

Decision 08-06-002 June 12, 2008

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

In the Matter of the Application of California-American Water Company (U210W) for an order authorizing it to increase its rates for Water Service in its Los Angeles District to increase revenues by \$2,020,466 or 10.88% in the year 2007; by \$634,659 or 3.08% in the year 2008; and by \$666,422 or 3.14% in the year 2009.

Application 06-01-005  
(Filed January 9, 2006)

**DECISION ADOPTING A CONSERVATION RATE DESIGN SETTLEMENT**

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Appendix A - Amended Settlement Agreement Between the Division of Ratepayer Advocates, the City of Duarte, and California-American Water Company on Conservation Rate Design Issues

Attachment to Appendix A

## **DECISION ADOPTING A CONSERVATION RATE DESIGN SETTLEMENT**

### **1. Summary**

This decision adopts a March 25, 2008 settlement agreement that resolves all Phase 2 rate design issues in this proceeding. Specifically, the settlement proposes as a Pilot Program the first conservation rate design for customers in California-American Water Company's (Cal-Am) Los Angeles district and incorporates into the Pilot Program two ratemaking mechanisms that remove any disincentive for Cal-Am to implement conservation rates and conservation programs. The settlement also requires Cal-Am to work closely with all interested cities within the Los Angeles district in preparing its requests to the Commission for new capital improvements and replacement of aging infrastructure.

The Pilot Program we adopt here will be in effect for approximately two years. During this time, Cal-Am will undertake a comprehensive monitoring and data collection effort to assess customer response to the conservation rate design, and will meet regularly with all interested parties to discuss the tracking results. Cal-Am will file annual reports on the Pilot Program with the Commission and we will undertake a full review of the program in Cal-Am's next general rate case (GRC) proceeding for the Los Angeles district, which will be filed on January 1, 2009, with rates scheduled to be effective on July 1, 2010.

The settlement is sponsored by Cal-Am, the Commission's Division of Ratepayer Advocates (DRA), and the City of Duarte. No party protested the settlement. We direct Cal-Am to take all necessary steps to implement the new conservation rate design as soon as possible.

## **2. Procedural Background**

The Commission regulates water service provided by Cal-Am in its seven California districts pursuant to Article XII of the California Constitution, the Public Utilities Code, and the Commission's rules and regulations. For Cal-Am and other Class A water utilities, Public Utilities Code Section 455.2, as implemented in Decision (D.) 04-06-018, provides for a GRC proceeding every three years.<sup>1</sup>

There are approximately 27,200 customers in the Los Angeles district. The district has three physically separated service areas, the largest being San Marino. The other two are the neighboring Duarte service area and the more distant Baldwin Hills service area.<sup>2</sup> The district is served by wells and irrigation water utilizing Cal-Am's groundwater rights and by purchases from municipal wholesalers. The San Marino and Duarte service areas use primarily groundwater while the Baldwin Hills service area uses approximately 50% purchased water from the Metropolitan Water District and the West Basin Municipal Water District.

On April 10, 2006, Cal-Am filed a motion requesting that this proceeding be bifurcated to allow it time to withdraw its contested consolidated rate design proposal and then to develop and file a conservation rate design proposal. Cal-Am proposed that the revenue requirement portion of its GRC application

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<sup>1</sup> A Class A utility is defined as an investor-owned water utility with over 10,000 service connections.

<sup>2</sup> The San Marino service area is situated ten miles northeast of downtown Los Angeles in the San Gabriel Valley, and the Baldwin Hills service area is centrally located in an unincorporated area of Los Angeles County southwest of downtown Los Angeles and just a few miles east of the Los Angeles International Airport.

be heard and decided first, in Phase 1, and rate design issues be heard and decided in a later schedule, in Phase 2. On May 22, 2006, the assigned Commissioner issued a scoping memo granting Cal-Am's request to bifurcate the proceeding and adopting a procedural schedule.

On August 24, 2007, the Commission issued D.07-08-030, its final decision on Phase 1 issues. This decision removed from Phase 2 to a generic industry proceeding the Commission's consideration of Cal-Am's proposed Water Revenue Adjustment Mechanism (WRAM) and Modified Cost Balancing Account (MCBA), as well as the related issue of a return on equity adjustment. The decision also encouraged the parties to modify a pending Phase 2 settlement to replace the proposed WRAM with a more narrow conservation loss adjustment mechanism (CLAM).<sup>3</sup>

DRA filed an application for rehearing of D.07-08-030, taking issue with the Commission's (1) announced policy preference for a CLAM, and (2) statement that adoption of a CLAM for Cal-Am would not require an adjustment to Cal-Am's return on equity. In D.07-12-058, the Commission modified D.07-08-030 to remove language addressing the CLAM's impact on a return on equity adjustment and to remove a sentence stating "if a CLAM can be negotiated, the rate design in Phase 2 is likely to proceed smoothly." The Commission retained language stating a policy preference for a CLAM and encouraging Cal-Am and DRA to modify their pending Phase 2 settlement to

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<sup>3</sup> In response to a petition to modify filed by Cal-Am, the Commission, in D.07-11-014, modified D.07-08-030 to include additional tables that would allow Cal-Am to implement the revenue requirement under the existing rate design finding that good cause existed to grant Cal-Am's petition because in D.07-08-030 we changed the scope and schedule of Phase 2.

include a mechanism that is focused solely on cost under- and over-recovery caused by our conservation policies. Finally, the decision denied rehearing.

On October 17, 2007, a prehearing conference (PHC) was held to discuss the status of Phase 2. At the PHC, the parties indicated their interest in again pursuing a settlement, and an all-party settlement conference was duly noticed and held on October 30, 2007. Following a second PHC on November 20, 2007, Cal-Am and DRA filed a joint petition to modify D.07-08-030 to allow consideration of the WRAM and MCBA mechanisms, in conjunction with conservation rates, in Phase 2 of this proceeding. The Commission granted this petition in D.08-01-034, issued on February 1, 2008.

### **3. Proposed Settlement**

Pursuant to Article 12 of the “Rules of Practice and Procedure” of the Commission (Rules 12.1 – 12.7), Cal-Am, DRA, and the City of Duarte submitted by motion the proposed settlement to the Commission for review and approval. The original settlement was filed on February 5, 2008 and the amended settlement was filed on March 25, 2008.

The settling parties amended the settlement in order to specify a procedural forum and process to measure the effect of the settlement’s proposed WRAM/MCBA mechanisms on the Los Angeles district’s return on equity. For purposes of this decision, we consider only the amended proposed settlement (settlement).

#### **3.1. Standard of Review for Settlements**

We review the settlement under the requirements set forth in Rule 12.1(d). This rule provides that, prior to approval, the Commission must find a settlement “reasonable in light of the whole record, consistent with the law, and in the public interest.”

In addition, Rule 12.5 states that, unless the Commission expressly provides otherwise, Commission adoption of a settlement does not constitute approval of, or precedent regarding, any principle or issue in the proceeding, or in any future proceeding.

### **3.2. Terms of the Settlement**

The settling parties state that the settlement proposes conservation-oriented increasing block rates and related ratemaking mechanisms for ensuring full recovery by Cal-Am of all authorized fixed costs and actual variable costs. The conservation rate design and related WRAM and MCBA ratemaking mechanisms constitute a Pilot Program to become effective within 90 days after a Commission decision adopting the proposed settlement. The Pilot Program will be reviewed in the next GRC proceeding for this district, which, pursuant to the Commission's Rate Case Plan set forth in D.07-05-062, will be filed January 1, 2009, with rates scheduled to be effective July 1, 2010.

The proposed settlement is attached as Appendix A to this decision. Appendix A consists of a 13-page settlement with an attachment to the settlement containing worksheets for the three service areas.<sup>4</sup> For the Baldwin Hills service area, an additional worksheet is attached that shows sample WRAM and MCBA balancing account transactions.

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<sup>4</sup> Each service area has a separately numbered worksheet for (1) rate design and revenue check spreadsheets, (2) residential customer bill impact analysis for small user, average user, and large user for summer and winter seasons, (3) a bill impact analysis at various usage levels, (4) a non-residential customer bill impact analysis, (5) a graph comparing current and proposed monthly total bills for residential customers at different usage levels, (6) a graph comparing current and proposed average unit costs, and (7) a bar graph showing the marginal cost per unit under the proposed tiered rate design for residential customers.

In their motion for adoption of the settlement, the settling parties state that they represent three of the four active parties in Phase 2 of this proceeding and are fairly representative of affected interests; DRA represents the interests of customers in general, the City of Duarte represents the interests of its residents, and Cal-Am represents the interest of the utility.

The settlement is presented as an integrated package, such that parties are agreeing to the settlement as a whole, as opposed to agreeing to specific elements of the settlement. The parties state that approval of the proposed settlement by the Commission should not be construed as precedent or statement of policy of any kind in any current or future proceeding.

No party protested or filed comments on the proposed settlement.

We review the specific provisions of the proposed settlement next.

### **3.2.1. Conservation Rate Design**

The three service areas in the Los Angeles district currently share the same tariff sheets, with customer categories being General Metered Service, Measured Irrigation Service, and Private Fire Protection Service. All of the residential, commercial, industrial, public authority, irrigation and “other” customers in the three service areas have metered service connections. Current rates for each customer class include a service (or meter) charge and a single quantity charge (or volumetric rate) per hundred cubic feet.<sup>5</sup> Most customers are billed on a bimonthly basis.

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<sup>5</sup> The only flat-rate customers are privately owned fire protection service. Fire protection is a fixed charge, much like a meter service charge, and as such it is not included in the balancing accounts.

The settlement proposes a rate design, termed a “conservation rate design” because its objective is to provide customers with a greater financial incentive to conserve water, especially during peak times of the year, and especially for residential usage beyond average indoor usage levels. For all customers except “other” and private fire service, the rate design shifts 50% of the current fixed monthly service charge to the volumetric rate and applies a seasonal adder for usage during the peak season, defined as May 1 through October 31.<sup>6</sup>

For residential customers, an increasing quantity three tier (or block) rate design is also proposed. The parties state that developing increasing block rates for non-residential customers is currently not feasible as it would likely require reclassification of these customers based on customer and consumption data that is currently unavailable.<sup>7</sup>

The proposed conservation rates are designed to collect the same revenue requirement as current rates for each service area and customer class; this is defined by the parties as revenue neutrality. The three residential tiers are set at separate consumption levels for each service area, based on Cal-Am and DRA’s analysis of mean and median summer and winter usage patterns and bill frequency in each service area.<sup>8</sup> All residential customers have a 5% seasonal

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<sup>6</sup> Fire protection service is a stand-by service, meaning it is only used when needed. Therefore, there is no conservation rate design. The category “other” is metered customers with private fire hydrant service. This is distinct from private fire protection service, which is provided under a separate tariff, Schedule No. LA-4.

<sup>7</sup> See Appendix A, Section III.B.3, page 7.

<sup>8</sup> The parties state that the methodology used in their analysis is consistent with methodologies outlined by the California Urban Water Conservation Council, the

*Footnote continued on next page*

adder applied to the volumetric rates of Tier 2 and Tier 3 during the summer months. Recognizing that the monthly service charge has been reduced by 50%, the three tiers of volumetric rates are shown in the table below.

<b>Proposed Residential Volumetric Rates</b>
<p>In winter (November 1 - April 30):</p> <ul style="list-style-type: none"><li>- Tier 1 is approximately 15-20% higher than current single volumetric rate;</li><li>- Tier 2 is approximately 10% higher than Tier 1; and</li><li>- Tier 3 is approximately 20% higher than Tier 1.</li></ul>
<p>In summer (May 1 - October 31):</p> <ul style="list-style-type: none"><li>- Tier 1 is approximately 15-21% higher than the current single volumetric rate;</li><li>- Tier 2 is approximately 15% greater than Tier 1; and</li><li>- Tier 3 is approximately 25% greater than Tier 1.</li></ul>

In Section III.E, the settlement contains a discussion of the impact of the proposed rate design on low-income customers. The parties state that there is general agreement that rate structures that rely on quantity versus fixed charges benefit low-income customers because, to the extent the customers can manage their consumption, they can better manage their bill. In addition, the adoption of break points for the tiers that is based on an analysis by service area of who uses

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American Water Works Association, and Western Resources Advocates. These studies were discussed during the evidentiary hearings. The specific tier consumption levels for each service area are shown on the worksheets attached to the proposed settlement at Appendix A.

water, and when in the year water is being used, is designed to ensure that essential indoor water use is priced lower than non-essential use.

While an increasing block rate design is not proposed for non-residential customers in this Pilot Program, the parties do propose a higher seasonal adder of 10% during the summer months for these customers. This adder is twice the level of the residential adder, and is done in order to strengthen the price signal to conserve during peak periods.

The parties propose that the Pilot Program, consisting of the conservation rate design and the related WRAM and MCBA mechanisms, become effective within 90 days after a Commission decision adopting the proposed settlement. The 90 days will allow Cal-Am to modify its billing system and to distribute information regarding the new rate design to customers.

### **Discussion**

The settlement's conservation rate design proposal has been carefully examined and refined through the evidentiary hearing process and it reflects a thoughtful and collaborative approach by the parties. Both Cal-Am and DRA have made substantial changes to their initial conservation rate design proposals.

The underlying goal of the proposal is to reduce consumption by all major customer groups in a reasonable manner, without sudden rate shock. The proposal targets reductions in discretionary watering, which is mainly outdoor water use, and does this by the careful selection of tier break points based on residential consumption usage patterns in each service area, avoiding dramatic increases between rate tiers, and using seasonal adjustments to further reduce water usage in peak outdoor watering periods.

The parties state that during this Pilot Program they will closely monitor residential and commercial consumption data, and measure the demand

response that takes place within each customer class and service area. The parties expect to propose further refinement, which could include steeper tier and seasonal changes and consideration of commercial increasing block rates, in the next GRC period based on the measurement and evaluation of this Pilot Program.

Cal-Am testified that when conservation rates were first introduced in 1997 in its Monterey district, the utility tracked and reported on the changes in consumption patterns of the top 100 residential customers; this report is Exhibit 63 in this proceeding. We find that a similar report for the top 100 residential customers in each of the three Los Angeles service areas would be beneficial in evaluating the Pilot Program. Therefore, we direct Cal-Am to track and report this information, in the same format as Exhibit 63, in its Los Angeles district annual report.

We find the proposed rate design gives clear and significant price signals to customers to reduce their usage throughout the year and particularly in the peak summer months. Important conservation features included in the proposed rate design are (1) shifting 25% of the total fixed cost recovery from the stand-by charge to the volumetric rate; (2) introducing increasing tiered rates for residential customers; and (3) adopting a seasonal adder to the volumetric rates for all customers that are billed under volumetric rates. These features are consistent with the goals of our Water Action Plan and the conservation principles being developed in our Conservation OII, Investigation (I.) 07-01-022.

We appreciate the careful usage and billing analysis performed by Cal-Am and DRA in determining the break points for the residential tiers, and agree with the parties that this analysis should be separately performed for each service

area. We find the magnitude of the rate increase for each tier to be appropriate for a Pilot Program.

We find two weaknesses in the rate design proposal. First, the parties, while agreeing that monthly customer billing is important in providing customers timely conservation price signals, do not provide a plan for moving the Los Angeles district from bimonthly to monthly billing. Cal-Am testifies there are two ways to move to monthly billing: double the meter reading staff in the district or replace existing customer meters with new radio-read meters. Cal-Am was not able to provide a report on the average age of meters in the Los Angeles district or the present rate of meter replacement.<sup>9</sup> Both Cal-Am and DRA testified it would not be cost-effective to install advanced meters for only high usage customers but that they would explore testing advanced meters for the Los Angeles district in the Pilot Program period and they would review the results of a test of radio-read meters Cal-Am is conducting in the Sacramento district.<sup>10</sup>

We encourage the parties to discuss the metering issue further during the Pilot Program and to collect the data necessary for a comprehensive analysis in the next GRC proceeding. We direct Cal-Am to present a proposal for moving to monthly billing in its next GRC filing. The proposal can contain separate timelines for customer classes or service areas, and can contain a mixture of temporary meter reading personnel and investment in new metering technology.

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<sup>9</sup> See January 9, 2007 transcript at page 911.

<sup>10</sup> *Id.* at pages 929-931.

The second weakness we find in the conservation rate design proposal is that the proposal for non-residential customer groups is more limited than the proposal for residential customers, and the record does not contain sufficient evidence to evaluate additional measures we could adopt for non-residential customers. In the settlement, the parties state that an increasing block rate design for non-residential customers is “currently not feasible;” no further explanation is provided in the settlement or the accompanying motion.

In reviewing testimony in the hearing record, we believe the feasibility statement is due to a lack of sufficient data and analysis for these customer groups, as well as a policy disagreement between Cal-Am and DRA on whether additional tariff schedules for non-residential customers should be developed based on individual water audits. Therefore, we direct Cal-Am to meet and confer with all interested parties in the next 90 days to determine the types of additional data that should be collected during the Pilot Program period in order for the Commission to consider additional conservation proposals for non-residential customers in the next GRC proceeding. The additional data collection may be for the purpose of analyzing increasing block rates, steeper seasonal adders, or other conservation rate design measures.

Overall, we find that the settlement’s rate design proposal before us is a good first step in implementing conservation rate design in the Los Angeles district, and the proposal should be adopted. The two areas of concern we have discussed should be addressed by Cal-Am during the Pilot Program and revisited in the next GRC proceeding.

Given the importance of having conservation rates in place for the Los Angeles district for the summer season, Cal-Am should make every effort to implement the proposed conservation rate design as soon as possible after the

Commission issues a final decision in this proceeding. The settlement is unopposed and the proposed decision recommends it be adopted. Therefore, Cal-Am can begin the process of customer notification and billing system modifications when the proposed decision is first issued, and it should give priority to quickly accomplishing these tasks.

### **3.2.2. WRAM and MCBA Mechanisms**

In order to (1) remove any disincentive for Cal-Am to implement conservation rates and programs, (2) ensure any cost savings resulting from conservation are passed onto ratepayers, and (3) reduce overall water consumption in the Los Angeles district, the settling parties propose adopting a WRAM and MCBA in the Pilot Program.<sup>11</sup>

Together, these two mechanisms will operate to ensure recovery of the adopted fixed costs recovered through Cal-Am's volumetric rates, and the actual variable costs for purchased power, purchased water, and pump taxes. The fixed costs not included in these accounts will be recovered through the service charge, which is a monthly charge that customers pay regardless of consumption levels. Cal-Am stipulates that it will exercise due diligence in ensuring the least-cost water mix of its water sources and will make a showing in the next GRC filing demonstrating that it has exercised due diligence and that any significant change in water purchases was reasonable.<sup>12</sup>

Each of Cal-Am's three service areas will have its own WRAM and MCBA balancing accounts, with separate reporting by customer class maintained for

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<sup>11</sup> These are the three goals stated in Section VI of the settlement.

<sup>12</sup> Significant changes in water purchases are defined for each service area in Section IX.D and will be tracked for later reasonableness review.

each WRAM balancing account.<sup>13</sup> The WRAM and MCBA accounts for each service area will always be considered together, *i.e.* netted, when determining the need for additional revenue recovery from, or for refunds to, ratepayers in that service area. The WRAM and MCBA accounts will accrue interest at the 90-day commercial paper rate.

The settlement provides that by March 31<sup>st</sup> of each year, Cal-Am will provide the Water Division (with a copy to DRA) a written report that includes the net WRAM/MCBA balance in each service area. If the report shows the net balance exceeds 2.5% of a service area's total recorded revenue requirement for the prior calendar year, Cal-Am will file an advice letter within 30 days that amortizes the balance through a volumetric surcharge, if it is an under-collection, or a volumetric surcredit, if it is an over-collection. If the 2.5% threshold is not met, these balancing accounts will be amortized in the next GRC.

### **Discussion**

In D.07-08-030, the Commission expressed a policy preference for a revenue adjustment mechanism that focused solely on cost under- and over-recovery caused by conservation policies, rather than a broader WRAM mechanism. Cal-Am and DRA in their comments on the proposed decision stated that they did not have the data necessary to develop the proposed conservation-focused mechanism.

Since the issuance of D.07-08-030, the parties have again requested the Commission consider, as part of a Pilot Program scheduled to be in place for

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<sup>13</sup> While Cal-Am will track revenues in the WRAM account in each service area by customer class for analysis purposes, implementation of a surcharge or surcredit will be calculated using the WRAM balance for all customer classes in each service area.

approximately two years, the WRAM and MCBA mechanisms. Therefore, we assess the specifics of these mechanisms for the Los Angeles district Pilot Program.

The conservation rate design being proposed is expected to have a measurable but not substantial impact on sales during the Pilot Program. This is seen in our earlier discussion of the structure of the conservation rate design and is also apparent in the proposed balancing account recovery and refund procedures, which have an annual review, with a 2.5% annual revenue requirement threshold.

As a safeguard, the parties have also provided a provision in the settlement that would allow for a review and midcourse correction if the impacts of the WRAM and MCBA mechanisms go well beyond conservation impacts and instead produce a disparate impact on ratepayers or shareholders. This provision is found in Section III.3., and it would cause the parties to meet and discuss adjustments. We find that following this discussion, the parties should individually or jointly file a petition to modify this decision.

One disparate impact that could occur in the Pilot Program period would be a severe economic downturn in one or more of the Los Angeles service areas that causes a significant decrease in revenues. This could occur from a high rate of home foreclosures and/or business slowdowns or shutdowns. We find this would clearly be a disparate impact as the WRAM mechanism would shield shareholders from all financial consequences of the economic downturn while requiring ratepayers to bear the full cost. Since Cal-Am will be tracking sales levels by customer class and service area, any disparate impact can be quickly seen and addressed.

Given the expected modest balancing account impacts, the safeguards discussed above, and the limited time period of the Pilot Program, we find it reasonable to adopt the proposed WRAM and MCBA mechanisms. We expect that the usage information collected and evaluated during the Pilot Program will allow a conservation focused mechanism to be given consideration in the next GRC filing.

### **3.2.3. Procedural Process to Address Return on Equity Adjustment**

In Phase 1 of this proceeding, the Commission examined the issue of whether a downward adjustment to Cal-Am's Los Angeles district return on equity should be made if a WRAM mechanism was adopted in Phase 2. The initial proposed decision recommended a 50 basis point downward adjustment be adopted. The Commission removed consideration of both the WRAM and a return on equity adjustment from this proceeding in D.07-08-030, stating these issues should be examined in a generic proceeding for all water utilities (I.07-01-022). Subsequently, the parties filed a petition to modify D.07-08-030 that requested the WRAM be considered here, but did not address the related return on equity adjustment issue. In the settlement filed on March 25, 2008, the parties provide a procedural process for consideration of a return on equity adjustment for the WRAM in this settlement.

Section XIV of the settlement provides that if the Commission adopts in Phase 1B of I.07-01-022 a generic basis point adjustment to return on equity for water utilities that have WRAM/MCBA mechanisms that are similar to those approved for California Water Service Company and Park Water Company in D.08-02-036, then the same generic return on equity adjustment should be applied to the WRAM/MCBA adopted here. Further, the return on equity

adjustment should be applied here when conservation rates are implemented. If the return on equity adjustment decision is made in I.07-01-022 after a WRAM/MCBA is implemented for the Los Angeles district, then the balancing accounts would be subject to true-up to the date of implementation.

The settlement also provides that if the Commission issues a decision regarding a return on equity adjustment in I.07-01-022 that is not consistent with the generic adjustment described in the settlement, the parties will meet to discuss how that decision should affect this Pilot Program.

We find that I.07-01-022 is a procedural forum with an evidentiary record appropriate to deciding the return on equity adjustment issue for the WRAM/MCBA before us here. However, further specificity is needed on the procedural process if a Commission decision in I.07-01-022 does not resolve the matter for the Los Angeles district. Therefore, we direct that if the generic return on equity adjustment described in the settlement is not adopted in I.07-01-022, parties should meet and confer within 30 days and then file a petition to modify this decision within 15 days after the meeting, either jointly or separately, proposing a procedural forum and process to address a return on equity adjustment. The WRAM/MCBA balancing accounts adopted here will be subject to true-up to the date a final decision on a return on equity adjustment is made.

#### **3.2.4. Review of Infrastructure Reports**

At the request of the City of Duarte, which has concerns that ratepayers in the Duarte service area are being asked to subsidize plant additions for the other two Los Angeles district service areas, the settlement includes Section XIII. This section requires that Cal-Am provide, upon request, drafts of its Comprehensive Planning Study (CPS) and Condition-Based Assessment of Buried Infrastructure

(CBA) to any city with residents who are customers of Cal-Am's Los Angeles District by July 15, 2008.

Upon request, Cal-Am also agrees to meet with any city with residents who are customers of its Los Angeles District to discuss the draft CPS and/or draft CBA. The settlement provides that the city or cities shall have 30 days to review and provide comment on the CPS and CBA in writing before Cal-Am finalizes these reports and submits them to the Commission as part of its 2009 GRC application. The intent of these reports is to determine the need for system capital improvement and the replacement of aging infrastructure, address compliance with local applicable and industry standards, and to prioritize and schedule these improvements.

We find the provisions of this section reasonable.

### **3.2.5. Monitoring and Data Collection**

Section XII of the settlement provides that Cal-Am will track data, such as billing and usage data by meter size, by month, and by class of customer, for use in analyzing customer response to the proposed conservation rates so that it is readily available to the Commission and the parties to evaluate the results of this Pilot Program. In our review of the conservation rate design, we have also directed that the usage of the top 100 residential customers in each service area be tracked and analyzed, in the same manner as Cal-Am did when it introduced conservation rate design in its Monterey district in 1997.

To ensure an effective Pilot Program, we also direct Cal-Am to schedule a meeting every four to six months with all parties to discuss the customer response data it is tracking and whether there should be any changes in its conservation outreach programs in response to the results.

With our specification of the high user tracking report discussed in the conservation rate design section, and the addition of a regular meeting requirement, we find the monitoring and data collection proposed by the parties to be reasonable.

### **3.3. Action on Proposed Settlement**

Based on our review of the terms of the proposed settlement, we find each section to be reasonable in light of the whole record. In reviewing specific terms, we have added clarification to the settlement language and further direction to the parties for the review of this Pilot Program in the next GRC filing. We find that with these refinements, the settlement is reasonable in light of the whole record, consistent with the law, and in the public interest. Therefore, we should adopt the settlement.

### **4. Comments on Proposed Decision**

The proposed decision of the assigned Administrative Law Judge (ALJ) was mailed to the parties in accordance with Section 311 of the Public Utilities Code and Rule 14.3 of the Commission's Rules of Practice and Procedure. No party filed comments on the proposed decision.

### **5. Assignment of Proceeding**

John A. Bohn is the assigned Commissioner and Christine M. Walwyn is the assigned ALJ in this proceeding.

### **Findings of Fact**

1. This decision resolves all issues in Phase 2 of Cal-Am's Los Angeles district GRC application.

2. On February 5, 2008, Cal-Am, DRA, and the City of Duarte filed a settlement agreement and on March 25, 2008, the same parties filed an amended settlement agreement. No party filed comments on either settlement.

3. The March 25, 2008 settlement, with accompanying worksheets, is attached as Appendix A of this decision.

4. The settlement proposes a Pilot Program for this GRC period that consists of a conservation rate design for residential and non-residential customers in each of the three Los Angeles service areas and related ratemaking mechanisms, the WRAM and the MCBA.

5. The proposed conservation rate design has been carefully examined and refined through the evidentiary hearing process.

6. Important conservation features included in the proposed rate design are (1) shifting 25% of the fixed cost recovery from the stand-by charge to the volumetric rate; (2) introducing increasing tiered rates for residential customers; and (3) adopting a seasonal adder to the volumetric rates for all customers that are billed under commodity rates. These features are consistent with the goals of our Water Action Plan and the conservation principles being developed in our Conservation OII, I.07-01-022.

7. The rate design gives significant price signals to customers to reduce their usage throughout the year, and particularly in the peak summer months.

8. The parties should further discuss and review methods for moving to monthly billing so that customers receive clearer conservation price signals. During the Pilot Program, Cal-Am should collect and analyze the data necessary for a comprehensive review of this issue and it should present a proposal for moving to monthly billing in its next GRC filing.

9. The conservation rate design proposal for non-residential customers is more limited than the proposal for residential customers. Cal-Am should meet and confer with all interested parties in the next 90 days to determine the types of data collection necessary during the Pilot Program period in order for the Commission to consider further conservation rate design proposals for non-residential customers in the next GRC proceeding.

10. It would be useful for Cal-Am to track and prepare a report on the usage of the top 100 residential customers in each service area during the Pilot Program. This report should be in the same format as the report made for the Monterey district, as shown in Exhibit 63.

11. Cal-Am should make every effort to implement the new rate design during the summer peak period. It should begin the process of customer notification and billing system modifications when the proposed decision is issued.

12. The proposed WRAM and MCBA mechanisms will operate to ensure recovery of the adopted fixed costs recovered in volumetric rates and the actual variable costs for purchased power, purchased water, and pump taxes.

13. Cal-Am stipulates that it will exercise due diligence in ensuring the least-cost water mix of its water sources and will make this showing in its next GRC filing.

14. In D.07-08-030, the Commission expressed a policy preference for a revenue adjustment mechanism that is focused solely on cost under- and over-recovery caused by conservation policies, rather than the broader WRAM mechanism proposed here. We expect that the usage information collected and evaluated during the Pilot Program will allow a conservation focused mechanism to be given greater consideration in the next GRC filing.

15. Cal-Am should discuss the feasibility, as well as the costs and benefits, of conservation focused revenue adjustment mechanisms in its next GRC filing.

16. The conservation rate design being proposed is expected to have a measurable but not substantial impact on sales during the Pilot Program.

17. The settlement provides for adjustments to the Pilot Program if a disparate impact on ratepayers or shareholders occurs. The parties should meet to discuss adjustments and then either jointly or individually file a petition to modify this decision.

18. An example of a disparate impact would be a substantial economic downturn in one or more of the Los Angeles service areas that causes a significant decrease in revenues. This type of a disparate impact should be quickly noticed by Cal-Am based on its monitoring.

19. The initial proposed decision in Phase 1 recommended a 50 basis point downward adjustment to Cal-Am's Los Angeles district return on equity if a WRAM was adopted in Phase 2. The Commission removed consideration of both the WRAM and a related return on equity adjustment from this proceeding to a generic proceeding, then subsequently allowed consideration of a WRAM here.

20. The settlement provides that if the Commission adopts in Phase 1B of I.07-01-022 a generic basis point adjustment to return on equity for water utilities that have WRAM/MCBA mechanisms that are similar to those approved for California Water Service Company and Park Water Company in D.08-02-036, then the same generic return on equity adjustment should be applied to the WRAM/MCBA adopted here.

21. If the Commission issues a decision regarding a return on equity adjustment in I.07-01-022 that is not consistent with the generic adjustment

described in the settlement, the parties should meet and confer within 30 days and then, jointly or separately, file a petition to modify this decision within 15 days after the meeting. The WRAM/MCBA balancing accounts adopted here will be subject to true-up to the date of a final decision on a return on equity adjustment.

22. Cal-Am agrees to provide, upon request, drafts of its CPS and CBA reports to any city with residents who are customers of Cal-Am by July 15, 2008, and to provide those cities a 30-day period for review and submission of written comments before finalizing the reports.

23. In consultation with DRA and other interested parties, Cal-Am agrees to develop a comprehensive monitoring and data collection system for use in analyzing customer response to the proposed conservation rates and conservation programs. Cal-Am should schedule a meeting every four to six months with interested parties to discuss the customer response data it is tracking and whether there should be any changes in conservation outreach programs in response to the results.

24. This proceeding should be closed.

### **Conclusions of Law**

1. The Commission regulates water service provided by Cal-Am pursuant to Article XII of the California Constitution, the Public Utilities Code, and the rules and regulations of the Commission.

2. We review the proposed settlement under the requirements set forth in Rule 12.1(d) of the Commission's "Rules of Practice and Procedure."

3. We find the rate design proposed to be reasonable and an appropriate initial conservation rate design for the Los Angeles district.

4. Given the expected modest balancing account impacts, the safeguard provisions of the settlement, and the limited time period of the Pilot Program, we find it reasonable to adopt the proposed WRAM and MCBA mechanisms.

5. Applying a generic basis point adjustment to return on equity developed and adopted in I.07-01-022 to Cal-Am's WRAM/MCBA mechanisms here is reasonable, provided that if the Commission issues a decision in I.07-01-022 that is not consistent with the generic adjustment, the parties meet and confer, and then file jointly or separately a petition to modify this decision.

6. The monitoring and data collection effort proposed in the settlement, together with the refinements discussed in this decision, are reasonable for the Pilot Program and should be adopted.

7. The commitment made by Cal-Am to provide cities drafts of its CPS and CBA reports, together with an opportunity for cities to provide written comments prior to Cal-Am finalizing the reports is reasonable and should be adopted.

8. We find the proposed settlement, with the refinements discussed above, to be reasonable in light of the whole record, consistent with the law, and in the public interest. Adoption of this settlement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding, or in any future proceeding.

9. The March 25, 2008 settlement should be adopted.

10. Cal-Am should be directed to file a Tier 1 advice letter, in accordance with GO 96-B, and make effective on not less than five days notice, revised tariff schedules reflecting the adopted conservation rate design and rates and the adopted WRAM and MCBA mechanisms, as well as the schedule of recovery for the balances under these mechanisms.

**O R D E R**

**IT IS ORDERED** that:

1. The March 25, 2008 settlement attached at Appendix A is adopted.
2. California-American Water Company (Cal-Am) is directed to file a Tier 1 advice letter, in accordance with General Order (GO) 96-B , and make effective on not less than five days notice, revised tariff schedules reflecting the adopted conservation rate design and rates and the adopted Water Revenue Adjustment Mechanism (WRAM) and Modified Cost Balancing Account (MCBA) mechanisms, as well as the schedule of recovery for the balances under these mechanisms.
3. During the Pilot Program, Cal-Am shall collect and analyze the data necessary for Commission consideration of a proposal to move to monthly billing. Cal-Am shall present a proposal for this in its next Los Angeles district general rate case (GRC) filing.
4. Cal-Am shall meet and confer with all interested parties in the next 90 days to determine the types of data collection necessary in order for the Commission to consider further conservation rate design proposals for non-residential customers in the next GRC proceeding.
5. Cal-Am shall track and prepare a report on the usage of the top 100 residential customers in each service area during the Pilot Program. This report shall be in the same format as the report made for the Monterey district, as shown in Exhibit 63.
6. Cal-Am shall make every effort to implement the conservation rate design adopted here as soon as possible.

7. Cal-Am shall include in its next GRC filing a discussion of the feasibility, as well as the costs and benefits, of revenue adjustment mechanisms that are focused solely on conservation impacts.

8. If the Commission issues a decision regarding a return on equity adjustment in I.07-01-022 that is not consistent with the generic adjustment described in the settlement, Cal-Am shall meet and confer with all interested parties within 30 days and then, jointly or separately, file a petition to modify this decision within 15 days after the meeting.

9. The WRAM/MCBA balancing accounts adopted here shall be subject to true-up to the date of a final decision on a return on equity adjustment.

10. Cal-Am shall provide, upon request, drafts of its Comprehensive Planning Study and Condition-Based Assessment of Buried Infrastructure reports to any city with residents who are customers of Cal-Am as of July 15, 2008, and shall provide those cities a 30 day period for review and submission of written comments before Cal-Am finalizes the reports.

11. In consultation with DRA and other interested parties, Cal-Am shall develop a comprehensive monitoring and data collection system for use in analyzing customer response to the proposed conservation rates and conservation programs. Cal-Am shall schedule a meeting every four to six months to discuss with interested parties the results of the customer response data it is tracking and whether there should be any changes in conservation outreach programs in response to the results.

12. Application 06-01-005 is closed.

This order is effective today.

Dated June 12, 2008, at San Francisco, California.

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