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Decision 10-04-031 April 8, 2010

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of San Gabriel Valley Water Company (U337W) for authority to establish a conservation rate design, including a Water Revenue Adjustment Mechanism, modified cost balancing account, and Conservation Memorandum Account in compliance with Decision No. 08-06-022.	Application 08-09-008 (Filed September 10, 2008)

DECISION AUTHORIZING CHANGES IN RATE DESIGN AND RATESETTING MECHANISMS, AND DENYING MOTION FOR ESTABLISHMENT OF A MEMORANDUM ACCOUNT

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DECISION AUTHORIZING CHANGES IN RATE DESIGN AND RATESETTING MECHANISMS, AND DENYING MOTION FOR ESTABLISHMENT OF A MEMORANDUM ACCOUNT

1. Summary

This decision authorizes a pilot two-tier increasing block water conservation rate design and water revenue adjustment mechanism for the Fontana Water Company (FWC) division and Los Angeles County (LAC) division of the San Gabriel Valley Water Company, effective July 1, 2010. It denies requests for conservation memorandum accounts and for a memorandum account to track certain expenses relative to this proceeding.

The conservation rate design adopted in this decision is a procedural methodology in which the parameters of service charge-to-quantity charge ratios, a low-income service charge discount, the number of pricing tiers and the rate differentials between tiers are determined, but specific rates are not. Specific rates are not calculated because they are dependent on revenue requirements that have been changing during the course of the proceeding and are expected to change further before the conservation rate design takes effect on July 1, 2010. The methodology adopted, composed of nine sequential steps, is set out in Figure 1: Conservation Rate Design Procedure.

Monthly residential water bills are composed of a "service charge" based on water meter size and a volumetric "quantity charge" based on the amount of water, measured in hundred cubic foot units (ccf), the customer has consumed. For the customer with a typical residential water meter (5/8" x ¾") the new rate design reduces the monthly service charge. (Illustrative examples, based on recent but now dated data, of monthly service charges for all residential meter

sizes are provided at Table B, Illustrative Examples of Residential Service Charge Rates, in the Attachment).

The adopted rate design calls for a higher proportion of the total annual revenues to be derived from quantity charges than is the case under the current single-tier rate. A comparison of this adopted rate design with those requested by the San Gabriel Valley Water Company and proposed by the Division of Ratepayer Advocates, respectively, is provided in Table A, Comparison Chart of Illustrative Examples and Proposed Residential Conservation Rates, in the Attachment.

The usage break point that is set between tier 1 and tier 2 in each division (through 16 ccf for the FWC division and through 13 ccf for LAC division) approximates the median winter water use. Over the years 2003-2008 the average monthly residential use was 25 ccf for the FWC division and 20 ccf for the LAC division. In neither division will the residential tiered rates be applied to apartments or trailer parks.

For customers on a typical sized residential meter the water quantity rates in the FWC division for tier 1 usage (0 through 16 ccf per month) will be 15% less than those for tier 2 usage (17 ccf per month and above). Based on 2003-2008 average monthly residential use, approximately 57% of the water sold to residential customers is expected to be billed at tier 1 rates, and 43% at tier 2 rates.

For customers on a typical sized residential meter in the LAC division the water quantity rates for tier 1 usage (0 through 13 ccf per month) will be 15% less than those for tier 2 usage (14 ccf and above). Based on 2003-2008 average monthly residential use, approximately 55% of the water sold to residential customers is expected to be billed at tier 1 rates, and 45% at tier 2 rates.

Low income households in each division will have the benefit of a 50% discount from what their service charge would have been under traditional ratemaking.

San Gabriel Valley Water Company is required to report a range of information that will be available for later evaluation of how the pilot conservation rate designs in the two divisions have worked in practice.

With this decision, the proceeding is closed.

2. Background

2.1. The Commission's Water Conservation Rate Design Initiative

In its 2005 Water Action Plan (WAP), the Commission included among its objectives the strengthening of conservation programs among the investor-owned water utilities to a level comparable to the conservation plans of the energy utilities.[1] In part, this called for "the elimination of flat-rate and un-metered water service" and the encouragement of "increasing conservation and efficiency rate designs (such as increasing block rates) where feasible to promote greater conservation."[2] The Commission announced that it would direct the Class A and Class B water utilities to participate in the California

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[1] WAP, California Public Utilities Commission (December 15, 2005) at 7.

[2] *Id.* at 7-8. Increasing block rate designs charge a higher price for higher levels of consumption. The WAP at 9, cautioned "Before instituting increasing block rates, however, the Commission will carefully consider the impact on low income customers and may develop specific low income water rates, similar to its approach for low income energy ratepayers."

Urban Water Conservation Council (CUWCC) and follow the cost-effective Best Management Practices of the CUWCC.[3]

On January 16, 2007, the Commission ordered an investigation of water conservation policies, Investigation (I.) 07-01-022 (Water Conservation OII), relative to Class A water utilities. That proceeding, which led to the settlement of several consolidated water conservation rate design matters,[4] is now in its second phase. When the Commission adopted a revised rate case plan for Class A water utilities in 2007, it set out a list of conservation and efficiency directives, including a mandate to submit a plan for reducing average customer water use 5% during the three-year general rate case (GRC) cycle.[5]

San Gabriel Valley Water Company (San Gabriel) filed an application for its FWC on August 10, 2007 seeking, in part, authority to fund and implement the Commission's WAP objectives and to establish a Conservation Memorandum Account to record costs of water conservation activities for potential subsequent

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[3] *Id.* at 8-9, 24-27 (Appendix A). One of the Best Management Practices (BMPs) of the CUWCC, BMP No. 1.4 (formerly No. 11), calls for using a price signal as an economic incentive for the customer to conserve. The BMPs are available in Exhibit 1 of the Memorandum of Understanding Regarding Urban Water Conservation in California, available at:
http://www.cuwcc.org/uploadedFiles/Resource_Center/MOU/MOU-08-12-10.pdf

[4] The applications and water utilities involved with the settlements were Application (A.) 06-09-006 (Golden State Water Company), A.06-10-026 (California Water Service Company), A.06-11-009 (Park Water Company), A.06-11-009 (Suburban Water Systems), and A.07-03-019 (San Jose Water Company). While San Gabriel is a party to the investigation proceeding, its application, the subject of the instant proceeding, was not consolidated with, and remains outside, the investigation proceeding.

[5] Decision (D.) 07-05-062 at A-29 and A-30.

recovery in rates.[6] In a decision adopting a settlement between San Gabriel and the Commission's Division of Ratepayer Advocates (DRA), the FWC was authorized to establish an interim surcharge consisting of three components (conservation programs, conservation specialists, and additional payroll-related expenses) to fund the conservation programs and activities authorized by the decision.[7]

In early 2008 Governor Schwarzenegger set a goal of 20% statewide per capita urban water use reduction by 2020.[8] In February of 2008 the Commission announced an intention to meet a goal ranging, "at a minimum, from a 3%-6% reduction in per customer or service connection consumption every three years once a full conservation program, with price and non-price components, is in place."[9]

Of late, in November 2009, new state legislation was enacted that mandates the 20% urban-use reduction by the end of 2020, with an interim incremental reduction of 10% by the end of 2015 and the development of standardized water use reporting.[10] Each urban retail water supplier of sufficient

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[6] A.07-08-017, filed August 10, 2007, *In the Matter of the Application of San Gabriel Valley Water Company (U337W) for approval of Implementation by its Fontana Water Company Division of the Commission's Water Action Plan objectives, including a request to utilize existing Facilities Fees revenues, for such purposes or in the alternative, for authority to increase rates not to exceed $882,200 or 2%.*

[7] D.08-08-018.

[8] A multi-agency undertaking to develop a "20x2020 Water Conservation Plan" has been evolving since then.

[9] D.08-02-036 (Phase 1A decision in the water conservation OII) at 11.

[10] Senate Bill 7 (7th Ex. Sess.), adding new Part 2.55 (Sustainable Water Use and Demand Reduction) in Division 6 of the California Water Code, §§ 10608-10853. San Gabriel attached a copy of Part 2.55 to its Reply Brief.

size, whether publicly or privately owned,[11] must select and adopt a method among several alternatives given for arriving at its urban water use target.[12] Those suppliers are to include in their 2010 Urban Water Management Plans "baseline daily per capita water use," conservation targets and references to supporting data.[13]

Against the foregoing 2005-2009 backdrop, it is noteworthy that the instant proceeding on San Gabriel's application is the only water conservation rate design matter that has both gone through full evidentiary hearing and not settled. Also noteworthy is the fact that San Gabriel has been reclassifying some large-use customers from the residential to the non-residential class. Late in the instant proceedings San Gabriel finished compiling data on five years of residential customer water usage in each of its divisions. The results show residential usage reductions from 329 ccf to 311 ccf, or 5.5% in the FWC division and from 273 ccf to 235 ccf, or 14% in the LAC division.[14] In terms of overall water production[15] not disaggregated by customer class, the July 2008 through June 2009 drop for FWC was 5.1% and for LAC was 6.1%; the month of June 2009

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11 The definition includes a water supplier "that directly provides potable municipal water to more than 3,000 end users or that supplies more than 3,000 acre-feet of potable water annually at retail for municipal purposes," California Water Code § 10608.12(p).

12 Water Code § 10608.20(b).

13 Water Code §10608.20(e).

14 SG Exhibit 5, Additional Supplemental Testimony of Daniel A. Dell'Osa at 5:line 13-line 14, line 25–line 26.

15 While water production, the amount of water introduced to a utility's system, is not equivalent, due to system losses, to customer water use, reductions in production translate into reductions in use.

showed a drop of 16% compared to June 2008 for FWC and 16.2% for LAC.[16] These usage, reclassification and production data are subject to differing interpretations,[17] leaving unclear the extent, if any, to which San Gabriel, without tiered conservation pricing, has been approaching or meeting the Commission's water conservation goals in terms of the rate of annual improvement in reduced residential water use.[18]

2.2. Procedural History of the Application

On September 10, 2008, San Gabriel filed this application, requesting that the Commission authorize (1) a conservation rate design and rates, (2) revenue decoupling mechanisms, and (3) conservation memorandum accounts to capture program costs for San Gabriel's LAC and FWC divisions. The application was filed in response to Ordering Paragraph 13 of the Commission's Decision (D.) 08-06-022.[19] Protests to the application were timely filed by the Consumer

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16 *Id.* at Attachment 3.

17 The Division of Ratepayer Advocates attributes the reductions to the reclassification of large-use customers from the residential class to the non-residential class. *See* Comments of the DRA on the Proposed Decision of Administrative Law Judge Weatherford, January 21, 2010 at 3. San Gabriel reaches the opposite conclusion in its Reply Comments, January 26, 2010 at 1-2.

18 D.08-02-036 at 11, fn. 14, stated: "Until we finalize a targeted reduction in consumption, Class A water utilities shall comply with D.07-05-062's required water conservation plan by stating how price and non-price programs will achieve reductions of 1% to 2% annually during the GRC cycle." The Commission expects to finalize the targeted reductions in Phase 2 of the Water Conservation OII, Investigation (I.) 07-01-022.

19 San Gabriel Valley Water District "shall file a conservation rate design application, including a Water Revenue Adjustment Mechanism, modified cost balancing account and conservation memorandum account proposals for its Divisions with[in] 90 days of issuance of this decision. That application shall be coordinated with its Fontana

Footnote Continued on Next Page

Federation of California (CFC)[20] and the City of Fontana (City).[21] Commissioner John Bohn and Administrative Law Judge (ALJ) Jonathan Lakritz were assigned to the proceeding. DRA was authorized to file its protest[22] late through an October 17, 2008 e-mail from ALJ Lakritz. On October 27, 2008, San Gabriel filed a response to the protests.

At the November 10, 2008 prehearing conference (PHC), ALJ Lakritz, on behalf of the assigned Commissioner, expressed concerns that San Gabriel's proposal for a unitary water conservation rate, plus surcharge, as opposed to a tiered increasing block design, was not satisfactory and suggested that San Gabriel submit supplemental testimony to propose a multi-tier water conservation rate design more consistent with those the Commission has adopted for other Class A water companies. In its December 1, 2008 response, San Gabriel determined that it would be appropriate and beneficial to supplement its testimony previously served in this proceeding by submitting an alternative rate design proposal that employed multiple tiers. San Gabriel also indicated that it might include revisions to its proposal for a form of water revenue adjustment mechanism (WRAM).

Division's July 2008 GRC application and may be consolidated with Investigation 07-01-022." D.08-06-022 at 73, Ordering Paragraph 13, in A.07-07-003.

[20] CFC contended that the proposed rates would result in excess revenue, discriminated by sparing classes of customers a conservation surcharge, lacked conservation incentives and were not grounded on cost of service as required by Pub. Util. Code § 701.10.

[21] City asserted its interest in having ratepayer classes treated fairly and conservation fostered without unduly burdening ratepayers.

[22] DRA, among other things, criticized the single quantity rate/surcharge approach, contrasting it with the increasing block designs adopted by other Class A investor owned water utilities, and argued that revenue neutrality was lacking.

After being granted a week's extension by ALJ Gary Weatherford, to whom the proceeding had been assigned in mid-January 2009, San Gabriel served Supplemental Direct Testimony on February 25 that proposed, for each division, a two-tier residential customer class alternative conservation rate design and a WRAM to track variances in revenues between recorded sales at tiered quantity rates and at uniform single-block rates. On March 27, 2009, DRA moved for a clarification of San Gabriel's proposals.[23] On March 30, 2009, ALJ Weatherford ordered the parties to consult and confer for the purpose of trying to reconcile conflicts between San Gabriel's Application and its Supplemental Testimony. San Gabriel and DRA reported to ALJ Weatherford on April 3, 2009, that such reconciliation had been achieved. San Gabriel then served revised direct testimony reflecting the reconciliation, providing a basis for DRA to prepare and, after having been granted an extension by ALJ Weatherford, serve its report.[24] DRA served revisions to its report[25] on June 3, 2009.

Public participation hearings were conducted by ALJ Weatherford in Fontana and El Monte on June 24 and 25, 2009, respectively.[26] Transcripts of

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[23] Motion of DRA for Clarification of Proposals Set Forth in A.08-09-008 and Supplemental Testimony and Motion to Shorten Response Period.

[24] DRA Exhibit 101, Report on the Application of San Gabriel Valley Water Company for Authority to Establish Conservation Rate Designs, Water Revenue Adjustment Mechanisms, and Conservation Memorandum Accounts (served on May 29, 2009).

[25] DRA Exhibit 102, Errata to Report on the Application of San Gabriel Valley Water Company for Authority to Establish Conservation Rate Designs, Water Revenue Adjustment Mechanisms, and Conservation Memorandum Accounts.

[26] Communities served by the FWC division include portions of Fontana, Rancho Cucamonga, Rialto and vicinity in San Bernardino County. Communities served by the LAC division include portions of Arcadia, Baldwin Park, El Monte, City of Industry,

Footnote Continued on Next Page

those hearings are part of this record. Among the concerns expressed by speakers in Fontana were water bill impacts upon customers with outdoor vegetation and fruit trees, and upon multi-family customers on the same meter; effects of pipeline breakage and leakage; and customer confusion due to multiple notices of proposed changes in rates and cost of capital. In El Monte, the concerns included the following subjects: water utility spending and earnings; impacts on gardens, large-lot ("light agriculture") owners, orchard owners, neighborhood appearance and dust control, horse owners, swimming pools, multi-dwelling parcels and extended-family or multi-family residences; wholesale water charges, if any; the impact of new and proposed development on local water supplies; the compatibility, or not, between the company's conservation goals and policies of local governments; qualifications for the low-income alternative rate program; and possible misclassification of customers.

Rebuttal testimony by San Gabriel to DRA's Report was served on July 10, 2009. On July 23, ALJ Weatherford requested supplemental testimony of San Gabriel and DRA bearing on marginal cost rate setting, water consumption data, indoor and outdoor water use, and the prospect of tier crossing by extended family households.[27] San Gabriel, DRA, and CFC engaged in Alternate Dispute Resolution in late July that failed to result in any settlement.

Irwindale, La Puente, Montebello, Monterey Park, Pico Rivera, Rosemead, San Gabriel, Santa Fe Springs, South El Monte, West Covina, Whittier and vicinity in Los Angeles County.

[27] ALJ Ruling Regarding Supplemental Testimony, Requirements for Settlement, Time Estimates for Evidentiary Hearing and the Scheduling of a Telephonic Prehearing Consultation.

The ALJ-requested supplemental testimony by San Gabriel and DRA was served on August 14, 2009.[28] Included in San Gabriel's supplemental testimony was a three-tier increasing block option.[29] August 14 was also the date on which San Gabriel moved for authority to establish a memorandum account to track the legal and related costs of participating in the instant proceeding.[30] DRA opposed the motion on August 31.[31]

At the outset of the evidentiary hearing on August 19, San Gabriel presented more prepared testimony.[32] That testimony reported on San Gabriel's customer reclassification results as well as on figures showing significant reductions in water consumption during recent years. DRA requested and was granted an extension to analyze this new information. Resumption of the evidentiary hearing was set for September 29, 2009. On August 26, San Gabriel served testimony that updated the three-tier conservation rate design on the basis of refined data.[33] DRA served a proposed exhibit on September 16 showing

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[28] Exhibit SG 4, Supplemental Testimony of Daniel A. Dell'Osa (San Gabriel) and DRA Exhibit 6, Supplemental Testimony on the Application (DRA).

[29] In an August 10, 2009, e-mail ALJ Weatherford asked the parties to be prepared on cross examination to step away from their preferred tiered rate design and suggest a next-best design. San Gabriel was asked to consider a three-tier design and DRA was asked to consider a two-tier design.

[30] Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account.

[31] The DRA's Response to the Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account.

[32] SG Exhibit 5, Additional Supplemental Testimony of Daniel A. Dell'Osa. By e-mail on August 10, 2009, ALJ Weatherford had given leave to each party to respond in writing on August 19 to any other party's August 14 submission.

[33] SG Exhibit 6, Three-Tier Option Testimony of Daniel A. Dell'Osa.

the results of its review of San Gabriel's reclassification of customers.[34] Following that, DRA served a proposed exhibit setting out a two-tier conservation rate design.[35]

At the September 15, 2009, PHC that focused on the process for resolving San Gabriel's then-pending motion seeking authority to set up a memorandum account, ALJ Weatherford informed the parties of his intention to apply the Commission's four-pronged test[36] in ruling on the motion and gave the parties leave to supplement the related factual record by making comments. Comments by San Gabriel were filed on September 25, followed by DRA's on October 27.

Evidentiary hearings both resumed and were concluded on September 29, 2009. Common-outline opening briefs were filed by San Gabriel and CFC on October 27 and by DRA on October 28, followed on November 10 by reply briefs from those parties.

3. Competing Proposals of Parties

3.1. Conservation Rate Designs

The proposals of San Gabriel and DRA described in this section are abstracted on Table A in the Attachment.

3.1.1. Reduced Service Charges

San Gabriel proposes to reduce the FWC service charge from $16.85 to $16.69 and the LAC service charge from $20.04 to $18.36. This was expected to produce a revenue ratio of service charge to quantity charge of 38:62 in FWC and

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[34] DRA Exhibit 107, Significance Test for Customer Reclassification.

[35] DRA Exhibit 108, Response to ALJ Weatherford's Question, served on September 24, 2009.

[36] *See* e.g., Resolution No. W-4276 (July 12, 2001).

34:66 in LAC, in both instances short of the minimum standard of 30:70 promoted by the CUWCC,[37] and which the company seeks to meet in steps. Rate increases since the filing of the application in this proceeding appear to be altering the ratios for the better.[38]

DRA proposes a service charge of $12.25 for FWC and of $13.03 for LAC that would result in ratios of 26:74 and 27:73, respectively.[39] DRA promotes the application of the 30:70 minimum standard to residential customer class revenue, not just to revenue of all customer classes in the aggregate which is the CUWCC formula.[40]

3.1.2. Quantity Rates

3.1.2.1. Tiered Increasing Block Structure

To allocate quantity charges among residential customers, San Gabriel seeks a two-tier increasing block structure. The first tier would cover consumption from 0 to 20 ccf[41] and bear a rate[42] of $1.92 per ccf in FWC, and $1.89 per ccf in LAC. The second tier would apply to all consumption of 21 ccf and above at a rate of $2.11 per ccf in FWC, and $2.08 per ccf in LAC.[43] The rate

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37 *See* BMP 1.4 referenced at *supra,* note 3.

38 RT 168:21-169:5.

39 DRA Exhibit 101 at 13: line 23-line 24.

40 *Id.* at 13:line 16-line 23.

41 San Gabriel borrowed the 20 ccf break point from Suburban Water Systems rather than looking to the indigenous data of FWC and LAC.

42 Unless otherwise indicated, rate figures shown in this decision have been rounded to the closest cent.

43 *See* SG Exhibit 6, Attachment 2 (Updated Table E) at 1.

differential between the first and second tier would be 10% in each of the divisions.

When pressed to conceive of a possible three-tier alternative,[44] San Gabriel fashioned a structure for FWC and LAC in which the first tier covered consumption through 15 ccf, the second tier included 16 ccf through 30 ccf, and the third captured consumption 31 ccf and above. For FWC, the rates would be $1.93, $1.99, and $2.13 per ccf, with a 3% differential between tier 1 and tier 2, and 7% between tiers 2 and 3. Going up the tiers, the rates for LAC would be $1.90, $1.94, and $2.09 per ccf, with a 2% differential between tier 1 and tier 2, and 7% between tiers 2 and 3.[45]

As the proceedings progressed, San Gabriel, citing recent Commission-approved increases in quantity rates, came to take the position that the Commission should not adopt specific rates but instead adopt a rate calculation methodology.[46]

DRA countered San Gabriel's preferred two-tier design with a three-tier design with different breaking points between tiers for FWC and LAC. The first tier for FWC would cover 0 through 16 ccf of consumption; the second would include 17 through 30 ccf; and the third would capture consumption 31 ccf and above. The rates for those tiers would be $1.68, $1.85, and $2.40 per ccf,

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[44] In a July 23, 2009 Ruling, ALJ Weatherford asked San Gabriel and DRA to be ready to have their respective witnesses at the evidentiary hearing move off of their preferred positions temporarily and posit an alternative tier structure, i.e. two tiers for DRA and three tiers for San Gabriel. Subsequently, both parties submitted exhibits in response. *See* SG Exhibit 6 and DRA Exhibit 108.

[45] *See* SG Exhibit 6, Attachment 2 (Updated Three-tier Option Table E) at 1.

[46] Reply Brief of San Gabriel Valley Water Company at 6-7. San Gabriel applied the suggested methodology in its updated Table E in SG Exhibit 6, Attachment 1.

respectively, with a differential of 12% between tiers 1 and 2, and a differential of 30% between tiers 2 and 3. The first tier for LAC would cover 0 through 13 ccf of consumption; the second would include 14 through 21 ccf; and the third would capture consumption of 22 ccf and above. The rates for those tiers would be $1.56, $2.03, and $2.97 per ccf, respectively, with a differential of 29% between tiers 1 and 2, and a differential of 46% between tiers 2 and 3.[47]

When pressed to conceive of a possible two-tier alternative, DRA crafted a seasonal rate structure[48] for FWC and LAC in which different rates applied in the winter and the summer. For FWC, the first tier would cover 0 through 16 ccf of consumption and the second tier would catch all consumption of 17 ccf and above. For the first tier the winter and summer rate would be the same, $1.65 per ccf. For the second tier the winter rate would be $1.85 per ccf and the summer rate would be $2.22 per ccf. The differentials between the two tiers would be 12% in the winter and 35% in the summer. For LAC, the first tier would cover 0 through 13 ccf of consumption, and the second tier would catch all consumption of 14 ccf and above. For the first tier the winter and summer rate would be the same, $1.76 per ccf. For the second tier the winter rate would be $2.03 per ccf and the summer rate would be $2.53 per ccf. The differentials between the two tiers would be 15% in the winter and 43% in the summer.

3.1.2.2. Customer Reclassification and Revenue Neutrality

During the course of this proceeding, San Gabriel has been in the process of reviewing its residential customer lists in its divisions in order to identify

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[47] *See* DRA Exhibit 102, Appendix D (Conservation Rate Design) at 16 and 19.

[48] *See* DRA Exhibit 108.

customers misclassified as residential who should be reclassified as non-residential. During the evidentiary hearings, San Gabriel reported on the then current results of that ongoing effort,[49] revealing that some customers had been misclassified. Correction by reclassification under these circumstances creates a variance between adopted residential quantity-rate revenue and the counterpart revenue that would actually be forthcoming under San Gabriel's proposed rate design. The expected resulting change in the proportional contribution of residential and non-residential sales, respectively, to the total revenue from quantity rates poses the issue of whether San Gabriel's proposal, as affected by customer reclassification, is revenue neutral. San Gabriel addressed this issue by adjusting the adopted quantity-rate residential sales figure downward, using a ratio (comparing before-reclassification to after-reclassification data) based on 5-year average annual residential sales to adjust for customer reclassification.[50] DRA contends that the application of the foregoing methodology by San Gabriel does not achieve revenue neutrality.[51]

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[49] SG Exhibit 5 at 4:line 19-5:line 2.

[50] *See* RT 263:26-266:26; also, Updated Table E attached to SG Exhibit 6.

[51] Reply Brief of the DRA at 5-6:

> In order to verify whether a rate design is revenue neutral, it is necessary to calculate the revenues that [sic] specific rate design will collect for both residential and non-residential customers and compare those with what would have been collected with a uniform quantity rate. San Gabriel still has not done this calculation to verify that its proposal is revenue neutral.

3.1.2.3. Long-Run Marginal Cost

DRA's rate design for FWC was based on long-run marginal cost pricing[52] using an average incremental cost (AIC) methodology.[53] DRA sees expansion of capacity, such as the addition of a well, to be the likely response of a California water utility to increased water scarcity. If current prices are set equal to long run marginal cost in advance of the expansion project, DRA argues, customers will conserve in a manner that could "possibly put off into the future or prevent the necessity of implementing that project, thus lowering costs for ratepayers."[54]

The AIC was not used by DRA to calibrate the third tier in its design for LAC, but rather the second tier, because it turned out that the estimated average incremental cost for that division was the same as the new single quantity rate.[55]

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[52] In DRA Exhibit 101 at 16-17, DRA argues:

> Setting prices such that they reflect the marginal cost of production communicates to customers the cost of increasing production by one additional unit. Setting the highest block rate design to the marginal cost tells customers consuming in that block the cost of increasing their consumption by one unit. This is an important message to send to the customers with the highest usage; customers can then "choose" between maintaining their present consumption and paying for additional production.

Recognizing that the calculation of the AIC for FWC was a "ballpark estimate," DRA refrained from setting the third tier rate at the AIC for an additional well. Rather, it selected a rate that was 50% higher than the current quantity rate in the belief that it approximated the long run marginal cost. *Id.* at 20-21.

[53] *Id.* at 18-19. DRA cites Thomas W. Chestnutt, et al., *Designing, Evaluating, and Implementing Conservation Rate Structures*, CUWCC (July 1997), as authority for the use of marginal cost and average incremental cost pricing in increasing-block water conservation rate setting.

[54] *Id.* at 18.

[55] *Id.* at 21-22.

3.1.2.4. Cost of Service Standard

CFC thinks that San Gabriel's application should be dismissed, primarily arguing that a "cost of service study to determine the cost of serving each customer class" should precede any rate design.[56] CFC believes the setting of conservation rates for only one class of customers, in this instance the residential class, is discriminatory in violation of Pub. Util. Code § 453(c) and § 701.10(b) and (f).[57] Neither San Gabriel nor DRA supports those arguments.

3.1.2.4.1. Extended or Multiple Family Occupancy

San Gabriel has given assurances, in response to customer concerns voiced at the public participation hearings held in Fontana and El Monte, that tiered conservation rates would not be applied to multiple-dwelling units, such as apartments and trailer parks, where high quantity use is aggregated and displayed at a single meter.[58] As to the issue of any unfair impact of tiered rates on the customer bill of a household occupied by a large or extended family, or by

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[56] Opening Brief of the CFC at 3.

[57] § 453(c) provides: "No public utility shall establish or maintain any unreasonable difference as to rates, charges, service, facilities, or in any other respect either as between localities or as between classes of service." § 701.10, in part, declares state policy to be that water rates and charges established by the Commission shall:

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(b) Minimize the long-term cost of reliable water service to water customers.

(c) Provide appropriate incentives to water utilities and customers for conservation of water resources.

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(f) Be based on the cost of providing the water service including, to the extent consistent with the above policies, appropriate coverage of fixed costs with fixed revenues.

[58] Public Participation Hearing, June 24, 2009, Fontana, CA, RT 39:25-40:31.

multiple families, San Gabriel indicated that it currently lacks the data that would be needed to define and address the issue.[59]

In the context of its own three-tier proposal, DRA saw little prospect of an unfair impact based on household size, employing the state standard of 55 to 75 gallons usage per day per person in support of its position.[60]

3.2. Water Revenue Adjustment Mechanism[61]

San Gabriel seeks authority to set up a "Monterey-styled" WRAM in each division to track the differences between revenues for actual metered sales at the block volumetric rate and at the uniform single quantity rate calculated to yield the authorized revenue requirement.[62] This type of WRAM has been authorized for Suburban Water Systems and San Jose Water Company in the consolidated water conservation Order Instituting Investigation (OII).[63] DRA supports the creation of Monterey-styled WRAMs for the divisions.[64]

To address the contingency that the Commission might adopt a rate design like the one proposed by DRA, which arguably would involve a greater risk of sales fluctuations and revenue losses, San Gabriel presented the fallback

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59 Public Participation Hearing, June 25, 2009, El Monte, CA, RT 129:4-21.

60 See California Code of Regulations, Title 23, Section 697, Chapter 2, Article 5, cited in DRA Exhibit 106 at 12:line14-14:line 13.

61 Without an accounting mechanism, water conservation programs can reduce sales to a point where costs cannot be recovered, impacting the finances of the water utility. A WRAM allows positive and negative variances to be later collected from or refunded to ratepayers.

62 SG Exhibit 1 Revised at 5:line 26-6:line 15.

63 *See* D.08-02-036 at 25 (Suburban), and D.08-08-030 at 22 (San Jose).

64 DRA Exhibit 101 at 35:line 1-36:line 3. DRA adds conditions at 38:line 1-40:line 7.

alternative of a full WRAM[65] in a post-hearing brief.[66] DRA opposes that alternative.[67]

3.3. Balancing Account

San Gabriel currently has full cost balancing accounts[68] for FWC and incremental cost balancing accounts[69] for LAC. The LAC accounts track changes in the actual price for pumped water, purchased water and purchased power. The company finds full cost balancing accounts to be superior.[70]

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65 Unlike a Monterey-styled WRAM, a full WRAM adjusts for all variances from an adopted sales forecast, without regard to whether the variances are due to conservation efforts. Full WRAMs were adopted for three Class A water companies (California Water Service Company, Park Water Company, and Golden State Water Company) in Phase 1 of the Water Conservation OII. In its Direct Testimony at 6:line 1-line 15, San Gabriel criticized full WRAMs for their alleged tendency to cause "artificial rate swings in future years," an outcome that it claims "muddles any intended price signals and conflicts with the conservation objective."

66 Reply Brief of San Gabriel at 24-25.

67 Reply Brief of DRA at 6. DRA earlier had indicated, however, that a WRAM/Modified Cost Balancing Account mechanism should be considered as an alternative in the event there was any move toward combining a limited WRAM with a revenue shortfall tracking account. *See* DRA Exhibit 101 at 36:line 14-37:line 7.

68 Full cost balancing accounts track all cost variances. They track the monthly difference between actual cost x actual quantity and the authorized cost x forecasted quantity of purchased water, purchased power or pump taxes.

69 Incremental balancing accounts track variances in costs due to supplier price changes but not variances resulting from the water supply mix. They track the monthly difference between the actual cost x actual quantity and the forecasted cost x forecasted quantity of water sold.

70 SG Exhibit 1 Revised at 6:line 27-8:line 2.

DRA proposes that both divisions have incremental cost balancing accounts, to provide an incentive to reduce purchases of water from the more expensive sources.[71]

3.4. Conservation Memorandum Account

San Gabriel seeks a conservation memorandum account to record the costs of "extraordinary water conservation programs and activities not expressly identified in a prior general rate case."[72]

DRA, while recognizing that the Commission ordered San Gabriel to include a request for such an account in its application,[73] argues that the account is "not necessary or warranted." DRA cites balances in the conservation budgets in both divisions that allegedly are sufficient "to cover unanticipated conservation needs that arise as well as expanded public outreach and education programs," and argues that the account request fails to meet a four-prong test for memorandum accounts.[74]

3.5. Public Outreach and Education

San Gabriel proposes[75] to gather relevant ideas from other southern California agencies and to implement the programs described in its WAP conservation applications approved by the Commission in 2008.[76] It does not

[71] DRA Exhibit 101 at 40:line 9–43:line 3.

[72] SG Exhibit 1 Revised at 8:line 13-line19.

[73] Ordering Paragraph 13 of D.08-06-022 at 73.

[74] DRA Exhibit 101 at 44:line 8-line 21.

[75] SG Exhibit 1 Revised at 9:line 11-line 19.

[76] A.07-08-017 (D.08-08-018) for FWC and A.07-07-003 (D.08-06-022) for LAC.

now expect to expand those programs, but if it were to do so it would want to track the related costs in a memorandum account.[77]

DRA urges the Commission not to authorize any additional funding for any expansion of the foregoing programs, arguing that the unspent balances in the pertinent GRC budgets can cover the costs of the programs and any expansion.[78] DRA asserts that there are no-cost or low-cost opportunities for educating customers through website links and telephone numbers of which San Gabriel should avail itself.[79]

3.6. Low-Income Features

San Gabriel's divisions offer California Alternative Rates for Water (CARW) to low-income households. CARW households receive a 50% reduction in their service charges. While that same fractional benefit would apply under the San Gabriel's proposed conservation rate design, it would be 50% of a reduced service charge.

Recognizing that its own proposal to reduce service charges would lessen the benefits to CARW households, DRA proposes that there be a flat dollar monthly service charge discount for them, amounting to about $8.29 in FWC and about $10.02 in LAC.[80] San Gabriel agrees in principle but has not proposed figures.[81]

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[77] DRA Exhibit 103 at 3.

[78] DRA Exhibit 101 at 50:line 21-53:line 15.

[79] *Id.* at 53:line 16-55:line 17.

[80] DRA Exhibit 101 at 57:line 5-line 13.

[81] RT 194:28.

3.7. Reporting Requirements

San Gabriel sees no need to add to its existing reporting requirements. It points out that its annual report includes customer and sales data by customer class as well as balancing and memorandum account information. It argues for evaluating "usage trends over a period of several years, rather than spot changes during any isolated year because of the multiple independent factors that influence the volume of sales."[82] San Gabriel testified that:

> Water usage by San Gabriel's customers is affected by a great many factors such as population, temperature, rainfall, economics, commercial and industrial needs, technology, consumer preferences, and water conservation programs of other entities as well as our own conservation programs. There are no reliable ways to isolate the water usage of each factor.[83]

DRA wants the company to "collect data on billing and usage per customer or per service connection by meter size, by month, and by class of customer, for use in analyzing customer response" to the conservation rate and WRAM pilot project.[84]

3.8. Effective Date

Both San Gabriel and DRA want the conservation rate design and associated features to become effective July 1, 2010.

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[82] SG Exhibit 1 Revised at 9:line 29-10:line 2.

[83] *Id.* at 4:line15-line 19.

[84] DRA Exhibit 101 at 58:line 9-line 12, asking for the data to be presented at the next GRC for each division in a specific format (at 58:line 16-59:line 14).

4. Analysis and Resolution

4.1. Conservation Rate Design

The conservation rate design adopted in this decision is a procedural methodology in which the parameters of service charge-to-quantity charge ratios, number of pricing tiers and the rate differentials between tiers are determined, but specific rates are not. Specific rates are not calculated because they are dependent on revenue requirements that have been changing during the course of the proceeding and are expected to change further before the conservation rate design takes effect on July 1, 2010. The methodology, composed of nine sequential steps, is set out in Figure 1: Conservation Rate Design Procedure.

Figure 1: Conservation Rate Design Procedure

1. First, calculate division-wide rates by traditional rate design procedures (Standard Practice U-07-W, para. 11) to obtain uniform rates, using GRC-adopted customers and sales quantities and GRC-adopted revenue amounts (as adjusted by subsequently effective advice letters) for the time period during which the proposed rates will be charged.

2. Convert the resulting low-income discount (50% of the service charge according to the CARW customer's meter size) into the dollar amount to apply as the CARW discount.

3. Calculate the amount of any required BMP 1.4 revenue shift from the monthly Service Charges to the Quantity Rates, based on the Commission-adopted targets. [This decision sets these targets as at least 64.6% of the adopted revenue requirement collected from the quantity revenues for the LAC division and at least 72.03% of the adopted revenue requirement collected from the quantity revenues for the FWC division.]

4. Add the dollar amount of the required BMP 1.4 revenue shift determined under Step No. 3 to the adopted Residential Quantity Rate Revenue used in Step No. 1.

5. Calculate the Single (uniform) Quantity Rate to be used in the Water Revenue

Adjustment Mechanism calculation for residential customers by dividing the dollar amount developed in Step No. 4 by the Adopted Annual Residential ccf Sales used in Step No. 1.

6. Segregate the Adopted Annual Residential ccf Sales between the two rate tiers using the adopted percentages. [This decision finds that 55% of the adopted ccf sales quantities will be in the 1-13 ccf/mo. first tier for the LAC division and that 57% of the adopted ccf sales quantities will be in the 0-16 ccf/mo. first tier for the FWC division.]

7. Using the adopted tier 1/tier 2 rate differential, develop tier 1 and tier 2 Quantity Rates for residential customers that are designed to produce the exact same revenues as those produced by the uniform quantity rate determined in Step No. 5. [This decision sets the tier 1/tier 2 rate differential at 15%]

8. Subtract the dollar amount of the required BMP 1.4 revenue shift determined under Step No. 3 from the adopted revenue requirement collected from the service charge for Residential customers.

9. Develop monthly service charges by meter sizes for residential customers by dividing the service charge revenue calculated in Step No. 8 by the adopted number of residential services. (This monthly service charge will be calculated by taking the service charge derived from the Adopted Residential Revenue Requirement multiplied by one minus the required BMP 1.4 percentage revenue shift and multiplying this product by Commission-adopted meter ratios to develop service charge rates for each meter size.)

4.1.1. Reduced Service Charges and BMP 1.4 (30:70) Ratio

We find San Gabriel's proposed steps toward the minimum CUWCC revenue ratio of 30:70 (service charge: quantity charge) to be too modest and DRA's proposed realignment of service[85] and quantity charges to be excessive.

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[85] In this proceeding DRA has sought to apply the 30:70 ratio using customer class quantity revenue, not total quantity revenue (residential and non-residential) as provided in BMP 1.4. We find that approach to be too aggressive for this pilot conservation rate design.

The reduced monthly service charge figures[86] will be calculated to result in a service-charge-to–quantity-charge ratio[87] of 28:72 in FWC, exceeding the BMP 1.4 minimum standard (30:70), and of 35:65 in LAC,[88] moving toward but not reaching that standard. The movement from a 38:62 ratio to 28:72, slightly surpassing the CUWCC 30:70 threshold, is reasonably achievable in one step and will further the water conservation objectives of the Commission. The shortfall for LAC is justifiable in this pilot conservation rate design due to the considerable distance, from 46:54 to 30:70, that the LAC rate design has to travel. The incremental step authorized here for LAC is reasonable in light of that gap. We will expect, however, to see San Gabriel reach, if not exceed, the 30:70 ratio in its 2010 GRC rate plan for the LAC division. While we are only changing the rate design for residential customers, that change causes a change in the overall ratio that comprehends all customers, residential and non-residential.

4.1.2. Quantity Rates

4.1.2.1. Tiered Increasing Block Rate Structure

As discussed above, San Gabriel prefers a two-tier, and DRA a three-tier, rate design. The percentage difference in rates between the two tiers in San Gabriel's proposal is 10. Rather than relying on customer usage data from within its own divisions, San Gabriel borrowed its breaking points, 20 ccf for

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86 Table B of the Attachment provides illustrative examples, based on recent but now inapplicable revenue requirement data, of monthly service charges for all residential meter sizes.

87 Unless otherwise indicated, the components of ratios shown in this decision are rounded to the closest two digits.

88 Not rounded, those respective ratios are 27.97:72.03 for FWC and 35.40:64.60 for LAC. *See* Table 1.

each division, from the rate design of Suburban Water Systems,[89] an approach that DRA criticized and that we discourage.

In DRA's proposal for FWC, the percentage difference between tiers 1 and 2 is 12, and between tiers 2 and 3 is 30; for LAC the percentage difference between tiers 1 and 2 is 29, and between tiers 2 and 3 is 46. We find the DRA proposal to be imbalanced. DRA's proposal would reduce a larger number of residential bills by placing an extraordinarily higher burden on the highest tier, benefitting to an unreasonable extent those customers situated exclusively in tier 1. We do not find an adequate record to resolve the issue, posed by DRA's proposal, whether tier 1 customers whose bills would be less than before would have an incentive to use less or more water.[90]

In lieu of adopting any of the two rate designs preferred by San Gabriel and DRA, respectively, or any of the two alternate tiers designs posed by them in response to the ALJ's request, we adopt a two-tier conservation rate design without seasonal rates, with a 15% differential between tiers for each division, with different water-usage breaking points approximating median winter water use[91] between tiers 1 and 2, for FWC and LAC. A differential of 15% lies within the percentage used in the conservation rate designs adopted by the Commission for Class A water companies to date[92] and strikes a reasonable balance between a

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[89] SG Exhibit 2 at 13:line 1-line 5.

[90] *See*, e.g., Opening Brief of the DRA at 14.

[91] Reliance is placed here on the median winter water usage calculations done by DRA, explained in its Exhibit 101 at 27:line 7-line 23, and embodied in the break points between tiers 1 and 2 of its preferred three-tier proposal and alternative two-tier seasonal proposal (*see* Table A in Attachment to this decision).

[92] *See* SG Exhibit 2, at Table D, Summary of Adopted Conservation Rates.

differential that would provide too little and one that would provide too aggressive an incentive for reducing consumption. The specific rates for each tier in each division are to be calculated using the Conservation Rate Design Procedure provided in Figure 1. In developing the illustrative examples of tiered rates in Table A of the Attachment, we utilized data from DRA worksheets.[93]

In FWC, the quantity rates will be calculated for tiers 1 and 2, respectively, with the breaking point between the tiers at 16 ccf. Approximately 57% of the sales for residential bills are expected to come from tier 1 and 43% from tier 2.[94]

In LAC, the quantity rates will be calculated for tiers 1 and 2, respectively, with the breaking point between the tiers at 13 ccf.[95] Approximately 55% of the sales for residential bills are expected to come from tier 1 and 45% from tier 2.[96]

We adopt this particular increasing block design for several reasons. It is founded on median winter water use which is a rough measure in residential settings of indoor water use that, in turn, tends to be less discretionary than outdoor water use. This means that usage within tier 2 has a greater potential than tier 1 for reduction in response to a higher price signal. We conclude that a pilot two-tier increasing block residential conservation rate design is superior to a three-tier design for the FWC division and the LAC division due to its

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93 Worksheets 1 and 2 for FWC and LAC, respectively, in Appendix D of DRA Exhibit 101 as revised by DRA Exhibit 102.

94 Using 2003-2008 as a base period and applying the 16 ccf break point, the respective percentages are 56.75% and 43.25%.

95 Over the years 2003-2008 the average monthly residential use was 25 ccf for the FWC division, and 20 ccf for the LAC division. DRA Exhibit 101 at 14, Table 1, and 15, Table 2.

96 Using 2003-2008 as a base period and applying the 13 ccf break point, the respective percentages are 55.08% and 44.92%.

comparative simplicity, ease of implementation and capacity to capture conservation potential without unduly burdening a small segment of customers.

4.1.2.2. Revenue Neutrality

Following the Conservation Rate Design Procedure set out in Figure 1 should assure revenue neutrality in the conservation rate design. The proposed rate design is revenue neutral in that the revenue derived through the tiered rate design equals the revenue derived through a uniform rate design. Also, when the Commission's most recent adopted revenue requirement is used as an input to this rate design model, the model will calculate the proper increasing block rates and will be revenue neutral.

4.1.2.3. Long-Run Marginal Cost

In addition to its immediate proposal, DRA is also urging that AIC should become "a guideline in future rate designs" concerning San Gabriel.[97] DRA may be viewing this proceeding as a suitable vehicle to begin a Commission initiative applying long-run marginal cost pricing to Investor-Owned Utility (IOU) water rate setting similar to what has been done for some years in IOU energy rate setting. Long-run marginal cost has not been an overt factor in the conservation rate designs adopted within the aegis of the Water Conservation OII.

We do not utilize marginal cost pricing, short- or long-run, in the rate design adopted in this decision for two reasons. First, we do not find the

[97] DRA Exhibit 101 at 22:line21. DRA specifically calls for San Gabriel to be required to provide an AIC estimate in the next GRC: "The sources for potential capacity expansion should all be considered, and those which have the highest expected costs should be used to estimate the AIC." *Id.* at 23:line15-line18. Because the Commission has not embarked on a Class-A-wide policy of promoting marginal cost pricing, no such requirement is imposed here.

estimation of capital expansion offered in this proceeding to be persuasive. There was not sufficient evidence that the estimation of capital expansion -- the bringing on line of a new well in each of the divisions -- was based on a realistic projection of supply and demand forecasting or a comparative analysis of either potential capital projects or potential non-capital projects. Second, we think that the application of marginal cost pricing, using the AIC methodology, to IOU water ratesetting raises a host of technical and policy issues best addressed in either a rulemaking proceeding or a larger Class A GRC.[98] To embark on a new departure of the magnitude sought by DRA, without extensive study and deliberation, simply would not be prudent.

4.1.2.4. Cost of Service Standard

CFC contends that "[c]harging conservation rates to only one class is discriminatory" and that it is "also discriminatory to fix rates without any evidence of the cost of serving each class."[99] Since application of the Conservation Rate Design Procedure (Figure 1) will assure revenue neutrality, meaning that the revenue generated by each class of customers will not change under this decision, there is no sound basis for CFC's discrimination argument.[100]

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[98] Our refusal to adopt marginal cost pricing here does not mean that it is without merit or should be irrelevant in the Commission's future setting of water rates. Marginal cost pricing employing the AIC methodology has been promoted by the CUWCC, a recognized authority cited by DRA and relied upon by the Commission in the formulation of its WAP and by the Legislature in its most recent enactment on water conservation, e.g., § 10608.43, California Water Code.

[99] Opening Brief of the Consumer Federation of California at 5.

[100] CFC does not find comfort in "single point in time" revenue neutrality, arguing that the response of residential customers to price signals will result in a lessening of the cost of serving them, with the cost of serving other customers remaining the same. This concern goes to the allocation of the revenue requirement among customer classes, a

Footnote Continued on Next Page

CFC's efforts, based on Pub. Util. Code § 701.10(f),[101] to postpone water conservation rate implementation until cost of service studies are conducted were rejected by the Commission in Phase 1 of the Water Conservation OII.[102] The proper juncture and forum for consideration of cost of service is the GRC, where all the costs of utility operation, as well as the allocation of those costs among customer classes, are considered. For that reason we deny CFC's request to postpone action on a conservation rate design.

4.1.2.5. Extended or Multiple Family Occupancy

To avoid the inequity that would occur from applying tiered conservation rates to apartments and trailer parks, we agree with the promise already offered

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proper subject at a triennial GRC where customer classes are considered in the course of adopting an overall rate design for the water company. The Monterey Style WRAM corrects for the difference between revenue collected under conservation rates and revenue that would have been collected for the same amount of water if it were sold under uniform rate design. Similar to the Commission standard rate design, the utility is at risk for lost revenues from decreased sales (no guarantee the utility will recover adopted fixed cost). Conversely, the utility keeps excess revenues from increased sales.

[101] "The policy of the State of California is that rates and charges established by the commission for water service provided by water corporations shall …

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(b) Minimize the long-term cost of reliable water service to water customers.

(c) Provide appropriate incentives to water utilities and customers for conservation of water resources.

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(f) Be based on the cost of providing the water service including, to the extent consistent with the above policies, appropriate coverage of fixed costs with fixed revenues."

[102] *See* D.08-02-036 at 6-7 and 12-13. The Commission at 12, did indicate that the "reductions in consumption we finalize at the conclusion of Phase 2 shall apply to all customer classes." *See,* also, following an application for rehearing, D.09-06-053 at 12-16.

by San Gabriel that those rates should not be so applied. San Gabriel must vigilantly maintain customer classification and reclassification records so that those types of customers are properly identified and fairly charged.

An unfair impact upon large, extended or multi-family households does not appear likely under the adopted two-tier rate design. Using the lower figure of gallons-per-day (gpd) reasonable domestic use (55 gpd per person), a household of seven in FWC and of five in LAC would not cross over into the second tier. At the higher usage figure (75 gpd) that defines the end of the upper range of reasonable domestic usage, a household of five in FWC and of four in LAC would not cross over into tier 2.[103] Under both examples, of course, greater than median winter use, as occurs with landscape irrigation, could move households of any size into tier 2. At the mid-2010 (LAC) and mid-2011(FWC) GRCs, San Gabriel should summarize incidences, if any, of apparent unfair impact upon large, extended or multi-family households due to the two-tier rate design. In the interim, the Commission plans to address the subjects of "household size and other socio-economic characteristics of customer household

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[103] *See* California Code of Regulations, Title 23, Section 697, Chapter 2, Article 5, as cited in DRA Exhibit 106 at 12:line14-14:line 13, for source of the 55 to 75 gpd range. Section 697 is cautionary, however: "Allowances for domestic use are variable, depending upon the character of the place of use, method of use, character of use and availability of water." The household sizes provided in the text above were calculated by multiplying either the 55 or 75 gpd figure x 30 days, dividing 748 gallons (1 ccf) into that product and dividing that outcome into the break point between tiers 1 and 2 for each division.

composition," among others, in a workshop in Phase 2 of the Water Conservation OII.[104]

4.2. Water Revenue Adjustment Mechanism

The rate designs adopted in this decision for FWC and LAC have a limited, "Monterey-style" WRAM such as authorized for Suburban Water Company and San Jose Water Company.[105] We authorize that style of WRAM here for San Gabriel's divisions, following the primary proposals of both San Gabriel and DRA in that regard.[106] This revenue adjustment mechanism will track the difference between revenue San Gabriel receives for actual metered sales through the tiered volumetric rate and the revenue San Gabriel would have received for the same amount of water if it were sold under uniform, single quantity rates.[107] This ensures that San Gabriel will have no change in revenue per unit of water

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[104] Assigned Commissioner's and Administrative Law Judge's Ruling Setting Comments Pursuant to Decision 09-06-053 (Phase 1) and Second Amended Phase 2 Scoping Memo at 2.

[105] *See* D.08-08-030 (San Jose Water Company), at 22-23, and D.08-02-036 (Suburban Water Systems) at 25.

[106] Neither of the contingencies has occurred under which San Gabriel or DRA would favor, reluctantly as a fall back position, authorization of a full WRAM. *See* discussion at Section 3.2 above. We have not adopted a rate design that would likely cause revenue variability warranting consideration of a full WRAM.

[107] The WRAM will track the actual water amount sold in a month and apply the single quantity rate to result in an adjusted revenue amount for that month. The difference between the adjusted revenue and the actual revenue will be reflected in the balancing account. The account will not track revenues recovered through the service charge. The single quantity rate that will serve as a baseline for the limited WRAM will be set effective July 1, 2010, based on the conservation rate design procedure adopted herein. For an example of the determination of single quantity rates, see the Motion of the Division of Ratepayer Advocates and San Jose Water Company to Approve Settlement Agreement from A.07-03-019, where a discussion on the single quantity rate occurs at 12-13, with a calculation at 14.

sold as a result of adopting conservation rates compared to revenues it would have had under a uniform rate design.

Commencing in 2011, San Gabriel shall include in its annual report to the Division of Water and Audits a report on the revenue over- or under-collected relative to water sales at single quantity rates in each of the two ratemaking divisions during the preceding calendar year by March 31 of the following year. That difference will accrue interest at the 90-day commercial rate. If the WRAM over- or under-collection for any ratemaking area exceeds 2% of that area's total authorized revenue requirement for the preceding calendar year, a tier 1 advice letter[108] is to be filed within thirty days by San Gabriel that requests amortization of the balance in the account, which relates only to the residential class of customers. If the percentage is 2 or less, the account balance is to be amortized in the next GRC.

4.3. Balancing Accounts

There is a sound basis for retaining full cost balancing accounts in the FWC division and incremental cost balancing accounts in the LAC division, and we do so here. The Commission approved full cost balancing accounts for the FWC division in 2004 because "both water production and power supply costs are subject to wide variations and the supply mix is determined by hydrological conditions that are beyond San Gabriel's ability to predict or control."[109] Those conditions do not appear to have changed for the better. Drought conditions continue to highlight the supply uncertainties and variabilities inherent in FWC's lower cost source, Lytle Creek surface water. Tracking all cost variances,

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[108] General Order 96-B (updated as of April 21, 2009), Water Industry Rule 7.3.3.

[109] D.04-07-034 at 62, quoted in testimony of Dell'Osa at RT 200:24-201:13.

including those prompted by actual quantities, of purchased water, purchased power and pump taxes, is therefore warranted for that division.

While San Gabriel has expressed an interest in also having full cost balancing accounts for its LAC division,[110] which relies on a changeable operating safe yield of groundwater from the Main San Gabriel Basin, an adequate record was not established here for such a change. Incremental cost balancing accounts, tracking variances in cost due to supplier price changes, will be retained for the LAC division.

4.4. Conservation Memorandum Accounts

San Gabriel followed the Commission's earlier order when it requested conservation memorandum accounts in its September 2008 application that commenced this proceeding.[111] We do not find a compelling basis in the record, however, for such accounts. San Gabriel has had running balances in the conservation budgets in both divisions[112] that appear sufficient to support expected and unexpected expenses for the public outreach and education programs. Given the relatively low rate of spending and the unspent balances, no indication of any planned expansion in the public outreach and education programs,[113] and our sense of the scale of implementation costs associated with the pilot conservation measures in this decision, San Gabriel has not established

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110 SG Exhibit 3 at 17:line 18-18:line10.

111 Ordering Paragraph 13 of D.08-06-022 at 73.

112 As of March 31, 2009, the unspent funds from the conservation budgets of FWC and LAC totaled a half million dollars. DRA Exhibit 101at 44: line 12-line 17. San Gabriel is in the process of refunding approximately 67% of the authorized conservation budget in the FWC division. RT 178:5-9; also, 192:20-22.

113 Rebuttal Testimony, SG Exhibit 3 at 20:line 1-line 8.

that the expenditures that would be tracked in the memorandum accounts requested would be of a substantial nature. The request for conservation memorandum accounts is denied.

4.5. Public Outreach and Education

San Gabriel is not asking for authority to expand the public outreach and education programs described in its WAP conservation applications approved by the Commission in 2008. We support San Gabriel's stated intent to gather relevant water conservation ideas from other southern California water agencies and to further implement its existing water conservation programs. We believe that the unspent balances in the GRC conservation budgets can cover the costs of the programs going into the next GRC cycles.

During this proceeding, San Gabriel agreed to DRA's suggestions[114] and began to pursue a number of no-cost or low-cost opportunities for educating customers that DRA has suggested.[115] We encourage San Gabriel to continue those efforts.

4.6. Low-Income Features

In D.05-05-015, the Commission authorized San Gabriel to implement a rate relief program for the low-income ratepayers in its FWC and LAC divisions.

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[114] Rebuttal Testimony, Exhibit 3 at 20:line15-line 20:

> DRA recommends several things, including: (1) adding the customer class to the monthly bill, with a call-in telephone number for questions and concerns, (2) including a website and telephone number to the monthly bills for requesting conservation information, and (3) adding links to the company's websites for wholesaler's information. San Gabriel agrees and has already begun to implement these recommendations.

See, also, Hearing Transcript at 171:line25-172:line 10.

[115] Report, Exhibit 101 at 53:line 19-55:line 17.

This CARW program currently provides a discount of 50% of the service charge for qualifying customers. For example, this equates to a current dollar discount of $8.43[116] per month for qualifying customers in the FWC division, and $10.02[117] per month for qualifying customers in the LAC division, based on the unique service charges currently authorized for each division for a residential customer with a 5/8" x ¾" meter.

With the Commission's reduction of the service charge as part of its implementation of water conservation rate design, unless some alternative form of the authorized CARW discount is determined, qualifying customers in the FWC and LAC divisions would receive a lower discount than has previously been authorized. In order to maintain the same dollar discount currently authorized for qualifying San Gabriel customers with 5/8" x ¾", ¾", and 1" meters, we authorize in each division a CARW discount equivalent to 50% of the residential service charge under traditional rate design. This avoids any loss of benefit that would result from applying the existing percentage discount. In the next GRC, San Gabriel shall propose a new method for determining CARW discounts that results in a discount comparable to that which qualifying customers received in the last GRC for that division, independent of the amount of the authorized service charge.

4.7. Reporting Requirements

San Gabriel has highlighted the apparent fact that multiple and largely unquantifiable factors, not solely price signals, underlie any pattern of reduced

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116 Service Charge for 5/8" x ¾" meter of $16.85/2 = $8.425; Tariff Sheet 1903-W, D.09-06-027.

117 Service Charge for 5/8" x ¾" meter of $20.04/2 = $10.02; Tariff Sheet 1839-W, D.08-06-022.

residential water consumption. Data currently either do not exist, or are not in a usable format, for either San Gabriel or the Commission to quantify and weigh the influence of factors such as the weather, evapo-transpiration, household size, outdoor plant mix, landscape footprint, customer income and conservation education. The time and cost of designing and implementing a long-term pilot to gain a better handle on factors that may influence consumption would be prohibitive at this juncture. While this uncertainty prevents a reliable determination of the relative contribution made by price signals to reduced consumption, it should not prevent an effort to collect the most accessible data on water usage as is practicable at this time.

San Gabriel shall provide the following information in the GRC filing in July 2011 for FWC and July 2013 for LAC:

- Monthly per customer or service connection changes in consumption (compared to the same month in the previous year) by ratemaking division, separated by meter size and customer class, following the implementation of the conservation rate design pilot program;
- Surcredits and surcharges by ratemaking division and customer class implemented in amortizing WRAMs;
- Meter-reading errors, by division, that cause an unjustified crossing of tiers or retention within tiers;
- Number of low-income program participants disconnected for nonpayment by ratemaking division for two years before adoption of conservation rate design and for each year after that adoption;
- Number of residential disconnections for nonpayment by ratemaking divisions for two years before adoption of conservation rate design and for each year after that adoption; and

- Any other ratemaking division-specific factor that might contribute to consumption changes and an estimation of its impact.

As discussed above in Section 4.2 San Gabriel is to make WRAM-related reports within its annual reports.

San Gabriel shall track significant changes in the cost of purchased water and make a showing in its 2011 GRC for FWC and 2013 GRC for LAC that it has exercised due diligence in ensuring the least-cost mix for its water sources and that any significant change in water purchases was reasonable.

4.8. Effective Date

The effective date for the conservation rate design and associated features shall be July 1, 2010, as recommended by San Gabriel and DRA.

5. Motion for Memorandum Account

5.1. Arguments of San Gabriel and DRA

San Gabriel has moved for authorization to open a memorandum account "to track and potentially recover in a future general rate case [costs] limited to the outside attorneys' fees, costs of providing public notices, travel costs, and other 'out-of-pocket' costs that would not have been incurred had San Gabriel not been required to pursue this water conservation rate design application."[118]

San Gabriel cites as precedent the allowance of memorandum accounts in D.08-02-036 at 46, for all Class A water companies to cover the costs of participation in the Investigation to Consider Policies to Achieve the

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[118] Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account, filed August 14, 2009 at 1. *See*, also, Comments of San Gabriel Valley Water Company in Support of Motion for Authorization to Open a Memorandum Account, filed September 25, 2009.

Commission's Conservation Objectives for Class A Water Utilities, I.07-01-022 (Water Conservation OII).[119] Included in San Gabriel's request are "costs of preparing and filing [the A.08-09-008 Application], or at least to the extent of costs incurred since that application was filed in [sic] September 10, 2008."[120] San Gabriel argues that its request meets five conditions established previously for memorandum accounts.[121]

In response, DRA argues that San Gabriel's "late stage" request should have been made earlier in the context of the regulatory expense budget at a GRC; that it comes too late to be the subject of discovery and evidentiary hearings; that it does not meet the conditions for memorandum accounts described in Resolution W-4276, D.02-08-054, and D.04-06-018; that it is distinguishable from the circumstances underlying the memorandum accounts authorized in the Water Conservation OII; and that it runs counter to the prohibition against retroactive ratemaking (Pub. Util. Code § 728).[122]

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119 *Id.* at 1-4.

120 *Id.* at 9.

121 San Gabriel's Motion for Authority to Open a Memorandum Account at 5, cites and quotes five factors enumerated in para. 25 of Standard Practice U-27-W.

122 The Division of Ratepayer Advocates' Response to the Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account, filed August 31, 2009. *See*, also, Reply Comments of the Division of Ratepayer Advocates Opposing San Gabriel Valley Water Company's Motion for Authorization to Open a Memorandum Account, filed October 27, 2009.

5.2. Analysis and Discussion

5.2.1. Memorandum Accounts in Water Conservation OII

There has been pending before this Commission a proposed decision[123] that would affirm, after rehearing, D.08-02-036's approval of a memorandum account for all Class A water utilities to track legal and related expenses incurred in the Water Conservation OII proceeding. We find that the approval of memorandum accounts in the OII proceeding is not controlling here as there are material differences on the merits between that situation and this.

San Gabriel did request that its application be consolidated with the pending OII,[124] something that the Commission itself had earlier posed as a possibility.[125] That request was not granted. Had it been, San Gabriel would have gained the advantage of the Commission's generic authorization in the OII of memorandum accounts for all the Class A water utilities incurring costs of participation in the OII.[126] Reasonable bases existed for the Commission choosing not to consolidate the instant proceeding into the OII. Phase 1B of the OII, involving five settlements, went to hearings and resulted in D.08-08-030 issued on August 25, 2008. San Gabriel filed its application on September 10, 2008, placing it out of sync with the progression of the OII that was moving on into Phase 2, a quasi-legislative stage of the proceedings dealing with non-rate-

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[123] *See* Proposed Decision of ALJ Janice Grau, mailed January 26, 2010.

[124] Application at 5, para. 12.

[125] D.08-06-022 at 73, Ordering Paragraph 13, indicating that the conservation rate design application that it was ordering San Gabriel to file "may be consolidated with Investigation 07-01-022."

[126] D.08-02-036 at 45-47 and 56-57 (Ordering Paragraph 5).

design conservation measures. Unlike the instant proceeding, Phase 1 of the OII involved an accession of multiple parties, including five consumer groups, considerable controversy, and extensive settlement negotiations that extended the proceedings. Also, the authorization of a memorandum account there extended only to expenses related to settlement negotiations and litigation of the consolidated applications after the issuance of the OII, unlike the application preparation expenses sought by San Gabriel here.

San Gabriel waited eleven months after filing its application, and until two weeks before the evidentiary hearing, before filing its motion for a memorandum account. [127] We have considered the equities surrounding San Gabriel having lost the memorandum-account benefit that consolidation would have brought the company. After taking into account the timing of San Gabriel's application and its motion, and of differences between the OII proceeding and the instant one, we conclude that the equities, on balance, weigh against San Gabriel gaining the advantage of the approval of memorandum accounts in the OII proceeding.

5.2.2. Motion in this Proceeding

5.2.2.1. Purposes of Memorandum Accounts and Conditions for Their Authorization

A memorandum account allows a utility to track costs arising from events that were not reasonably foreseen in the utility's last GRC. By tracking these costs in a memorandum account, a utility preserves the opportunity to seek recovery of these costs at a later date without raising retroactive ratemaking issues. However, when the Commission authorizes a memorandum account, it

[127] San Gabriel could have filed an advice letter under Standard Practice U-27-W shortly after it filed its application in this proceeding.

has not yet determined whether recovery of booked costs is appropriate, unless so specified.

We have not applied a fixed set of factors in determining whether to establish memorandum accounts for water utilities. Some of the factors we have considered were articulated in Resolution No. W-4276, D.02-08-054, and D.04-06-018, as DRA notes. In Standard Practice U-27 W, paragraphs 25 and 44 contain similar lists of factors. Even when the Commission has applied these factors, it has not always applied all of them or required that they all be met before authorizing a memorandum account. Thus, at different times, the Commission has considered all these factors, considered only some of these factors, or relied on other public policy considerations in determining whether to authorize a memorandum account. Regardless of the specific factors considered, the question presented to the Commission in all instances is whether a utility should be permitted to seek recovery of these costs at a later date without encountering retroactive ratemaking issues.

We find the factors identified first in Resolution No. W-4276 (also in D.02-08-054 and D.04-06-018) useful in considering San Gabriel's request. In that resolution, the Commission described that memorandum accounts are appropriate when the following conditions exist:

- The expense is caused by an event of an exceptional nature that is not under the utility's control;
- The expense cannot have been reasonably foreseen in the utility's last GRC and will occur before the utility's next scheduled rate case;
- The expense is of a substantial nature in the amount of money involved; and
- The ratepayers will benefit by the memorandum account treatment.

As explained below, we find that San Gabriel's request is not consistent with these factors. We therefore deny San Gabriel's memorandum account motion.

5.2.2.2. First Factor: "Caused by an event of an exceptional nature that is not under the utility's control"

San Gabriel rightly asserts that the filing of the instant application was mandated by the Commission.[128] To that extent this proceeding certainly is "not under the utility's control." But are the doings of this compulsory proceeding "events of an exceptional nature"? San Gabriel believes so, arguing in part that "[r]ate design is normally addressed in periodic general rates [sic] cases, as specified in the Rate Case Plan (D.07-05-062)."[129] DRA counters that compulsory filings are not exceptional at the Commission, particularly when compared to something like the "rolling blackouts of 2001."[130]

By mid-2008 there had been numerous actions by the Commission reflecting our policy of promoting water conservation among the Class A water IOUs.[131] Increasing block rates were among the mechanisms identified in the Commission's WAP in late 2005. The January 2007 Water Conservation OII sought comments on increasing block rates. In August 2007 San Gabriel applied for authority to implement WAP features in its FWC division, prevailing in a

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[128] Ordering Paragraph 13 of D.08-06-022.

[129] Comments of San Gabriel Valley Water Company in Support of Motion for Authorization to Open a Memorandum Account at 3.

[130] The DRA's Response to the Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account at 5, fn. 7.

[131] *See* discussion at in Section 2.1 above.

Commission decision in August 2008. Against this backdrop, we find that a compulsory proceeding to authorize a conservation rate design and related accounts is not an event of an "exceptional nature."

5.2.2.3. Second Factor: "Cannot have been reasonably foreseen in the utility's last general rate case and will occur before the utility's next scheduled rate case"

San Gabriel contends that nothing in the record of the 2007 LAC and General Office GRC, nor in the later 2009-2010 FWC Test Year proceeding, made the prospect or expense of a conservation rate design proceeding reasonably foreseeable.[132] DRA disagrees, stating that San Gabriel should have anticipated the expense as a regulatory expense either in the FWC GRC application filed on July 1, 2008, 17 days after the June 13, 2008 Commission order requiring the filing of a conservation rate design application, or within the 45-day period allowed for updating the GRC.[133] DRA argues that the costs San Gabriel seeks to track in a memorandum account may have been covered by the regulatory expenses authorized by the Commission, which would make them "incremental to costs already included in rates."[134]

Unquestionably, San Gabriel's out-of-pocket expenses for participation in this proceeding will occur before the July 2010 LAC GRC and the July 2011 FWC GRC, satisfying the latter element of this second factor. As noted in the

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132 *See* Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account at 7-8, and Comments of San Gabriel Valley Water Company in Support of Motion to Authorization to Open a Memorandum Account at 4-7.

133 *See* The Division of Ratepayer Advocates' Response to the Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account at 5.

134 *Id.* at 5-6.

discussion above of the first factor, the 2005 Water Action Plan and 2007 Water Conservation OII provided notice of the Commission's intention to implement water conservation policies.

The issue is whether that notice made the prospect or expense of a conservation rate design proceeding reasonably foreseeable as of the July 2007 LAC GRC and/or the July 2008 FWC GRC (or within the 45 days after those dates that is allowed for updating). Specifically, would it have been reasonably foreseeable at those times that such an expense would be required before the end of the relevant triennial GRC cycle, i.e., before July 2010 as to LAC and before July 2011 as to FWC?

We conclude that such an expense was not reasonably foreseeable at the juncture of the July 2007 LAC GRC. The trajectory and timing of the Commission's commitment to conservation rate designs was not as clear then as it was a year later in July 2008 when, in our judgment, such an expense was reasonably foreseeable.

Thus, this second factor is met in relationship to LAC but not in relationship to FWC.

5.2.2.4. Third Factor: "Expense is of a substantial nature as to the amount of money involved"

San Gabriel revised its out-of-pocket cost estimate for the instant proceeding from $150,000 to $200,000, having concluded that either figure qualifies as "substantial' and far exceeds the "less than $15,000 per year" that it contends are reflected in rates for "non-GRC regulatory expense."[135] Applying a "significant expense" standard of "equal to or greater than 1% of test year gross revenues," DRA calculated that the initial cost estimate of $150,000 fell short because it represented only 0.14% of San Gabriel's total revenue requirement.[136] Using the standard proposed by DRA (that an expenditure less than 1% of the total revenue requirement is insubstantial for purposes of this factor), the $200,000 estimate would fall short as well.

The Commission has considered a substantiality threshold of 2% of the estimated operating costs in a previous proceeding.[137] Under that standard, the

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[135] *See* Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account at 8, and Comments of San Gabriel Valley Water Company in Support of Motion for Authorization to Open a Memorandum Account at 8.

[136] The Division of Ratepayer Advocates' Response to the Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account at 6, fn. 12, quoting the Rate Case Plan, authorized in D.07-05-062, that states: "A significant expense is equal to or greater than 1% of test year gross revenues," at A-22, Section II.A.1., fn. 3. We note, for context, that cite requires a water utility to submit GRC testimony explaining "significant changes between last adopted figures and recorded amounts."

[137] In D.02-07-011, involving a request for a security memorandum account at 7, the Commission stated:

> Here, we find that the additional expenditures are not clearly required (at least on the bases cited by Cal-Am) and constitute less than 2% of the projected operating costs. Our ratemaking assumes that utility management can and will reassess its priorities to deal with developments of this magnitude. Specifically, Cal-Am may utilize management discretion to allocate funds for capital and expense items to those areas where the expenditure is most necessary, and also to attain its authorized rate of return.

San Gabriel's 2008 annual report revealed a combined operating expense for the two divisions of $58.8 million. San Gabriel's expense estimate of $200,000 is far less than 1% of that combined operating figure.

$200,000 estimate would be only 0.7% of the estimated operating costs in FWC and 0.6% in LAC, and would not be a substantial amount.

We do not need to choose between particular quantitative percentage standards for substantiality in this instance. With the 1% of revenue requirement and 2% of estimated operating costs measures as informative reference points against which to test our judgment, we find, apart from those reference points, that in the context of San Gabriel's total operations the expense sought to be tracked and ultimately recovered is not of a substantial nature.

5.2.2.5. Fourth Factor: "Ratepayers will benefit by memo account treatment"

San Gabriel sees a benefit for the ratepayer in the fact that the expenses tracked in a memorandum account are actual costs and that those costs are recoverable from ratepayers only after a reasonableness finding, compared to forecasted costs under which the ratepayers generally pay earlier and "may either pay more or less than what the utility incurred."[138] DRA repeats its position that San Gabriel fails to show that the expenses are not already recoverable in current rates within already-GRC-approved regulatory expense budgets; further, it cites conduct of San Gabriel in the instant proceeding that it alleges has not benefited ratepayers.[139]

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[138] Comments of San Gabriel Valley Water Company in Support of Motion for Authorization to Open a Memorandum Account at 8.

[139] The Division of Ratepayer Advocates' Response to the Motion of San Gabriel Valley Water Company for Authority to Open a Memorandum Account at 7-8.

We are not persuaded by San Gabriel's arguments. Reasonableness review is a safeguard[140] that must precede cost recovery in connection with memorandum accounts. As an implicit ratepayer benefit, such review cannot be used as a bootstrap to satisfy the fourth factor which is designed to test the merits of each proposed memorandum account on a case-by-case basis. San Gabriel's further argument that ratepayers can benefit under memorandum account cost recovery, compared to forecasted cost recovery, by paying less and by paying later is speculative in part and does not take into account that within the forecasted-to-actual cost timeline some ratepayers may benefit and others may not from deferred payment.

San Gabriel has not established that its requested memorandum account would benefit ratepayers.

5.2.3. Conclusion

As described above, San Gabriel's request for a memorandum account is consistent with only a portion of the second of four factors that we use to assess the request. The prospect or expense of this conservation rate design proceeding was not reasonably foreseeable at the time of the July 2007 LAC GRC. However, we find that the proceeding is not an event of an exceptional nature, and that the expense is not of a substantial nature. Further, San Gabriel has not established that ratepayers would benefit by the requested memorandum account treatment. For these reasons, we deny San Gabriel's request.

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[140] *See* General Order 96-B, Water Industry Rule 1.8; also, Standard Practice U-27-W (Revised May, 2008) at para. 28: "Advice letter memo account recovery requests require an earnings test and proof of reasonableness."

Although we deny the motion for a memorandum account, we do want to express our belief that a clear, itemized, record needs to be developed in water company rate cases concerning forecasted expenses that may also be proposed for recovery later by a memorandum account. In the face of a request for a memorandum account, the claims and counterclaims over whether an expense is or is not covered by existing rates adopted in a previous rate case are difficult to resolve if relevant facts either are lacking in a record or reside in a settlement which did not fully define the allocated revenue requirement. Going forward, we will be expecting as well developed a record in water company rate cases as practicable in this regard.

6. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Separate opening comments were filed by San Gabriel and DRA on January 21, 2010, and by CFC on January 22, 2010. Separate reply comments were filed by San Gabriel, DRA and CFC on January 26, 2010. San Gabriel and DRA took the common position that the specific quantity rates set out in the proposed decision, and based on already-outdated revenue requirements, ought to be supplanted by a 9-step methodology that would allow rates based on then-current revenue requirements to be set via advice letter. The decision has been revised accordingly, with a nine-step procedural methodology (Figure 1) added to the body of the decision and set out in the Attachment, and illustrative examples of specific quantity rates and service charges placed in Table A and Table B, respectively, of the Attachment.

DRA argued that the data showing recent reductions in water usage were not provable by customer class and argued that those data reflected customer reclassifications only, preventing any sound judgment as to San Gabriel's progress in meeting the Commission's goal regarding residential water conservation. DRA similarly contended that the reported system-wide reductions in water production could not be directly translated into conclusions about reductions in residential use. San Gabriel interpreted the reclassification and production data in the record differently, supporting the relevant portions of the proposed decision. The decision has been revised to indicate that it is unclear how much, if any, of the usage reductions were attributable to the reclassification of large-use customers from the residential class to the non-residential class.

San Gabriel complained that the conclusion of law (No. 5) referring to shareholder risk relative to ratepayer risk had no predicate in the record. That complaint being meritorious, the conclusion was removed.

San Gabriel realleged in its comments that the denial of its memorandum account motion is discriminatory and unfair. Its arguments were fully considered in the proposed decision and this decision denies the motion as well, although we modify the discussion somewhat.

In its comments CFC repeated its arguments that there ought to be predicate cost-of-service studies for each customer class and that setting conservation rates for only one class of customers is unlawfully discriminatory. We find nothing in CFC's comments that warrant a change of position from the proposed decision.

7. Assignment of Proceeding

John A. Bohn is the assigned Commissioner and Gary Weatherford is the assigned ALJ in these proceedings.

Findings of Fact

1. To date the Commission has restricted increasing block water conservation rate designs to residential classes of consumers.

2. A pilot two-tier increasing block residential conservation rate design is superior to a three-tier design for the settings of the FWC division and the LAC division due to its comparative simplicity, ease of implementation and capacity to capture conservation.

3. The single quantity rate calculated to be the baseline for the limited, Monterey-style WRAM can be calculated effective July 1, 2010, based on the conservation rate design procedure adopted herein.

4. Over the years 2003-2008, the average monthly residential use was 25 ccf for the FWC division and 20 ccf for the LAC division. Median winter water use by residential customers in the FWC division is 16 ccf per month and in the LAC division is 13 ccf per month, and that use, weighted as it is mostly by indoor water use, is a proper measure for determining the breaking point between tier 1 and tier 2 in a two-tier increasing block conservation rate design, as outdoor water use is likely to be more responsive to higher price signals. Under this rate design, approximately 57% of the water sold to residential customers is expected to be billed at tier 1 rates and 43% at tier 2 rates for the FWC division, and approximately 55% of the water sold to residential customers is expected to be billed at tier 1 rates and 45% from tier 2 rates for the LAC division.

5. The service-charge-to–quantity-charge ratio of 46:54 in the LAC division can best be moved toward a 30:70 objective in a two-stepped manner through the adoption of a 35:65 ratio for the pilot conservation rate design.

6. A low-income (CARW) discount equivalent to 50% of the residential service charge under traditional rate design is more equitable than a straight percentage discount where service charges are being reduced.

7. For the 2004-2008 period, average annual water usage per customer was reduced in the residential class in the Los Angeles County division and the Fontana Water Company division, respectively, but it is unclear how much, if any, of those reductions were attributable to the reclassification of large-use customers from the residential class to the non-residential class. Two-tier increasing block rates for residential customers can be expected to reduce water use.

8. During the course of these proceedings San Gabriel modified its proposed conservation rate design from one with a unitary residential rate and surcharge to one with a two-tier increasing block rate structure. Later, at the request of the assigned ALJ, the company submitted an alternative three-tier proposal.

9. During the course of these proceedings, the DRA proposed a three-tier increasing rate design. Later, at the request of the assigned ALJ, the Division of Ratepayer Advocates submitted an alternative two-tier proposal.

10. CFC requested that the Commission delay implementation of conservation rates until cost studies are done.

11. During the course of these proceedings the revenue requirements changed for the San Gabriel's LAC and FWC divisions and may change further prior to the effective date of this decision and/or the next GRC. The revenue requirements for the LAC and FWC divisions may change further prior to the effective date of the increasing block rates contemplated in this decision and/or prior to the next GRC.

12. San Gabriel's non-residential rate design will not change under the pilot increasing block rate design.

13. The Commission has found that water revenue adjustment accounts relieve a company of additional variability in its revenues and that future proceedings would weigh that impact in determining risk and adopting a return on equity.

14. The Commission has found that balancing accounts for purchased water, purchased power, and pump taxes track variances in those costs and provide cost recovery.

15. The expense to San Gabriel of implementing conservation measures is not of a substantial amount in connection with a request for adoption of a Conservation memorandum account.

16. San Gabriel did not file its motion for a memorandum account to track legal and related costs of participating in the proceeding until 11 months after its initial application.

17. The expense to San Gabriel Valley Water Company of the legal and related costs to participate in this proceeding does not arise from an exceptional event, could have been reasonably foreseen at the last GRC for the Fontana Water Company division but not for the Los Angeles County division, is not of a substantial amount and adoption of a memorandum account to cover the expense would not be of benefit to ratepayers.

18. Dates for filing the next GRCs are July 2010 for the LAC division and July 2011 for the FWC division.

19. This proceeding was submitted on December 1, 2009.

Conclusions of Law

1. The pilot, two-tier conservation rate designs and Conservation Rate Design Procedure presented and adopted in this decision will advance the conservation objectives of the Commission's WAP. They will be reviewed after experience has been gained to determine their contribution to targeted reductions in consumption.

2. This rate design should apply only to direct-metered residential customers, excluding apartments, trailer parks, and any other facility in which residential customers receive service through a master meter.

3. The Monterey-style WRAMs and balancing accounts adopted in the decision implement the WAP's objective of decoupling sales and revenues to encourage successful conservation programs.

4. The single quantity rate to serve as the baseline for the limited, Monterey-style WRAM should be set effective July 1, 2010, based on the conservation rate design procedure adopted herein.

5. Equity considerations weigh against granting San Gabriel's motion for a memorandum account to track costs associated with its participation of this proceeding.

6. It is reasonable to deny San Gabriel's motion for authority to open a memorandum account relative to participation in this proceeding because this proceeding is not an exceptional event, could have been reasonably foreseen at the last GRC for the Fontana Water Company division but not for the Los Angeles County division, the amount of the expense is not substantial and there was not an adequate showing of ratepayer benefit.

7. It is reasonable to deny San Gabriel's request for authority to open conservation memorandum accounts because San Gabriel has not established that the amount of the expenses involved would be substantial.

8. It is reasonable to deny CFC's request that the Commission delay implementation of conservation rates until cost studies are done.

9. In order to promptly implement conservation rates, water revenue adjustment mechanisms, balancing accounts, customer education, outreach, data collection and reporting, this decision should be effective immediately and the conservation rate design and associated features should become effective July 1, 2010.

10. This proceeding should be closed, effective immediately.

O R D E R

IT IS ORDERED that:

1. San Gabriel Valley Water Company shall implement a pilot conservation rate design for the residential customer class in its two divisions. The rate design shall use the two-tier increasing block rate designs set forth below:

Topic	Adopted FWC	Adopted LAC
Service Charge		
Residential Meter Sizes	TBD	TBD
Low-Income Residential Meter Sizes	50% Discount	50% Discount
Quantity Charge		
Adopted		
Tiers #	2	2
Break ccf	0-16/≥17	0-13/≥14
Rates $	TBD/TBD	TBD/TBD
Differ %	15%	15%
Ratio		
BMP 1.4 Status (30/70)	27.97:72.03	35.40:64.60

The complete schedule of adopted service charge rates for all sizes of residential meters shall be determined based on adopted revenues for the 12 months beginning July 1, 2010. In implementing the pilot conservation rate design and any Commission-authorized change in revenue requirement on July 1, 2010, or thereafter, San Gabriel shall follow all of the steps in the "Conservation Rate Design Procedure" set out as Figure 1 in this decision and in the Attachment.

2. San Gabriel Valley Water Company shall file a tier 1 advice letter no later than 20 days prior to July 1, 2010 in order to implement the adopted conservation rate design procedure that is effective July 1, 2010. San Gabriel Valley Water Company shall apply this rate design only for the duration of the pilot, which is until the effective date of rates approved in the 2011 General Rate Case in the Fontana Water Company division and the effective date of rates approved in the 2013 General Rate Case in the Los Angeles County division, unless extended by further order of the Commission. This rate design shall apply only to direct-metered residential customers, excluding apartments, trailer parks, and any

other facility in which residential customers receive service through a master meter.

3. San Gabriel Valley Water Company shall apply in each division flat rate "California Alternative Rates for Water" (CARW) discounts equivalent to 50% of the residential service charges under traditional rate design. If the Commission authorizes a change to San Gabriel's revenue requirement, San Gabriel shall calculate the discount for CARW customers using the method used in this decision and described in the Conservation Rate Design Procedure set out in this decision and in the Attachment as Figure 1. In the next General Rate Case (GRC), San Gabriel shall propose a new method for determining CARW discounts that results in discounts comparable to that which qualifying customers received in the last GRC for that division, independent of the amount of the authorized service charge.

4. Monterey-styled water revenue adjustment mechanisms shall be applied in the two divisions.

(a) San Gabriel Valley Water Company shall file a Tier 1 advice letter updating the preliminary statement in its tariff to incorporate the Monterey-styled WRAM prior to its July 1, 2010 effective date.

(b) Commencing in 2011, San Gabriel Valley Water Company shall submit a written report to the Division of Water and Audits on the revenue over- or under-collected relative to sales of the same quantity of water at single quantity rates in each of the two ratemaking areas during the preceding calendar year by March 31 of the following year. That difference shall accrue interest at the 90-day commercial rate.

(c) The single quantity rate that shall be used as the baseline for the limited, Monterey-styled WRAM must be included in the advice letter filing, to be set effective July 1, 2010, based on the conservation rate design procedure adopted herein.

(d) If the water revenue adjustment mechanism over- or under-collection for either ratemaking division exceeds 2% of that area's total authorized revenue requirement for the preceding calendar year, a tier 1 advice letter shall be filed within 30 days by San Gabriel Valley Water Company that requests amortization of the balance in the account, which applies only to the residential class of customers. If the percentage is 2 or less, San Gabriel Valley Water Company shall propose amortizing in the next General Rate Case.

5. The existing full cost balancing accounts, which track all cost variances, shall continue to be applied in the Fontana Water Company division and existing incremental cost balancing accounts, which track variances in costs due to supplier price changes, shall continue to be applied in the Los Angeles County division.

6. San Gabriel Valley Water Company shall provide the following information in the General Rate Case filing in July 2011 for the Fontana Water Company division and July 2013 for the Los Angeles County division:

- Monthly per customer or service connection changes in consumption (compared to the same month in the previous year) by ratemaking division, separated by meter size and customer class, following the implementation of the conservation rate design pilot program;
- Surcredits and surcharges by ratemaking division and customer class implemented in amortizing water revenue adjustment accounts;
- Meter-reading errors, by division, that cause an unjustified crossing of tiers or retention within tiers;
- Number of low-income program participants disconnected for nonpayment by ratemaking division for two years before adoption of conservation rate design and for each year after that adoption;

- Number of residential disconnections for nonpayment by ratemaking division for two years before adoption of conservation rate design and for each year after that adoption;
- Incidences, if any, by ratemaking division of apparent unfair impact upon large, extended or multi-family households due to the two-tier rate design; and
- Any other ratemaking division-specific factor that might contribute to consumption changes and an estimation of its impact.

7. San Gabriel Valley Water Company shall include each general metered service customer's billing class (such as residential, commercial or public authority) on the monthly bill, as well as a telephone number for customers to call with questions or concerns about their customer classification. San Gabriel Valley Water Company shall include a website, with links to water conservation information, and a telephone number on customer bills for customers to call to obtain information about water conservation. In the interim, San Gabriel Valley Water Company shall include a link on the bill to one of its wholesalers: Metropolitan Water District's conservation website (www.bewaterwise.com), which contains water conservation information.

8. San Gabriel Valley Water Company shall track significant changes in the cost of purchased water and make a showing in its 2011 General Rate Case for the Fontana Water Company division and 2013 General Rate Case for the Los Angeles County division that it has exercised due diligence in ensuring the least-cost mix for its water sources and that any significant change in water purchases was reasonable.

9. San Gabriel Valley Water Company's request for authorization to establish conservation memorandum accounts is denied.

10. San Gabriel Valley Water Company's motion for authorization to establish memorandum accounts for participation in this proceeding is denied.

11. Any other motions or requests that may be pending in this proceeding, which relates to changes in rate design and ratesetting mechanisms, are denied.

12. With this decision, Application 08-09-008 is closed.

This order is effective today.

Dated April 8, 2010, at San Francisco, California.

MICHAEL R. PEEVEY
President
DIAN M. GRUENEICH
JOHN A. BOHN
TIMOTHY ALAN SIMON
NANCY E. RYAN
Commissioners

ATTACHMENT

Table A: Comparison Chart of Illustrative Examples and Proposed Residential Conservation Rates

Topic	Illustrative Examples(Based on dated 2009 Revenue Requirements, using adopted Conservation Rate Design Procedure; *see* Table 1)		San Gabriel		DRA	
	FWC	**LAC**	**FWC**	**LAC**	**FWC**	**LAC**
Service Charge						
5/8"x3/4" Current	$16.85	$20.04	$16.85	$20.04	$16.85	$20.04
Adopted/ Proposed	$15.67	$18.04	$16.69	$18.36	$12.25	$13.03
Low-Income						
Current	$8.425	$10.02	$8.425	$10.02	$8.425	$10.02
Proposed	$7.425	$8.02	$8.265	$8.34	$3.825	$3.01
Quantity Charge						
Current	$2.102	$1.5655				
Adopted			$1.9780	$1.8135		
RevSBR	$2.1731	$1.6972	1.9882	1.9378		
Adopted/ Proposed						
Tiers #	2	2	2	2	3	3
Break ccf	0-16/≥17	0-13/≥14	0-20/≥21	0-20/≥21	0-16/≥17-30/≥31	0-13/≥14-21/≥22
Rates $	$2.0079/$2.3500	$1.5889/$1.8300	1.9191/2.1110	1.8869/2.0753	1.6750/1.853/2.405	1.566/2.027/2.968
Differ %	15%	15%	10%	10%	12% 30%	29% 46%
Alternate						
Tiers #			3	3	2 Winter; Summer	2 Winter; Summer
Break ccf			0-15/≥16-30/≥31	0-15/≥16-30/≥31	0-16/≥17; 0-16/≥17	0-13/≥14; 0-13/≥14
Rates $			1.9344/1.982/2.128	1.9008/1.9378/2.0906	1.650/1.853; 1.650/2.223	1.763/2.027; 1.763/2.525
Differ %			3% 7%	2% 7%	12%; 35%	15%; 43%
Ratio BMP 1.4 Status (30/70)						
Current			37.5:62.5	45.7: 54.3		
Proposed	27.97:72.03	35.40:64.60	33.75:66.25	37.85:62.15	26.37:73.63	27.07:72.93

Table B
Illustrative Examples of Residential Service Charge Rates
(Based on dated 2009 Revenue Requirements)

	Fontana	**Los Angeles**
Meter Size	*Rate*	*Rate*
5/8 x 3/4 inch	$15.67	$18.04
3/4 inch	$15.67	$18.04
1 inch	$39.18	$45.09
1.5 inch	$78.35	$90.18
2 inch	$125.36	$144.29
3 inch	$235.06	$270.54
4 inch	$391.76	$450.90
6 inch	$783.53	$901.80
8 inch	$1,253.64	$1,442.88
10 inch	$1,802.11	$2,074.14
12 inch	$2,585.63	$2,975.94
Two 2-inch	$250.73	$288.58
Three 2-inch	$376.09	$432.86
Four 2-inch	$501.46	$577.15
Two 4-inch	$783.53	
Two 3-inch		$541.08
Three 3-inch		$811.62
Two 4-inch		$901.80
Three 4-inch		$1,352.70
One 8-inch, One 2-inch		$1,587.17

Figure 1: Conservation Rate Design Procedure

1. First, calculate division-wide rates by traditional rate design procedures (Standard Practice U-07-W, para. 11) to obtain uniform rates, using GRC-adopted customers and sales quantities and GRC-adopted revenue amounts (as adjusted by subsequently effective advice letters) for the time period during which the proposed rates will be charged.

2. Convert the resulting low-income discount (50% of the service charge according to the CARW customer's meter size) into the dollar amount to apply as the CARW discount.

3. Calculate the amount of any required BMP 1.4 revenue shift from the monthly Service Charges to the Quantity Rates, based on the Commission-adopted targets. [This decision sets these targets as at least 64.6% of the adopted revenue requirement collected from the quantity revenues for the LAC division and at least 72.03% of the adopted revenue requirement collected from the quantity revenues for the FWC division.]

4. Add the dollar amount of the required BMP 1.4 revenue shift determined under Step No. 3 to the adopted Residential Quantity Rate Revenue used in Step No. 1.

5. Calculate the Single (uniform) Quantity Rate to be used in the Water Revenue Adjustment Mechanism calculation for residential customers by dividing the dollar amount developed in Step No. 4 by the Adopted Annual Residential ccf Sales used in Step No. 1.

6. Segregate the Adopted Annual Residential ccf Sales between the two rate tiers using the adopted percentages. [This decision finds that 55% of the adopted ccf sales quantities will be in the 1-13 ccf/mo. first tier for the LAC division and that 57% of the adopted ccf sales quantities will be in the 0-16 ccf/mo. first tier for the FWC division.]

7. Using the adopted Tier 1/Tier 2 rate differential, develop Tier 1 and Tier 2 Quantity Rates for residential customers that are designed to produce the exact same revenues as those produced by the uniform quantity rate determined in Step No. 5. [This decision sets the Tier 1/Tier 2 rate differential at 15%]

8. Subtract the dollar amount of the required BMP 1.4 revenue shift determined under Step No. 3 from the adopted revenue requirement collected from the service charge for Residential customers.

9. Develop monthly service charges by meter sizes for residential customers by dividing the service charge revenue calculated in Step No. 8 by the adopted number of residential services. (This monthly service charge will be calculated by taking the service charge derived from the Adopted Residential Revenue Requirement multiplied by one minus the required BMP 1.4 percentage revenue shift and multiplying this product by Commission-adopted meter ratios to develop service charge rates for each meter size.)