correct and reasonable.

Apple Valley may recover in the annual escalation year filing the prior year's balance in its CARW Discount Balancing Account, subject to refund, based on a reasonableness review in its next general rate case. The recovery should be treated as a revenue adjustment.

4. CARW Implementation Memorandum Account

It is also fair to allow Apple Valley an opportunity to recover its reasonable implementation costs that are incremental to costs already included in its test year revenue requirement. We have no reliable current estimate by Apple Valley of the scope or the cost of implementation. For example, if Apple Valley could show that programming costs are necessary to modify the billing system, then Apple Valley should be able to recover those costs. Similarly, specific advertising or notices for the service may be incremental to embedded costs for customer communications. We will authorize Apple Valley to file an advice letter to create an implementation memorandum account to record its incremental costs.

Balancing accounts as authorized by the Commission have an associated expectation of recovery, they have been, so to speak, pre-authorized by the Commission, and it is the recorded amounts that are reviewed for reasonableness. Memorandum accounts, in contrast, are accounts to record costs for tracking purposes to allow the utilities to meet their burden of proof for the later opportunity to recover recorded costs. Recovery is not automatic. Because we cannot predetermine the full scope of recoverable implementation costs, in contrast to the revenue reallocation discussed above, a memorandum account is the appropriate mechanism to recover the reasonable CARW program implementation costs.

Apple Valley may recover its reasonably incurred implementation costs subject to these limitations: (1) the costs are solely related to implementing and operating a CARW program; (2) the costs are incremental to cost already included in the test year forecast; and (3) Apple Valley can demonstrate that they were the lowest reasonable costs necessary to implement the program. These

tests are the same tests we impose on utilities for a catastrophic event memorandum account, where we do not know the costs in advance, but we still impose a duty to exert reasonable management control. Again, Apple Valley must meet its burden of proof for any cost recovery.

Apple Valley may recover its CARW Implementation Memorandum Account, subject to refund, based on a reasonableness review, in its next general rate case scheduled for a test year 2009.

Apple Valley shall report annually on March 1, to both ORA and the Water Division, on the number of actual participants and the balance in the CAWR Implementation Memorandum Account and in the CARW Discount Balancing Account.

14. Unresolved Ratemaking Issues

The Comparison Exhibit (Ex. 20) identifies 17 unresolved ratemaking issues. In this section we address the positions of the parties and finally resolve eight of these issues. Four of the 17 issues were resolved elsewhere by adopting a standard five-year average of 2000 – 2004. We also address elsewhere in today's decision the other five issues (notice of new supply facility fees, return on equity, emergency generator reporting, low-income programs, and depreciation in working cash).

A. Customers, Water Sales and Operating Revenues

There are nine separate customer categories for water sales, and there is no agreement on the test year forecast. The parties agree on the method to estimate sales forecasts for all customer classes. For the residential customer class, they agree to use a monthly econometric model that includes time, rain, temperature and monthly dummy variables. For all other customer classes, the parties agree to use a five-year average of recorded sales per customer. One difference is the

inclusion of 2004 data by Apple Valley. We have resolved this issue and will include 2004 data in the test year forecast.

Apple Valley requests that the Commission make a specific finding of fact adopting the use of dummy variables as consistent with the intent of the adoption of the New Committee Method in D.04-06-018, the rate case plan decision.[45] It believes that the Commission intended to adopt a common forecasting methodology for sales. Apple Valley's concern is that ORA, or a water company, could opportunistically pick the method that produced a result favoring their interest in any given proceeding and then argue the other method under or over-estimates unit consumption.

ORA's sales forecast witness did not prepare ORA's deficiency notice that required Apple Valley to provide a forecast without dummy variables, but in preparing his testimony he was prepared to accept the applicant's data including dummy variables.[46] He accepted it here "[i]n this particular case for this particular year or set of years, [because] the use of dummy variables provided the better correlation … When you do forecasting, you do various scenarios, various forecasting variables. You try various forecasting variables. And I certainly would try dummies as well as without dummies for comparative purposes."[47]

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[45] A dummy variable is a numerical variable used in regression analysis to represent subgroups of the study sample. Using dummy variables enables a single regression equation to represent multiple groups.

[46] Transcript, p. 147.

[47] Transcript, pp. 149 – 150.

The proper forum to interpret D.04-06-018 is in the rulemaking, or by a Petition to modify the decision, where all interested parties have adequate notice. (See Rule 47.) For our specific purposes in this decision, ORA's witness correctly noted that our objective is to find the best estimate, and, in this case, ORA believes that Apple Valley's use of dummy variables provides the statistical "best correlation." We will only find that for this proceeding, with the available data, the use of dummy variables provided a reasonable forecast for Apple Valley's test year 2006.

For water sales and operating revenues, we will use the five-year average 2000 – 2004, and we will use the data set that includes dummy variables for test year 2006. Unless subsequently clarified, Apple Valley must include two data sets in its next rate case application: one with dummy variables, and another without.

B. Purchased Power

The parties agree on the basic method to estimate purchased power. The estimate is developed from the ratio of recorded power consumption in kilowatt-hours (kWh) and actual water production in hundred-cubic-feet (Ccf) multiplied by the estimated water production in Ccf. Apple Valley and ORA disagree on the time period that should be used to develop the factor of power consumption per water production (kWh/Ccf). Apple Valley's 2006 test year estimate is $1,159,600 using data from June 2003 through May 2004. ORA's estimate used a three-year average, 2002 – 2004.

There are two components to resolve: the kWh/Ccf factor, and the sales estimate, already adopted above.

Apple Valley's position is that averaging is not an appropriate methodology to use when circumstances have changed. Apple Valley's rebuttal

shows that from 2002 to 2004 the kWhs it takes to pump a Ccf of water had increased. This was attributed to the fact "that the pumping levels of the majority of AVR's Wells are dropping."[48] Further, this is caused by localized stress which Apple Valley explained has the effect of lowering the pumping levels of wells.[49]

ORA argues that the aquifer stress is not constant, and it can change from year to year.[50] ORA defends its use of the most recent three-year average as an appropriate indicator of the historical trend.

We have a limited choice of either Apple Valley's weather-affected single season of data, June 2003 – May 2004, or ORA's three-year trend, 2002 – 2004. Using three-years shortens the five-year trend we have identified as the preferred statistical device. We will rely on the most recent three-year trend because Apple Valley has not shown that the single season's significant change is likely to be permanent rather than cyclical, and is not dependent on such as factors as climatic conditions varying from year to year. This three-year trend also includes the recent period that Apple Valley would otherwise use with less dilution of recent data than would occur in a five-year trend.

We have applied the 3 year-average for the production of Apple Valley's wells and energy consumption in kWh/Ccf to the sales/production forecast to derive the 2006 estimated expense of $1,159,200.

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[48] Ex. 17, p. 2.

[49] Transcript, pp. 241 – 242.

[50] Opening brief, p. 5, and citing to Transcript p. 242.

C. Customers Other Expenses

This one issue has been partially resolved elsewhere by adoption of the five-year average method using 2000 – 2004 data. This accounts for $2,631 of the difference. The remaining difference of $30,469 is whether Apple Valley requires additional temporary employees for the customer service department.

Apple Valley argues that customer growth will be approximately 21%, and ORA accepted that growth rate in the test year. Apple Valley believes it will need additional workforce, in the form of temporary rather than permanent employees, to meet this increased workload.[51] We find Apple Valley persuasive that a 21% increase in the number of customers will likely lead to the need for additional workers. We will adopt its forecast for 2006.

D. Insurance – Operating Expense

Apple Valley's forecast for 2006 insurance expenses is based on the actual policy for 2004-2005 policy-year and then adjusted based upon the recommendations of Park's insurance broker for a 2006 estimate of $811,300.[52] ORA's forecast is $705,400, a difference of $105,900, about 13% less.

ORA argues that Apple Valley relies on the "untested hearsay" of its insurance broker, whereas ORA used historical data escalated by the standard CPI-U rates.[53] However, ORA did not cross examine the Apple Valley rebuttal witness on insurance expenses, and did not raise a timely hearsay objection to Apple Valley's asserted advice from its insurance broker. ORA had the

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[51] Apple Valley Opening Brief, p. 7.

[52] Apple Valley Opening Brief, p. 9.

[53] ORA Opening Brief, pp. 10 – 11.

opportunity to pursue discovery on the underlying data used by Apple Valley to forecast 2006 insurance expenses, and we will not sustain any objection now.

The question before us is whether Apple Valley's forecast met the initial burden of proof and whether it is more or less credible than ORA's alternative calculation to escalate 2005 costs by the CPI-U. First, we find that a company the size of Apple Valley most probably needs to rely on brokers, or perhaps competitive bidding, for highly complex and competitive insurance options. That is, we do not expect most water utilities to have in-house insurance experts capable of independently forecasting insurance costs. Apple Valley of course would have to produce in discovery the normal business records and correspondence that the broker created, in offering a 2006 forecast. In rebuttal, Apple Valley demonstrated that 2000 – 2004 recorded insurance expense grew more rapidly than would have been forecast relying on ORA's published CPI-U factors.[54] Thus, we find that ORA's method of escalating 2005 costs by the CPI-U is unlikely to reasonably forecast 2006 expense.

We will adopt Apple Valley's 2006 forecast. We will direct Apple Valley to include in its workpapers for its next general rate case the detailed correspondence, and related requests or instructions to the insurance brokers, to expedite discovery.

E. Insurance – Main Office

The issues before us on main office insurance are identical to the other insurance issues in operating expense. We find that Apple Valley met its burden of proof and offered the most persuasive forecast for test year 2006.

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[54] Ex. 18, p. 2.

F. Gravity Irrigation Rate Design

Apple Valley has a gravity-fed irrigation service that is not connected with the potable water system. There is only one customer on that system and rate schedule – a golf course. Apple Valley has not proposed a cost-based tariff because it believes the customer is a by-pass risk if rates are increased significantly.[55] The requested rate is $0.575/Ccf. Apple Valley asserts that it has not offered a cost study in several recent rate applications.[56]

ORA states it would prefer to formulate its recommendation for gravity irrigation rates on a cost of service study in order to determine the appropriate rates of the gravity irrigation system. But Apple Valley did not prepare a report despite ORA's request.[57] ORA therefore extrapolated utility-wide data to formulate a rate of $0.665/Ccf and a revenue requirement of $226,115.

Without a cost study, we cannot determine with certainty the true cost to serve the gravity irrigation customer, nor any contribution to marginal costs by that customer. We must also consider the credibility of the by-pass threat: whether there are alternative service options and whether they are cost effective if rates were raised to full cost of service.

The Commission has a long-standing practice for energy utilities that allows a special contract rate for customers where there is an immediate threat of bypass, i.e., to leave the utility system. For the energy companies, a series of decisions granted special contract rates subject to certain limitations. In

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[55] Ex. 1, p. 64.

[56] Apple Valley Opening Brief, p. 20 ff.

[57] Transcript, pp. 251, 257

D.92-11-052[58] the Commission adopted an expedited review process to consider approval for special deals that would allow the utility an opportunity to retain a customer who may otherwise depart the system and leave the utility with stranded facilities. The following criteria were established:[59]

1. Bypass should be prevented if it is uneconomic, that is, if the customer's cost to bypass is more than the marginal cost of utility service.

2. Where uneconomic bypass is threatened, it should be possible to offer utility service at a negotiated rate that still contributes to the utility's fixed costs.

3. The utility's marginal cost to serve a customer is the appropriate standard to differentiate economic from uneconomic by pass.

4. The use of LRMCs [long-run marginal cost] as floor rates should ensure that long-term contracts generate a positive contribution to the utility's fixed costs.

Apple Valley failed to meet its burden of proof for gravity-fed rates. It made no evidentiary showing to substantiate a credible threat of bypass. It also failed to substantiate that the existing rate of $0. 575/Ccf is a reasonable anti-bypass rate (assuming a credible threat exists) that would meet any bypass avoidance criteria such as those in D.92-11-052 above.

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[58] 46 CPUC 2d, 444.

[59] 46 CPUC 2d, 444. 449. Conclusions of Law 1, 2, 4, and 10.

Apple Valley may subsequently file a separate application if it can demonstrate that a credible uneconomic bypass threat exists and the bypass avoidance rate covers Apple Valley's marginal costs to serve the customer. The Commission has also spoken on the appropriate standard for review.[60] Apple Valley must show:

1. Imminent customer bypass (customer's sworn affidavit)
2. Bypass would be uneconomic (criterion 3 above)
3. The avoidance rate is reasonable (criteria 2 and 4 above)

We will adopt ORA's rate of $0.665/Ccf as the best available approximation of the cost of service for gravity-irrigation service.

G. Unaccounted for Water

Parties agree that 90% of Apple Valley's unaccounted for water is from its gravity irrigation system. This system consists of a series of reservoirs and pipes that are used to irrigate a golf course and at times operate a trout farm. In its Opening Brief, ORA summarized its proposal as "not requesting heroic measures to reduce this loss but merely a reasonable review of this situation to identify possible low-cost solutions."[61] Apple Valley made a substantial presentation in rebuttal (Ex. 15.) indicating that it operates the system in accordance with its contractual requirements and believes it cannot identify or undertake any cost-effective capital improvements.[62]

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[60] See Conclusion of Law 13, D.92-11-052. The standards above are paraphrased to reflect a "rate" and not necessarily a contract, as was envisioned in that decision.

[61] ORA Opening Brief, p. 20.

[62] Apple Valley Opening Brief pp. 28-29.

ORA essentially asked for information, which Apple Valley should have, and update on a regular basis, to allow a prudent manager to consider possible improvements to the system. Additionally, water should be carefully husbanded and not wasted. We will direct Apple Valley to include a full and complete update of the information in Ex. 15 in its next general rate case. Apple Valley should be prepared to demonstrate that it has specifically reviewed its operations, considered low-cost and no-cost improvements, and perhaps even contract amendments, that could reduce water losses.

H. Pump Efficiency Improvement

ORA suggests that Apple Valley should replace or repair its low-rated pumps to improve pump efficiency.[63] ORA did not brief this issue, although Apple Valley did, in addition to its detailed rebuttal testimony. Apple Valley suggests that its pump efficiencies are typical, and that "it may be more cost effective to repair a high producing well that currently has a fair rating than a low producing well with a low rating." In other words, too simple a replacement requirement might result in uneconomic decisions. We agree, but we also agree with the general premise in ORA's recommendation that Apple Valley should examine its operations on an ongoing basis so that in its next general rate case it can support its overall economic efficiency by proposing those expenditures that provide the greatest long-run benefit to the company and its customers. No further order is required at this time.

[63] Ex. ORA 1, Page 3-8

15. Infrastructure Improvement Act

Apple Valley was required by D.04-06-018 to demonstrate that it was in compliance with the Infrastructure Improvement Act (Infrastructure Act).[64] In its application, Apple Valley indicates it determined in September 2004, that three pump lots with a total original cost of $7,188.06 were no longer used and useful, and they were removed from plant in service. Although ORA made no specific comment on the matter in testimony or briefs, the test year 2006 rate base reflects this adjustment.

Apple Valley is expected continue to account for the accrual of interest as prescribed in § 790(a) and hold the proceeds available for future investment whenever it sells or transfers the three parcels. No further action is required for this proceeding. Apple Valley must also include in subsequent rate cases a

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[64] "To the extent not included in a previous GRC application, include a detailed, complete description accounting for all real property that, since January 1, 1996, was at any time, but is no longer, necessary or useful in the performance of the water corporation's duties to the public and explain what, if any, disposition or use has been made of said property since it was determined to no longer by used or useful in the performance of utility duties. The disposition of any proceeds shall also be explained." (D. 04-06-018, Attachment A, p. 10.) *See* also § § 789 – 790.1, especially § 790.(a): "Whenever a water corporation sells any real property that was at any time, but is no longer, necessary or useful in the performance of the water corporation's duties to the public, the water corporation shall invest the net proceeds, if any, including interest at the rate that the commission prescribes for memorandum accounts, from the sale in water system infrastructure, plant, facilities, and properties that are necessary or useful in the performance of its duties to the public. For purposes of tracking the net proceeds and their investment, the water corporation shall maintain records necessary to document the investment of the net proceeds pursuant to this article. The amount of the net proceeds shall be a water corporation's primary source of capital for investment in utility infrastructure, plant, facilities, and properties that are necessary or useful in the performance of the water corporation's duties in providing water utility service to the public."

report on the specific disposition of any assets in the 2006 rate base that are deemed to be no longer used and useful for the next test year.

16. Justification of Back-up Generators

Apple Valley was required by D.03-08-069 to justify its need for and investment in backup generators used to provide additional power to supplement its pumping capacity at various locations. The issue was carried forward with an expectation that ORA would have the time in this proceeding to examine the data and decide whether there were issues of note to bring before the Commission.

ORA expressed concern that Apple Valley had acquired several back-up generators because of power interruptions or the avoidance of supply disruptions because of power interruptions. Apple Valley demonstrated that it has the generators to augment pumping, and they are only incidentally available in the event of infrequent disruptions.[65]

> We have the generators for two primary reasons. One is to save the costs that we would have associated with adding storage for emergency supply. What I mean by that is without our generators, we would have to have much more elevated storage to supply our water system for various reasons, such as power outages. [Secondly] We also are able to keep our system supplied with water when we have localized problems due to power.

We are satisfied that Apple Valley has a reasonable need for the backup generators, and thus that they are used and useful in providing utility service. Nevertheless, Apple Valley should continue the reports to track the use of the

[65] Transcript, p. 222.

back-up generators and should include them in the work papers of the next rate case.

17. Comments on the Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311(d) Pub. Util. Code and Rule 77.1 of the Rules of Practice and Procedure. Comments were filed _____ and reply comments were filed _____.

18. Assignment of Proceedings

Dian M. Grueneich is the Assigned Commissioner and Douglas Long is the assigned ALJ in this proceeding. (*See* Rule 5(l).)

Findings of Fact

1. Apple Valley, a water public utility under context of Pub. Util. Code § 216, is subject to the jurisdiction, control, and regulation of this Commission.

2. Apple Valley is a wholly owned subsidiary of Park, and provides public utility water service in and adjacent to the Town of Apple Valley.

Escalation

3. The rate case plan for Class A water companies, D.04-06-018, adopted the "Estimates of Non-Labor and Wage Escalation Rates", the "Summary of Compensation per Hour", and for any item that may not be covered by these factors, the most recent 12-month "US Cities CPI-U" to escalate recorded cost trends in the test year. These data are published by ORA. It is reasonable to use these most recent factors to forecast test year 2006.

Cost of Capital

4. It is reasonable to adopt the uncontested forecast capital structure of 42.33% debt and 57.67% equity for all three years, 2006 – 2008, and the

uncontested weighted average cost of debt of 8.49%, 8.41% and 8.35%, respectively.

5. Apple Valley has not demonstrated that its risk profile warrants a 90 basis point adder to the otherwise reasonable range for return on equity in the test year and escalation years. Apple Valley has not demonstrated that the return comparisons for natural gas distribution utilities are probative of the appropriate return on equity for a Class-A water utility.

6. ORA stipulated to an updated calculation of its recommendation of 9.85% return on equity. With a 30-point adder the 10.15% return on equity is 13 points above the recent settled average of 10.02%.

Rate Base

7. Apple Valley justified an increase in plant in service for 2006 and 2007 of approximately $6.7 million and $5.7 million, respectively. This includes three wells forecast to cost $3.485 million.

8. Rule 15, Main Extensions, allows Apple Valley to charge developers or other new customers a fee to reimburse the cost of extending service from the existing system. Depending on the circumstances, these fees may be either a non-refundable contribution to Apple Valley or a refundable advance subject to certain conditions. Wells are not specifically included in the list of facilities itemized in Rule 15.

9. Apple Valley and ORA stipulated to a 75/25 split of the costs for these new wells between new customers and existing customers. Under the stipulation 75% of the costs will only be recovered by a facilities charge on developments of 5 of or more connections and only 25% will be included in rate base. The stipulation is a reasonable allocation of the costs and benefits between new and existing customers. It is also reasonable to require Apple Valley to

monitor all new connections and count all connections by an individual or entity within an 18-month period against the 5 unit exemption.

10. Apple Valley and ORA stipulated to installing an average of 80 new standpipes during 2005 – 2007 (and the associated revenue requirement) to enhance system reliability and safety.

11. Apple Valley should refund the revenue requirement of any uninstalled standpipes. The refund should be reflected as a reduction of revenue requirements in its next rate case.

Working Cash

12. Depreciation expense is reasonably included in the working cash study as calculated using Standard Practice U-16. D.04-09-061 does not contain findings or conclusions of law to support ORA's interpretation that the Commission intended to modify its longstanding practice and exclude depreciation expense from the working cash calculation.

Five Year Average Forecast

13. Apple Valley updated its record period to use a five-year average for 2000 - 2004. This is consistent with the intention of the rate case plan.

Low-Income Program

14. A $2.27 monthly reallocation to non-recipients for a $5 monthly low-income ratepayer benefit is consistent with the San Gabriel low-income ratepayer assistance program authorized in D.05-05-015 that reallocated $2.32 per month to non-recipients for a $4.88 benefit.

15. By establishing a CARW Revenue Reallocation Balancing Account and a CAWR Implementation Cost Memorandum Account, Apple Valley will have a reasonable opportunity to recover the actual amount of discounts received by CARW customers and insure that non-recipient customers do not over- or under-compensate Apple Valley for its actual costs to implement and maintain the

program. A revenue balancing account, adjusted annually, is reasonable to recover the actual costs of the $5 per month discount given to eligible customers. An expense memorandum account is appropriate for the uncertain reasonable costs to implement the program. A reasonableness review in the next general rate case will ensure that Apple Valley prudently manages the costs of the program.

16. It is reasonable for Apple Valley to apply the annual income limitations as published annually by the Commission's Energy Division in compliance with Resolution E-3524.

Sales Forecast

17. With the available data, the use of dummy variables provided a reasonable sale forecast for Apple Valley's test year 2006.

Insurance

18. Based upon the 2004 – 2005 policy-year, and as adjusted by the insurance broker's forecast, Apple Valley reasonably forecast insurance costs for 2006 for its utility and main office operations.

Gravity Feed

19. Apple Valley did not meet its burden of proof to justify continuing the proposed gravity feed service rates. ORA made a best efforts calculation of a cost of service for gravity feed service of $0.655/Ccf and a revenue requirement of $226,115.

20. There was no persuasive evidence that Apple Valley faces a credible risk of uneconomic bypass that would justify a bypass avoidance rate below marginal cost.

21. Apple Valley does not face uneconomic bypass by its gravity feed service customer and cannot offer service below cost.

Unaccounted for Water

22. It is reasonable to expect a prudent manager to consider possible improvements to the system and make low-cost and no cost improvements. Apple Valley should include a full and complete up-date of the information in Ex. 15 in its next general rate case.

Pumping Efficiency

23. Apple Valley demonstrated that its current maintenance of pumping efficiency is reasonable. Apple Valley should examine its pumping operations on an ongoing basis so that in its next general rate case it can support its overall economic efficiency by proposing those expenditures that provide the greatest long-run benefit to the company and its customers.

Infrastructure Act

24. Apple Valley is in compliance with the Infrastructure Act and reported the removal of three land parcels from rate base.

Back-up Generators

25. Apple Valley demonstrated that it has back-up generators to augment pumping, and they are only incidentally available in the event of infrequent electric service disruptions.

Conclusions of Law

1. Apple Valley's rates as modified and authorized today are reasonable.

2. In order to provide fair and equitable rate treatment for existing customers it is reasonable to exclude from rate base the costs of new wells that are necessary to serve new customers, since their inclusion in rate base would require existing customers to subsidize the connection of new customers.

3. Apple Valley should impose on an individual or corporation or other entity a $1,000 fee per connection, for six or more new connections in an 18-month period, to pay for new facilities necessary to provide service.

4. Apple Valley should refund $2,050 per water standpipe for any unspent revenue requirement intended to be used to install 240 standpipes in 2005 through 2007.

5. Apple Valley's working cash calculation was made in conformance with Standard Practice U-16.

6. Apple Valley should establish a low-income ratepayer assistance program, known as CARW, as contemplated by Pub. Util. Code § 739.8.

7. It is necessary and reasonable and within our authority under § § 701 and 739.8 to establish a CAWR Revenue Reallocation Balancing Account and a CAWR Implementation Cost Memorandum Account to track and recover the reasonable costs of a low-income ratepayer assistance program.

8. Today's decision should be made effective immediately.

O R D E R

IT IS ORDERED that:

1. Apple Valley Ranchos Water Company (Apple Valley) is authorized to file by advice letter the revised schedules attached to this order as Appendices A - D, and to concurrently cancel its present schedules for such service. This filing shall comply with General Order (GO) 96 and be approved by the Commission's Water Branch. The effective date of the revised schedule shall be January 1, 2006 and apply only to service rendered on or after this effective date.

2. Apple Valley shall file an advice letter to modify its Rule 15 to add a special facilities fee as discussed in this decision. The fee shall apply to every connection by all individuals or entities that apply for more than five connections in an 18-month period.

3. If Apple Valley installs less than 240 new standpipes in the three-year period 2005 though 2007, it shall refund to ratepayers $2,050 for each shortfall in standpipes. The refund shall be a reduction to the revenue requirement in Apple Valley's next general rate case.

4. Apple Valley shall establish a low-incomes ratepayer assistance program, known as California Alternative Rates for Water (CARW), in conformance with Pub. Util. Code § 739.8. As authorized in this decision, Apple Valley shall file a tariff for CARW by advice letter.

5. Apple Valley shall establish by advice letter a CARW Revenue Reallocation Balancing Account to recover the differential in revenues for actual low-income assistance discounts. Apple Valley may recover the balance as a revenue adjustment in its 2007 and 2008 escalation year advice letter filings as a revenue adjustment.

6. Apple Valley shall establish by advice letter a CAWR Implementation Cost Memorandum Account to recover its reasonable costs to implement the CAWR program. Apple Valley shall include the memorandum account balance for recovery in its next general rate case.

7. Apple Valley shall develop a customer information program, subject to approval by the Commission's Public Advisor, to inform ratepayers of the CAWR low-income assistance program. Apple Valley shall inform all customers of the program in every billing cycle for the first twelve months following the effective date of this decision.

8. Apple Valley shall include a full and complete up-date of the information on unaccounted for water in its next general rate case.

9. Apple Valley shall include in its next general rate case a complete report on any items in the 2006 rate base that are no longer deemed used and useful.

10. Application 05-02-005 is closed.

This order is effective today.

Dated _____, at San Francisco, California.

APPENDIX A
1 of 1
APPLE VALLEY RANCHOS WATER CO.
TEST YEAR 2006
SUMMARY OF EARNINGS
(Dollars In Thousands)

	PRESENT RATES	AT AUTHORIZED RATE OF RETURN
OPERATING REVENUES	14,956.8	16,538.9
DEFERRED REVENUES	(0.5)	(0.5)
TOTAL REVENUES	14,957.3	16,539.4
OPERATIONS & MAINTENANCE		
PAYROLL-OPERATIONS	575.1	575.1
OPERATIONS-OTHER	205.5	205.5
PURCHASED WATER	0.0	0.0
PURCHASED POWER	1,159.2	1,159.2
LEASED WATER RIGHTS	810.8	810.8
REPLENISHMENT CHARGES	306.2	306.2
CHEMICALS	25.2	25.2
PAYROLL-CUSTOMER	355.5	355.5
CUSTOMERS-OTHER	200.9	200.9
UNCOLLECTIBLES .32%	47.9	52.9
PAYROLL-MAINTENANCE	332.6	332.6
MAINTENANCE-OTHER	773.5	773.5
PAYROLL-CLEARINGS	79.4	79.4
CLEARINGS-OTHER	304.0	304.0
SUBTOTAL O & M	5,175.8	5,180.9
ADMINISTRATIVE & GENERAL		
PAYROLL	972.8	972.8
PAYROLL-BENEFITS	731.6	731.6
INSURANCE	811.3	811.3
UNINSURED PROP. DAMAGE	4.2	4.2
REG. COMM. EXPENSE	54.2	54.2
FRANCHISE REQUIREMENTS 1.00%	149.6	165.4
OUTSIDE SERVICES	195.9	195.9
OFFICE SUPPLIES	387.1	387.1
A & G TRANSFERRED	(270.6)	(270.6)
MISCELLANEOUS	29.7	29.7
RENTS	2.4	2.4
MAIN OFFICE ALLOCATION (1)		
A & G EXPENSES	1,242.3	1,242.3
DATA PROCESSING	0.0	0.0
SUBTOTAL A & G	4,310.5	4,326.3
AD VALOREM TAXES (1)	331.4	331.4
PAYROLL TAXES (1)	210.1	210.1
RECOVER UNDERCOLLECTION		
DEPRECIATION (1)	1,749.7	1,749.7
CA INCOME TAX	177.6	315.6
FEDERAL INCOME TAXES	673.7	1,204.4
TOTAL EXPENSE	12,628.7	13,318.5
NET REVENUES	2,328.5	3,220.9
RATE BASE	34,081.8	34,081.8
RATE OF RETURN	6.83%	9.45%

(1)DEPRECIATION, AD VALOREM AND PAYROLL TAXES FROM PARK'S MAIN OFFICE HAVE BEEN INCLUDED IN THE APPROPRIATE LINE ITEM OF EXPENSE.

(END OF APPENDIX A)

APPENDIX B

APPLE VALLEY RANCHOS WATER COMPANY

Schedule No. 1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Town of Apple Valley and vicinity, San Bernardino County.

RATES

Quantity Rate:

	Per Meter Bimonthly (Every Two Month) 2006
Per 100 cu. ft.	$ 1.557

Service Charge:

For 5/8 x 3/4-inch meter	$ 20.94
For 3/4-inch meter	31.45
For 1-inch meter	52.35
For 1 1/2-inch meter	104.70
For 2-inch meter	167.55
For 3-inch meter	314.10
For 4-inch meter	523.50
For 6-inch meter	1,047.00
For 8-inch meter	1,675.20
For 10-inch meter	2,408.10

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the bimonthly charge computed at the Quantity Rates.

SPECIAL CONDITIONS

1. A late charge will be imposed per Schedule LC.
2. In accordance with Section 2714 of the Public Utilities Code, if a tenant in a rental unit leaves owing the company, service to subsequent tenants in that unit will, at the company's option, be furnished on the account of the landlord or property owner.
3. All bills are subject to the Public Utilities Commission Reimbursement Fee set forth on Schedule No. UF.

APPENDIX B

Page 2 of 6

APPLE VALLEY RANCHOS WATER COMPANY

Schedule No. 2

GRAVITY IRRIGATION SERVICE

APPLICABILITY

Applicable to all water service from the Company's gravity irrigation system.

TERRITORY

Within the entire service area of the Company.

RATES

Quantity Rate:

	Per Meter Per Month 2006
Per 100 cu. ft.	$ 0.665
Service Charge:	
For 5/8 x 3/4-inch meter	$ 20.94
For 3/4-inch meter	31.45
For 1-inch meter	52.35
For 1 1/2-inch meter	104.70
For 2-inch meter	167.55
For 3-inch meter	314.10
For 4-inch meter	523.50
For 6-inch meter	1,047.00
For 8-inch meter	1,675.20
For 10-inch meter	2,408.10

SPECIAL CONDITIONS

1. Service under this schedule is limited to lands not developed for residential use.

2. All outlets for this water shall be protected by signs stating: NON-POTABLE WATER – NOT FOR HUMAN CONSUMPTION.

3. A late charge will be imposed per Schedule No. LC.

4. All bills are subject to the Public Utilities Commission Reimbursement Fee set forth on Schedule #UF.

APPENDIX B

APPLE VALLEY RANCHOS WATER COMPANY

Schedule No. 4

NON-METERED FIRE SERVICE

APPLICABILITY

Applicable only for water service to privately owned fire hydrants and fire sprinkler systems where water is to be used only for the purpose of fire suppression or for periodic system testing.

TERRITORY

Town of Apple Valley and vicinity, San Bernardino County.

RATES

Size of Service	Per Service Per Month 2006
2-inch	$ 24.40
3-inch	36.60
4-inch	48.75
6-inch	73.10
8-inch	97.50
10-inch	117.70

SPECIAL CONDITIONS

1. The fire protection service connection shall be installed by the utility at the cost paid by the applicant. Such payment shall not be subject to refund.
2. The minimum diameter for fire protection service shall be two (2) inches, and the maximum diameter shall be not more than the diameter of the main to which the service is connected.
3. If a distribution main of adequate size to serve a private fire protection system in addition to all other normal service does not exist in the street or alley adjacent to the premises to be served, then a service main from the nearest main of adequate capacity shall be installed by the utility and the cost paid by the applicant. Such payment shall not be subject to refund.

APPENDIX B

APPLE VALLEY RANCHOS WATER COMPANY

A. Schedule No. 4

NON-METERED FIRE SERVICE

(Continued)

4. Service hereunder is for private fire systems which are regularly inspected by the local fire protection agency having jurisdiction and to which no connections for other than fire suppression purposes shall be made. Service shall be installed according to specifications of the utility and shall be maintained to the satisfaction of the utility. The utility will install the detector meter listed by the Underwriters Laboratories, Inc. or other device to indicate unauthorized use, leakage, or waste of water. The cost of such installation and the cost of the meter or other device shall be paid by the applicant.

5. The utility undertakes to supply water only at such pressures as may be available at any time through the normal operation of its system.

6. Any unauthorized use of water, other than for fire extinguishing purposes, shall be charged for at the regular established rate as set forth under Schedule No.1, and/or may be the grounds for the immediate disconnection of the service without liability to the Company.

7. A late charge will be imposed per Schedule No. LC.

8. All bills subject to the reimbursement fee set forth on Schedule No. UF.

APPENDIX B

APPLE VALLEY RANCHOS WATER COMPANY

Schedule No. LC

LATE PAYMENT CHARGE

APPLICABILITY

Applicable to all service.

TERRITORY

Within the entire service area of the Company.

RATES

Late Charge: A late charge of 1.5% on unpaid balance subject to special conditions and minimum charge below:

Minimum Charge: The minimum charge is $1.00

SPECIAL CONDITIONS

1. The balance is unpaid and subject to a late charge if the bill is Past-Due, or delinquent, as defined in Rule No. 11, Section B.1.a.

2. The late charge should be imposed only once on a delinquent bill since the account would be shut off before a subsequent bill and then subject to the reconnection fee as authorized by Tariff Rule No. 11.

3. All bills shall be subject to the reimbursement fee as set forth on Schedule No. UF.

APPENDIX B

APPLE VALLEY RANCHOS WATER COMPANY

Schedule No. UF

SURCHARGE TO FUND

PUBLIC UTILITIES COMMISSION

REIMBURSEMENT FEE

APPLICABILITY

This surcharge applies to all water and sewer bills rendered under all tariff rate schedules authorized by the Commission, with the exception of resale rate schedules where the customer is a public utility.

TERRITORY

This schedule is applicable within the entire territory served by the utility.

RATES

A 1.4% (.014) surcharge shall be added to all customer bills.

In 1982, the Legislature established the Public Utilities Commission Reimbursement Fee to be paid by utilities to fund their regulation by the Commission (Public Utilities (PU) Code Section 401-443). The surcharge to recover the cost of that fee is ordered by the Commission under authority granted by the PU Code Section 433.

(END OF APPENDIX B)

APPENDIX C
APPLE VALLEY RANCHOS WATER COMPANY
COMPARISON OF RATES
TEST YEAR 2006

USAGE	PRESENT	ADOPTED	INCREASE	PERCENT
0	19.98	20.94	0.96	4.80%
10	33.42	36.58	3.16	9.46%
20	46.86	52.22	5.36	11.44%
24 AVG	52.24	58.48	6.24	11.95%
30	60.30	67.86	7.56	12.54%
50	87.18	99.14	11.96	13.72%

Note: Based on Monthly Charges According to Schedule No. 1
Metered Comparison based on 5/8 x 3/4-inch meter
Rates do not include CPUC fees or surcharges that may appear on customer bills

(END OF APPENDIX C)

APPENDIX D
Page 1 of 6
APPLE VALLEY RANCHOS WATER COMPANY
ADOPTED QUANTITIES

Apple Valley Ranchos Water Company - Domestic

Net-to-Gross Multiplier	1.7728
Uncollectible Rate	0.32%
Franchise Fee	0.9979%
Federal Tax Rate	34.00%
State Tax Rate	8.84%
	2006
Water Consumption (KCcf)	
Domestic Water Sales	6,594.3
Unaccounted Water (10%)	732.7
Total Water Production	7,327.1
Replenishment Charges	
Make-up 2,286 AF@ $100/AF	$228,600
Adminstrative 16,821 AF @$2.93/AF	$49,286
Biological 16,821 AF @$0.64/AF	$10,765
Total Replenishment Cost	$288,651
Leased Water Rights	
6,486 AF @$125/AF	$810,750
Purchased Power	
Electric	
Cost	$1,057,366
Kilowatt Hours	12,811,353
Cost/Kilowatt Hour	$0.082534
Gas	
Cost	$25,433
Therms	37,518
Cost/Therm	$0.677888
Water Consumption (Ccf/Customer)	
Residential	284.3
Business	840.0
Industrial	551.0
Public Authority	7,770.0
Private Fire Service	6.0
Public Authority Irrigation	6,376.0
Pressure Irrigation	2,148.0
Temporary Construction	2,492.0

APPENDIX D
Page 2 of 6
APPLE VALLEY RANCHOS WATER COMPANY
ADOPTED QUANTITIES

Apple Valley Ranchos Water Company - Irrigation

Net-to-Gross Multiplier	1.7728
Uncollectible Rate	0.32%
Franchise Fee	0.9979%
Federal Tax Rate	34.00%
State Tax Rate	8.84%
	2006
Water Consumption (Ccf)	
Water Sales	285,210
Unaccounted Water (89.3%)	2,481,286.0
Total Water Production	2,766,496.0
Replenishment Charges	
Make-up 98 AF @ $140/AF	$13,720
Adminstrative ($0.00/AF)	$0
Biological 6,119 AF @$0.63/AF	$3,855
Total Replenishment Cost	$17,575
Purchased Power	
Electric	
Cost	$74,078
Kilowatt Hours	1,061,141
Cost/Kilowatt Hour	$0.069810
Water Consumption (Ccf/Customer)	
Gravity Irrigation	285,210.0

APPENDIX D
Page 3 of 6
APPLE VALLEY RANCHOS WATER COMPANY
ADOPTED QUANTITIES

Apple Valley Ranchos Water Company
Utility Plant In Service
(Dollars in Thousands)

Utility Plant In Service	2006	2007
Beginning Of Year Balance	65,469.0	70,079.0
Additions	5,002.0	5,394.3
Retirements	392.1	403.8
End Of Year Balance	70,079.0	75,069.4
Average Balance	67,774.0	72,574.2

Apple Valley Ranchos Water Company
Depreciation Reserve
(Dollars in Thousands)

Depreciation Reserve	2006	2007
Beginning Of Year Balance	14,246.6	15,623.1
Annual Accrual	1,757.1	1,902.7
Net Retirements	380.6	392.0
End Of Year Balance	15,623.1	17,133.8
Average Balance	14,934.8	16,378.5

APPENDIX D
Page 4 of 6
APPLE VALLEY RANCHOS WATER COMPANY
ADOPTED QUANTITIES

Adopted Rate Base Summary
(Dollars in Thousands)

	2006	2007
AVERAGE BALANCES		
PLANT IN SERVICE	67,774.0	72,574.2
WORK IN PROGRESS	0.0	350.0
MATERIALS & SUPPLIES	173.8	173.8
WORKING CASH	407.7	439.9
SUBTOTAL	68,355.4	73,537.9
LESS:		
DEPRECIATION RESERVE	14,934.8	16,378.5
ADVANCES	13,028.8	15,404.6
CONTRIBUTIONS	1,633.3	1,603.7
UNAMORTIZED ITC	90.4	85.6
DEFERRED INCOME TAX	5,501.5	5,753.8
SUBTOTAL	35,188.9	39,226.2
PLUS:		
METHOD 5 ADJUSTMENT	17.9	13.1
NET DISTRICT RATE BASE	33,184.4	34,324.8
MAIN OFFICE ALLOCATION	897.5	804.5
TOTAL RATE BASE	34,081.8	35,129.3

APPENDIX D
Page 5 of 6
APPLE VALLEY RANCHOS WATER COMPANY
ADOPTED QUANTITIES

Adopted Income Tax Calculations
(Dollars in Thousands)

	2006
OPERATING REVENUES	16,539.4
EXPENSES	
OPERATIONS & MAINTENANCE	5,128.0
UNCOLLECTIBLES .46%	52.9
ADMINISTRATIVE & GENERAL	4,160.9
FRANCHISE FEES 1.05%	165.4
AD VALOREM TAXES	331.4
PAYROLL TAXES	210.1
MEALS ADJUSTMENT	-8.5
SUBTOTAL	10,040.3
DEDUCTIONS	
CA TAX DEPRECIATION	1,705.9
INTEREST	1,223.5
CA TAXABLE INCOME	3,569.7
CCFT @ 8.84%	315.6
DEDUCTIONS	
FED. TAX DEPRECIATION	1,553.4
INTEREST	1,223.5
CA TAX	177.5
FIT TAXABLE INCOME	3,544.6
FIT (BEFORE ADJUSTMENT) 34.00%	1,205.2
PRORATED ADJUSTMENT	
INVESTMENT TAX CREDIT	-0.7
NET FEDERAL INCOME TAX	1,204.5

APPENDIX D
Page 6 of 6
APPLE VALLEY RANCHOS WATER COMPANY
ADOPTED QUANTITIES

	2006	2007	2008
Number of Customers			
Residential	17,757	18,857	19,757
Business	1,199	1,215	1,231
Public Authority	40	41	41
Industrial	2	2	2
Temporary Construction	22	22	22
Pressure Irrigation	65	65	65
Gravity Irrigation	1	1	1
Public Authority Irrigation	5	5	5
Private Fire	108	113	118
Total	19,199	20,321	21,242

(END OF APPENDIX D)