

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Order Instituting Investigation to Consider Policies to Achieve the Commission's Conservation Objectives for Class A Water Utilities.

FILED  
PUBLIC UTILITIES COMMISSION  
JANUARY 11, 2007  
SAN FRANCISCO, CALIFORNIA  
INVESTIGATION 07-01-022

**ORDER INSTITUTING INVESTIGATION TO CONSIDER POLICIES TO  
ACHIEVE THE COMMISSION'S CONSERVATION OBJECTIVES FOR CLASS  
A WATER UTILITIES**

By this order, we initiate an investigation to address policies to achieve the Commission's conservation objectives for Class A water utilities by requesting comments on increasing block rates, water revenue adjustment mechanisms, rebates and customer education, conservation memorandum accounts, and rationing programs. We also consolidate pending conservation rate design applications to set rates and adopt mechanisms and programs in accordance with policies adopted in this proceeding. A prehearing conference is set for February 7, 2007 to address the tentative schedule for this proceeding.

**1. Background**

The Commission's December 15, 2005 Water Action Plan (WAP) adopted the principle of efficient use of water and the objective of strengthening water conservation programs to a level comparable to those of energy utilities. In addition, the California Department of Water Resources (DWR) has recommended that California invest in reliable, high quality, sustainable, and affordable water conservation, efficient water management, and development of

water supplies to protect public health and improve California's economy, environment, and standard of living. (California Water Plan Update 255, Vol. 1, 2-4.)

Four applications to adopt conservation rate design programs for residential customers have been filed in response to Commission directives. Golden State Water Company (GSWC) filed Application (A.) 06-09-006 to adopt an increasing block rate design, a water revenue adjustment mechanism (WRAM), and a water shortage allocation policy to be established in advance of a drought situation. California Water Service Company (CalWater) filed A.06-10-026 to implement increasing block rates, a conservation memorandum account, and a WRAM for its 24 districts. Park Water Company (Park) filed A.06-11-009 to implement a WRAM, an increasing block rate design, and a conservation memorandum account. Suburban Water Systems (Suburban) filed A.06-11-010 to implement a low-income assistance program, an increasing block rate design that includes a price elasticity factor, and a WRAM.

## **2. Investigation on Conservation Issues**

We commence this companion investigation to the applications described above to allow the Commission to hear proposals other than those set forth in the individual applications, and to enable the Commission to enter orders on matters for which the utility may not be the proponent. The investigation will be consolidated and heard on a consolidated evidentiary record with A.06-09-006, A.06-10-026, A06-11-009, and A.06-11-010. The investigation will afford parties, and this Commission, an opportunity and forum to provide and consider evidence on similar issues of interest raised by the applications. GSWC, CalWater, Park, and Suburban are hereby placed on notice that the evidence taken in these consolidated proceedings may be the basis for findings and

Commission orders. Accordingly, the Commission commences this investigation to study and address overarching conservation policy issues raised by the filed applications, including increasing block rate design, WRAM design, conservation memorandum accounts, and water shortage allocation policy.

Subsequent applications raising similar issues that are filed by other Class A water utilities may also be consolidated with this proceeding. We will examine other issues, discussed below, to promote the WAP's conservation objectives. Initially, we solicit comments from interested parties on conservation issues. After issuing a decision on these broad policy issues, we anticipate (a) authorizing individual companies to file appropriate advice letters to implement authorized conservation measures, including rate design; or (b) scheduling any necessary proceedings (either in this investigation or in the individual applications) to implement in a decision conservation measures, including rate designs, for individual companies. Below we describe the issues we will consider in our initial policy decision and specific questions on which we require input.

### **2.1. Conservation Rate Design**

The WAP found there was an increasing use of conservation rate designs in California. In 2003, approximately half of California's water ratepayers had increasing block rates. However, almost no water utilities regulated by the Commission used this rate design. (WAP, pp. 8-9.) The WAP supported adoption of increasing block rates where feasible and recognized the need to consider the impact of increasing block rates on low-income customers.

The WAP encourages development and implementation of best conservation management practices as promoted by the California Urban Water Conservation Council (Council) and directs Class A and B Water Utilities to

participate in the Council. One best management practice is conservation pricing (BMP11). The Council is considering revisions to the existing BMP11.<sup>1</sup> The revised BMP 11 states that conservation pricing provides economic incentives (a price signal) to customers to use water efficiently. Uniform rates, seasonal rates, tiered rates, and allocation-based rates potentially are consistent with that definition of conservation pricing. Unmetered water service is inconsistent with conservation pricing.

In order to implement increasing block rates for Class A Water Utilities, we must determine whether certain conditions must be met prior to adopting increasing block rates, as follows:

- Should the company have a low-income assistance program?
- Should the company provide metered service for a major portion or for all of its customers?
- Should the company provide monthly bills?

We need to determine how we will implement increasing block rates. GSWC, CalWater, Park, and Suburban have filed applications for increasing block rates for their residential customer classes, because conservation rate designs for other customer classes are more complex. The proposals incorporate two- and three- rate tiers and first tier caps also vary. No company has raised the issue of a “baseline” water allowance for the first tier, comparable to the baseline quantities in place for residential gas and electric customers. The gas and electric baseline allowances are those necessary to supply a significant portion or the reasonable energy needs of the average residential customer. (Pub. Util. Code

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<sup>1</sup> [http://www.cuwcc.org/uploads/hotnews/BMP11\\_Revision\\_07-011-03.pdf](http://www.cuwcc.org/uploads/hotnews/BMP11_Revision_07-011-03.pdf)

§ 739(a).) Energy utilities have seasonal baseline usage allowances. We have the authority, in implementing rate relief and conservation incentives for low-income ratepayers, to take into account water needs caused by geography, climate, and the ability of communities to support these programs. (Pub. Util. Code § 739(8).) To implement increasing block rates we need to consider the following:

- Should there be a uniform number of rate tiers? What percentage increase in rates between tiers would most effectively promote conservation? Should they be seasonal? If cost differences within districts are substantial, should the rate tiers within that district vary? What percentage would constitute a substantial difference?
- What should the usage allowance be for the first tier? Should it be seasonal? Should it be set by geographic area? How should it be established?
- Will seasonal rates (*i.e.*, higher uniform rates during summer months) be adequate in districts or for particular customer classes (*e.g.*, commercial and industrial) where increasing block rates are overly burdensome to administer?
- Should the Commission consider increasing block rates for other customer classes in this investigation after the Commission has adopted increasing block rates for residential customers?

Conservation programs will decrease usage. One means of directly addressing declining consumption is incorporating a price elasticity factor into rate design to address the impact on usage changes resulting from new rate designs and the adoption of other water conservation measures. We will solicit comments, as follows:

- Should elasticity of demand be calculated? If yes, what methodology should be used?
- If elasticity of demand is calculated, should it be used to determine the appropriate tiers for increasing block rates?

## **2.2. Water Revenue Adjustment Mechanism**

The WAP recognizes that current ratesetting mechanisms provide a disincentive to conservation and supports removing those disincentives. Revenues after adoption of increasing block rates can be lower or higher than the utilities' adopted revenue requirement. A WRAM is a balancing account designed to decouple sales from revenues. Adoption of a WRAM will ensure collected revenues are adjusted to match the adopted revenue requirement and may remove one disincentive to conservation. Amortization of the WRAM through surcharges or surcredits will be necessary.

Class A water companies have other ratemaking constraints. They currently recover 50% of fixed costs in a service charge. (Water Division's Standard Practice (SP) U-07-W.) Those fixed costs are obtained by subtracting variable costs from revenue requirement.<sup>2</sup> Service charges, if set too high, can lessen the impact of increasing block rates.

To remove disincentives to conservation:

- What methodology for a WRAM should be adopted? Should all revenue fall under a WRAM or just some subset?
- Should surcharges/surcredits be amortized in conformance with SP-U-27-W?
- Should the Commission change its policy of permitting recovery of 50% of fixed costs in a service charge?

## **2.3. Rebates, Customer Education, and Excessive Consumption**

Rebates and customer education are proven means to increase conservation. The WAP supports improving customer education on water

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<sup>2</sup> Variable costs include purchased power, purchased water, chemicals, income taxes, uncollectibles and other costs that vary with usage.

conservation, including providing more information on the Commission's website. The Family of Southern California Water Agencies, an umbrella organization that comprises water districts which include customers of Class A water utilities, has extensive customer education programs and offers rebates for ultra low flush toilets and water conserving appliances with water utilities and districts. California-American Water Company has achieved substantial water savings in its Monterey district through a number of means, including rebates and customer education. Because water conservation efforts can be most effective initially and can decline over time, we will consider methods other than increasing block rates to encourage conservation, as follows:

- What customer education should utilities provide to encourage conservation?
- Should utilities be required to participate in or provide rebate programs, including ultra low flush toilets and water conserving appliances?
- Should utilities be required to provide conservation kits and landscaping water audits to residential customers?

Despite best efforts to promote conservation, some customers may fail to conserve. In those instances, more drastic measures may be necessary:

- How can excessive consumption be defined? Should it be established in a manner consistent with establishing baseline usage?
- Should customers with excessive water consumption be penalized in some way?
- What measures should utilities take to penalize those customers?

#### **2.4. Conservation Management and Memorandum Accounts**

Conservation programs have costs. Another best management practice promoted by the Council is system water audits and leak detection (BMP3). The Council currently is considering revising the existing BMP 3, which is outdated,

and shifting to a new water loss audit methodology developed by the American Water Works Association (AWWA) and the International Water Association (IWA).

- Should Class A utilities be required to perform and submit the results of a water loss audit to the Commission, using the free Water Audit Software developed by the AWWA?<sup>3</sup>

Adoption of best conservation management practices could result in unanticipated costs. Measures adopted in this investigation also may have costs. Most of these costs will not have been included in authorized rates. We will consider authorizing memorandum accounts, as follows:

- Should utilities track costs of best management practices in a conservation memorandum account?
- Should utilities track costs to implement any customer education or rebate programs required by this investigation?

## **2.5. Rationing**

Companies have requested guidance on rationing during droughts. Currently, Water Division's SP U-40-W discusses three levels of action – voluntary rationing, mandatory rationing and a service connection moratorium. Voluntary rationing is addressed in Rule 14.1, which is always in effect. (SP U-40-W, Appendix B.) Mandatory rationing is addressed in a company's Schedule 14.1, which is filed by advice letter as needed. SP U-40-W provides guidance on what can be included in Rule 14.1. We should revisit guidelines on voluntary and mandatory rationing, as follows:

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<sup>3</sup> The software is available at:

[http://www.awwa.org/WaterWiser/waterloss/Docs/03IWA\\_AWWA\\_Method.cfm](http://www.awwa.org/WaterWiser/waterloss/Docs/03IWA_AWWA_Method.cfm)

- Should guidelines on voluntary rationing be revised and, if so, how should they be revised?
- Should guidelines for mandatory rationing be established and, if so, what should those guidelines include?
- Should drought rates be established for periods of drought?

## **2.6. Implementation of Increasing Block Rates and Other Water Conservation Measures**

Implementation of increasing block rates presents several issues:

- Should increasing block rates be effective after completion of this proceeding or after the utility's next general rate case (GRC)?
- Should the utilities' required return on equity be adjusted if a WRAM is adopted?
- Should any savings realized on purchased water be tracked in a memorandum account?
- Should the Commission track water conservation (*i.e.*, per capita) achieved by the adoption of increasing block rates and other water conservation measures? If so, what mechanism should be used?

## **3. Other Issues in GSWC's Application**

GSWC proposes to implement statewide rates simultaneously with increasing block rates. We will not consider that proposal in this investigation. GSWC's application addresses other issues related to the WAP's goals of water quality and infrastructure. No other company has addressed programs to implement these goals in their conservation rate design applications. GSWC shall propose alternatives for consideration of the remaining issues in its application in its response on the preliminary scoping memo. Other parties may also comment on alternatives for consideration of these issues in their responses.

#### **4. Preliminary Scoping Memo**

This investigation will be conducted in accordance with Articles 6 and 7 of the Commission's Rules of Practice and Procedure. As required by Rule 7.1(d), this order includes a preliminary scoping memo. Pursuant to Rule 7.1(c), we preliminarily determine the category of this investigation proceeding to be ratesetting as the term is defined in Rule 1.3(e).

As described in Section 2, *supra*, we intend to consider all appropriate means to achieve the Commission's conservation objectives for Class A water utilities. We will consider policies applicable to all Class A water utilities initially, but may hold hearings to implement these policies for individual utilities. We do not expect that the overarching policy phase will require hearings.

As permitted by Rule 5.2, a party may, but is not required to, file a response. Any party filing a response to this preliminary scoping memo shall state in its comments any objections the party has regarding (1) the issues to be considered; (2) the need for hearings; and (3) the schedule for this proceeding as described in this order.

Following review of responses to the preliminary scoping memo, the assigned Commissioner will issue a scoping memo that finalizes the scope and schedule of this proceeding. (See Rule 7.3.) After the scoping memo issues, parties may file and serve an appeal to the Commission regarding the ruling on category. (See Rule 7.6.) If no comments are filed concerning the preliminary scoping memo, the preliminary scoping memo will be deemed the scoping memo for the proceeding, unless otherwise ordered.

## 5. Schedule

The schedule for this proceeding will depend on the comments we receive from the parties and additional input at the prehearing conference (PHC). For purposes of addressing the scoping memo requirements, we establish the following tentative schedule, which is subject to change by the assigned Commissioner or the assigned Administrative Law Judge (ALJ):

January 11, 2007	Order Instituting Investigation
January 22, 2007	Deadline for other interested persons to request their addition to the service list and indicate status (see Section 6, <i>infra</i> )
January 29, 2007	Deadline for filing responses on preliminary scoping memo
February 7, 2007	Prehearing conference at 10:00 a.m., Commission Courtroom, State Office Building, 505 Van Ness Avenue, San Francisco, CA 94102
February 15, 2007	Assigned Commissioner's Ruling and Scoping Memo (ACR)
March 2, 2007	Deadline for filing comments in response to ACR
March 19, 2007	Deadline for filing reply comments
May 22, 2007	Mailing of Proposed Decision
June 21, 2007	First possible Commission Consideration of Proposed Decision

After issuing a decision on these broad policy issues, we will implement increasing block rates and WRAMs for each utility by advice letter or subsequent decision. We solicit parties' input in their preliminary scoping memo responses on means to expedite implementation of increasing block rates and WRAMs in the context of considering these policy issues. Through the scoping memo and subsequent rulings, the assigned Commissioner and the assigned ALJ may adjust

the timetable as necessary during the course of the proceeding and establish the schedule for remaining events. In no event do we anticipate this proceeding to require longer than 18 months to complete.

## **6. Service List**

This investigation consolidates the four previously filed conservation rate design applications. The conservation rate design policies to be considered in this rulemaking could affect all Commission regulated Class A water service utilities and such changes may be of interest to all regulated water and sewer service utilities. We will direct that this investigation be served on GSWC, CalWater, Park, and Suburban, the remaining Commission regulated Class A water and sewer service utilities, the Water Branch of the Division of Ratepayer Advocates (DRA), the service lists for the consolidated applications, the service lists for the latest GRCs of all Class A Water Utilities, the DWR, and the Department of Health Services.

After initial service, a new proceeding service list will be formed by the Process Office, published on the Commission's Internet site and updated throughout the proceeding. Only Class A water service utilities and DRA will be included automatically on the new service list.

Other interested parties, including other water and sewer system utilities who wish to participate, must request to be added to the new service list by submitting a written request or electronic mail request to the Commission's Process Office, stating their full name, the entity or person they represent, the postal address and telephone number of the person to be served, the proceeding number for this OII, an e-mail address if they are willing to be served electronically, and their desired service list category (Appearance, State Service, or Information Only). All interested parties must notify the Process Office,

505 Van Ness Avenue, San Francisco, CA 94102 or [process\\_office@cpuc.ca.gov](mailto:process_office@cpuc.ca.gov), by January 22, 2007. Parties serving documents may rely on the Internet service list published as of the date their documents must be served or parties may obtain a copy of the service list by calling the Process Office at (415) 703-2021.

Parties must serve documents in this proceeding consistent with Rule 1.9 (Service) and 1.10 (Electronic Service). Filings may be made by hard copy with the Docket Office or electronically consistent with Resolution ALJ-188 (Electronic Filing) at <http://www.cpuc.ca.gov/static/efiling.htm>.

## **7. Public Advisor**

Any party interested in participating in this investigation and who is unfamiliar with the Commission's procedures should contact the Commission's Public Advisor's Office in San Francisco at (415) 703-2074, (866) 836-7825 (TTY-toll free) or (415) 703-5282 (TTY), or in Los Angeles at (866) 849-8391, or send an e-mail to [public.advisor@cpuc.ca.gov](mailto:public.advisor@cpuc.ca.gov).

## **8. Ex Parte Communications**

This proceeding is subject to Article 8 of the Rules of Practice and Procedure, which specifies standards for engaging in ex parte communications and the reporting of such communications. Pursuant to Rule 8.2(c), ex parte communications are subject to the restrictions set forth therein and the reporting requirements set forth in Rule 8.3.

**IT IS ORDERED** that:

1. An investigation on the Commission's own motion is instituted to address means to achieve the Commission's conservation objectives for Class A Water Utilities.
2. All Class A water utilities (utilities with over 10,000 service connections) are made respondents to this investigation.

3. Applications (A.) 06-09-006, A.06-10-026, A.06-11-009, and A.06-11-010 are consolidated for the purpose of considering the conservation proposals contained therein.

4. Class A water utilities are hereby placed on notice that the Commission, for good cause, and to advance the public interest, may enter orders beyond the confines of the requests in companion consolidated proceedings. This proceeding is classified as ratesetting. There is a need for hearings to implement rates for individual utilities.

5. The expected timetable for this proceeding is as set forth in the body of this order. The assigned Commissioner and the assigned Administrative Law Judge may adjust the timetable as necessary during the course of the proceeding, provided that in no instance shall this proceeding require longer than 18 months to complete.

6. All Class A water utilities, the Commission's Division of Ratepayer Advocates (DRA), the Department of Water Resources (DWR), the Department of Health Services (DHS), and other interested parties are invited to comment on the issues raised in this investigation, pursuant to the schedule adopted in this order.

7. Pursuant to Rule 5.2, a party filing a response to the preliminary scoping memo shall state in its comments any objections the party has regarding (1) the issues to be considered; (2) the need for hearings; and (3) the schedule for this proceeding as described in this order.

8. The Executive Director shall direct a copy of this order to be served upon Golden State Water Company, California Water Service Company, Park Water Company and Suburban Water Systems, all respondent Class A water and sewer service utilities, the DRA, the service lists for the consolidated applications, the

service lists for the latest general rate cases of all Class A Water Utilities, the DWR, and the DHS. After service of this order, the service list for this proceeding shall be formed following the procedures set forth in the Service List section in the body of this order.

This order is effective today.

Dated January 16, 2007, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
DIAN M. GRUENEICH  
JOHN A. BOHN  
RACHELLE B. CHONG  
Commissioners