

Decision 10-11-034 November 19, 2010

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Updated and Corrected
Application of GREAT OAKS WATER CO.
(U162W) for an Order Authorizing an Increase
in Rates Charged for Water Service, increasing
the revenue requirement by \$1,846,100 or
14.94% in 2010, by \$254,425 or 1.79% in 2011,
and by \$165,822 or 1.14% in 2012.

Application 09-09-001
(Filed September 3, 2009)
(Updated and corrected
caption filed November 12,
2009)

(See Appendix E for List of Appearances.)

DECISION RESOLVING GENERAL RATE CASE

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DECISION RESOLVING GENERAL RATE CASE

1. Summary

This decision resolves the general rate case application of Great Oaks Water Company (Great Oaks) for the test year July 1, 2010 – June 30, 2011 and the following two escalation years. The increases in revenue requirement we adopt here are:

	Increase in Revenue Requirement¹	Percentage
Test Year 2010/2011	\$820,250	6.97%
Escalation Year 2011/2012	(\$73,520)	(0.58%)
Escalation Year 2012/2013	\$47,490	0.38%

In this decision, we adopt a conservation rate design for single family residential customers. For this pilot program, we have lessened the rate impact customers will experience at the highest tier of usage under the rate design proposed by the Commission's Division of Ratepayer Advocates. Together with this rate design, we adopt a revenue adjustment mechanism that will protect the utility from revenue shortfalls due to the conservation rate design.

We decline to adopt additional revenue protection measures requested by Great Oaks, finding that the utility is not under a mandatory production limitation and has not actively promoted conservation in its service territory.

¹ These increases are calculated from the Division of Ratepayer Advocates' revenue requirement at present rates, as shown in Appendix A and use Great Oaks' current authorized rate of return. The revenue requirement will be updated to reflect any changes adopted by the Commission in Great Oaks' pending cost of capital proceeding, Application (A.) 09-05-007.

After the record in this proceeding closed, the Commission learned that Great Oaks had been withholding monthly payments to Santa Clara Valley Water District (SCVWD) of ratepayer-provided pump tax funds since April 2009. Great Oaks states it took this action as a litigation strategy related to a lawsuit it has against the SCVWD over the legality of the pump tax. The pump tax charge represents approximately 38% of the average customer bill and is treated for ratemaking purposes as a direct pass-through expense; Great Oaks had withheld approximately \$5,000,000 as of March 2010. Based on a Verification Report prepared by our Division of Water and Audits and comments submitted by Great Oaks and the Division of Ratepayer Advocates, we find that good cause exists to open an Order Instituting Investigation to further review Great Oaks' actions and to possibly impose fines for Great Oaks' failure to properly disclose its actions to the Commission and its staff.

This proceeding is closed.

2. Background

The Commission regulates water service provided by Great Oaks Water Company (Great Oaks) pursuant to Article XII of the California Constitution, the Public Utilities Code, and the Commission's rules and regulations.

Great Oaks is an investor-owned Class A water utility serving approximately 20,000 customers in the San Jose area.² It is a family-owned business, started 50 years ago by the parents of the current chief executive officer, and supplies customers with water from company-owned wells located in the service territory. Under the Commission's Rate Case Plan for Class A

² A Class A water utility is a Commission-regulated water utility serving over 10,000 customers.

Water Utilities, as revised in Decision (D.) 07-05-062 (Rate Case Plan), Great Oaks was scheduled to file a general rate case (GRC) application on July 1, 2009, with rates effective on July 1, 2010.³ By letter dated May 4, 2009, Great Oaks received permission to delay its GRC filing until September 1, 2009.⁴ On October 7, 2009, the Commission's Division of Ratepayer Advocates (DRA) filed a timely protest to the application.

Great Oaks filed an updated and corrected Application on October 19, 2009. The primary change in the updated application is the reflection of an interim rate increase of 1.75%, subject to refund, granted by Advice Letter 196C-W, effective September 1, 2009. Great Oaks was granted this interim rate increase because the Rate Case Plan's effective date for new rates was more than three years since the effective date of Great Oaks' last rate case.⁵ By Administrative Law Judge (ALJ) Ruling dated November 12, 2009, the caption of the proceeding was changed to reflect the revised revenue requirement increases contained in the updated filing.

³ Great Oaks' last GRC was handled through the advice letter process as an experiment to determine whether and when the advice letter process may be a suitable alternative to the formal application process. By Resolution W-4594, issued on May 11, 2006, Great Oaks was authorized a general rate increase for test year 2006-2007 and appropriate inflationary increases for escalation years 2007-2008 and 2008-2009.

⁴ The Commission's Executive Director had earlier denied Great Oaks' request for a three-year waiver in filing its GRC application. Great Oaks then filed, and subsequently withdrew, an application requesting a one-year postponement.

⁵ Great Oaks first filed Advice Letter 196-W in July 2009, requesting an interim rate increase of 21.6%, effective July 22, 2009. This advice letter, protested by DRA, was not accepted by the Commission's Division of Water and Audits. Subsequent filings of Advice Letters 196A and 196B were also not accepted. Advice Letter 196C-W and its accompanying tariff sheets were accepted by Division of Water and Audits on September 8, with an effective date of September 1, 2009.

A prehearing conference (PHC) was held on October 21, 2009 to discuss coordinating testimony and procedural schedules between this proceeding and Great Oaks' pending cost of capital proceeding, Application (A.) 09-05-007. At the PHC, a discussion was held regarding the Commission's conservation objectives, as set forth in our Water Action Plan, and Great Oaks was then granted the opportunity to submit a conservation rate design proposal, together with new conservation programs, in supplemental testimony.⁶

Following the PHC, it came to the attention of the Commission that Great Oaks had not provide its customers written notice of its request to raise rates, as required by Rule 3.2(d) of our *Rules of Practice and Procedure*. Great Oaks then provided this notice, together with the dates, place, and times for upcoming public participation hearings (PPHs), to all customers between November 5 and December 17, 2009. Pursuant to the preliminary schedule set at the PHC and confirmed in the December 2, 2009 assigned Commissioner's Scoping Memo (Scoping Memo), DRA served its report on December 9 and Great Oaks served its rebuttal testimony on December 28, 2009. Evidentiary hearings were held in San Francisco on January 21, 22, and 29, 2010. Opening briefs were submitted on February 25, 2010 and reply briefs on March 11, 2010. On May 27, 2010, Great Oaks filed Advice Letter 198-W requesting extension of its interim rates until the effective date of the decision in this proceeding; this advice letter was made effective July 1, 2010.

⁶ The date set for Great Oaks' supplemental testimony was November 16, 2009. On November 12, 2009, Great Oaks notified the ALJ by electronic mail that it was working cooperatively with DRA on developing a proposal and, therefore, rather than submitting supplemental testimony it would evaluate and consider adoption of DRA's proposal in its rebuttal testimony.

On March 19, 2010, DRA filed a “Motion to Reopen the Record to Admit Great Oaks’ Nondisclosure of Lack of Payment of Groundwater Charges and Request that the Commission Issue an Order to Show Cause for Violation of Rule 1.1. and Possible Violation of Section 2114.” The assigned Commissioner granted in part this motion, and directed our Division of Water and Audits to perform a verification and submit a report. We discuss our findings in a later section of the decision.

On August 20, 2010, Great Oaks filed a “Motion to Reopen Record for Limited Purpose of Updating and Revising Water Sales Data and Addressing Conservation Water Revenue Adjustment Mechanisms.” In its motion, Great Oaks asserts that language in the Commission’s Resolution W-4838, issued August 12, 2010, changes the beginning of the test year period in this application from July 1, 2010 to September 1, 2009, and thereby requires the Commission to accept new sales forecasts into the record and to change the rate making for the transition period September 1, 2009 – June 30, 2010.⁷

On September 8, 2010, DRA filed its opposition to the motion, asserting that the resolution’s language does not allow Great Oaks to retroactively establish a Water Revenue Adjustment Mechanism (WRAM) memorandum

⁷ Great Oaks cites to the following language in Resolution W-4838 as the basis of its motion:

Rejection of AL 197-W does not prejudice Great Oaks because the issues underlying the need to establish the two memorandum accounts requested by Great Oaks are being reviewed as part of our consideration of A.09-09-001. Given that Great Oaks has interim rates in place effective September 2009, the ultimate resolution of the issues raised in AL 197-W can be dealt with in A.09-09-001 without concern for retroactive ratemaking. (Resolution W-4838, Findings and Conclusions 20, *mimeo.* at 8.)

account back to September 2009 and the Commission's Rate Case Plan requirements do not allow the additional sales forecasts to be entered into this record.

On September 13, 2010, Great Oaks responded to DRA's opposition by again asserting that in Resolution W-4838 the Commission for the first time changed the effective date of the GRC rates in this proceeding, thereby triggering its motion to reopen the record.

We find that the language in Resolution W-4838 cited by Great Oaks does not say what Great Oaks asserts. The language does not change the test period of this GRC or state that a sales forecast for the transition period September 1, 2009 – June 30, 2010 will be established in this proceeding (A.09-09-001). The underlying issues referenced in the resolution are that the Commission in A.09-09-001 is setting both a new sales forecast for Great Oaks and considering a WRAM adjustment , and is doing both for the test period July 1, 2010 to June 30, 2011. As stated in Resolution W-4838, once this is done in A.09-09-001, the interim rates authorized in AL 196C-W will then be trued-up to the final rates that are adopted in A.09-09-001. On this matter, the resolution is consistent with our scoping memo, which states:

When final rates are adopted in this proceeding, a surcharge or surcredit will be imposed to recover or refund the difference between the new adopted GRC rates and the rates collected since September 1, 2009 under the interim rate authorization of AL 196C-W.⁸

⁸ Scoping Memo at 6.

Therefore, we find that Great Oaks' August 20, 2010 motion should be denied as the relief requested would violate (1) the Rate Case Plan's adopted procedure for rate adjustments during the Rate Case Plan's transition period and for updates during the scheduled proceeding, (2) the interim relief authority granted Great Oaks in AL 196C-W, and (3) the scope of this application.⁹

On October 12, 2010, Great Oaks filed another motion to reopen the record, again for the limited purpose of admitting evidence relevant to water sales forecasts and conservation issues. In this motion, Great Oaks addressed the accuracy and credibility of the evidence related to test period for this proceeding by asserting that if the Commission admits into the record the actual sales data for the months of July through September 2010, it will support the accuracy of its proposed forecast for the GRC period.

Great Oaks argues that the Commission should deviate from its Rate Case Plan procedures to do this because of the "unusual circumstance" of the Commission's proposed decision being delayed that allows for consideration of three months of actual sales data in the GRC period at issue. Great Oaks also updates the record on the actions of Santa Clara Valley Water District (SCVWD), which has rescinded its call for mandatory conservation and now requests 10% voluntary conservation.¹⁰

⁹ See D.07-05-062, issued May 30, 2007, *mimeo.* at 10-11 and Appendix A, Sections II-B and IV-F.

¹⁰ SCVWD issued a call to all Santa Clara Valley residents for 15% mandatory conservation in March 2009 and extended it in December 2009. In July 2010 it reduced its mandatory mandate to 10% and in September 2010 replaced its mandatory mandate with a call for 10% voluntary conservation. As will be discussed later in this decision, Great Oaks has never been under a mandatory production limitation from SCVWD.

We find that Great Oaks' October 12, 2010 motion should be denied as the relief requested would violate the Rate Case Plan's procedure for updates during the scheduled proceeding and Great Oaks has not met the Commission's standards for an extraordinary circumstance that would warrant the Commission deviating from its established procedure.¹¹ The procedural schedule set in D.07-05-062 for Great Oaks was an application to be submitted on July 1, 2009, a fourteen-month processing time, and rates effective on July 1, 2010.

The delays in issuing this proposed decision have not been extraordinary and, most importantly, have been solely caused by Great Oaks' own actions in (1) requesting a three-month delay in submitting its application, and (2) failing to disclose to the Commission and DRA that it had withheld payment to SCVWD since April 2009 of pump taxes it had collected from its customers. Great Oaks has not shown good cause for the Commission at this late date to reopen the record in order to accept three months of actual sales data and to provide DRA with a reasonable amount of time to respond to the updated information. Therefore, we deny the motion.

3. Public Participation

Two public participation hearings (PPHs) were held in San Jose on January 12, 2010. At the hearings, most speakers stressed that in these hard

¹¹ In Appendix A at A-9 of D.07-05-062, the Commission provides that under extraordinary circumstances, a water utility may seek discretionary post-application modifications. We state that "any such request must, at a minimum, show that the addition sought: (1) causes material changes in revenue requirement; (2) is the result of unforeseeable events; (3) is not off-set by other cost changes; and (4) can be fairly evaluated with proposed schedule changes that have been agreed to by all parties."

economic times people were struggling and could not pay the rate increase being requested by Great Oaks.

At the PPH, the Commission received a petition signed by 202 residents of the Rancho Santa Teresa Mobile Estates (Rancho Santa Teresa).¹² Barbara Walters, manager of the mobile home park, spoke at length. Rancho Santa Teresa has 302 occupied spaces and most residents have low incomes with little or no ability to pay for increases in the next three years. The park directly meters and bills each mobile home, so the residents do not qualify for Great Oaks' low income assistance program. Mrs. Walters has done all she can to assist customers, including distributing notices from SCVWD requesting customers to reduce their water consumption by 10%. Terry Walters, husband of Barbara Walters, testified that the level of Great Oaks' requested rate increase was unconscionable. Many of the residents of Rancho Santa Teresa Mobile Estates were retired people on Social Security and he understood Social Security is not going to go up this year or next year.

The first speaker at the afternoon session of the PPH, William Schaefer, testified he was generally a satisfied customer but that given the difficult economic times, if this increase were approved he would have to find ways to

¹² The Petition states:

We oppose the proposed increase in our water rates. We want to stop **any** increase and request the water rates to remain at the current rate. We are not enjoying any increase in wages or employment benefits. We have complied with the mandatory water conservation. Many of us are on fixed or low incomes and can barely afford to keep up with our food and housing costs. Some of us are facing losing our homes because of the economic troubles of this area. We often go without medical care and other necessities, because of the housing expenses we already pay. It is unfair for you to make **any** increase at this critical time in our economy.

conserve water as he is a retired person with limited income. The next speaker, Nancy Zampiello, testified that she found Great Oaks' notice of its application confusing and that she was living on a fixed income and could not afford the rate increase being requested. She later stated that the utility's explanations led her to believe that if she conserved water she would just be charged more. Don Catudal testified that in this bad economy, now was not the time to ask for a large rate increase. Rather, the utility should be doing as other businesses were doing and making cutbacks in operational expenses. He had reviewed the minor miscellaneous projects being requested and spoken with the company and did not find justification for a large increase. He also questioned whether foreclosures in the area rather than conservation were responsible for the utility stating its sales had declined. Richard Couderc agreed with the comments of earlier speakers and urged the Commission to heed the concerns expressed. Shirley Starr expressed extreme concern with the level of rate increase being requested and testified she would be unable to afford it.

Tracy Hemmeter requested that Great Oaks provide customers with more information, including proposed projects and the amount of increase from capital projects, conservation, and employee costs. She testified that many people are facing threats to their jobs, so every penny counts. She did not understand the conservation rate design proposal and testified that Great Oaks had never sent mailers about conservation.

Regarding DRA's proposal for tiered conservation rates for single family residential customers, Stu Goodgold testified that he lived in a 13 house development in an unincorporated area of Almaden Valley where the homes were on 2 acre lots and used a high amount of water. Water bills in the summer

were sometimes \$350 a month. He was very concerned about the effects a tiered conservation rate design would have on him and his neighbors.¹³

In addition to speakers at the PPH, the Commission has received nine written letters from customers. All of these customers oppose Great Oaks' request for a rate increase, and most harshly criticize the utility for requesting such a large increase in these hard economic times.

4. Discussion of Application

In a GRC proceeding, the Commission undertakes a comprehensive review of Great Oaks every three years, as prescribed in our Rate Case Plan. Based on the results of operations we authorize here, and using the cost of capital we authorize in A.09-05-007, the Commission will adopt a revenue requirement for Great Oaks' fiscal test year July 1, 2010-June 30, 2011, as well as fiscal years 2011/2012 and 2012/2013.

We will also establish a specific rate design to collect the authorized revenue requirement and from this adopt final rates for all customer classes. We address the establishment, discontinuance, or continuation of balancing and memorandum accounts and provide for all other tracking, monitoring, and reporting deemed necessary in the GRC period. In addition, based on final rates adopted in this proceeding, a surcharge or surcredit will be imposed to recover or refund the difference between the new adopted GRC rates and the rates

¹³ Goodhold further testified that three years ago Great Oaks asked to buy their small community water system and told the community that rates would be marginally higher than what they were paying for their small community water system but they would have the reliability of a Class A water system and avoid maintenance and the problems they had had with occasional repairs.

collected since September 1, 2009 under the interim rate authorization of AL 196C-W.

As set forth in the Rate Case Plan , Great Oaks “bears the burden of proving that its proposed rate increase is justified and must include in the proposed application and supporting testimony, all information and analysis necessary to meet this burden.”¹⁴

As part of this GRC, the Commission also examines the utility’s water quality and makes specific findings and recommendations concerning the utility’s water quality compliance.¹⁵ As summarized in DRA’s Report, Great Oaks’ water system consists of fifteen active and 5 standby wells and 5 storage tanks. These wells are permitted by the California Department of Public Health (CDPH) and the water system is routinely inspected and water samples tested by CDPH. DRA reviewed the information provided by Great Oaks and also contacted CDPH. The record reflects that Great Oaks system was last inspected in July 2009 and that between 2006 and September 2009 Great Oaks has been in compliance with all the State primary drinking water standards and does not have any violations.¹⁶

Therefore, based on the information in our record, we find that Great Oaks’ water system and water quality are in compliance with the requirements of CDPH.

¹⁴ See D.07-05-062, issued May 24, 2007, *mimeo.* at Appendix A at A-6.

¹⁵ In *Hartwell Corp. v. Superior Court*, 27 Cal.4th 256 (2002), the California Supreme Court held that the Commission has constitutional and statutory responsibilities to ensure that water utilities provide water that protects the public health and safety. For the scope of our water quality review in a GRC, see D.07-03-062, *mimeo.* at 24-26.

¹⁶ Exhibit 16 at Chapter 12.

5. Results of Operations

5.1. Sales Forecast

The largest dollar issue in dispute between Great Oaks and DRA is the sales forecast. The basis of the difference between the parties is Great Oaks' proposal to reduce projected water sales and the resulting forecasted sales revenue for each customer class except agriculture by applying a "drought adjustment" to the 2010-11 test year and the 2011-12 and 2012-13 escalation years.

Both parties use the New Committee Method regression analysis specified in the Rate Case Plan to forecast the per customer usage for residential, multifamily, and business customers. Great Oaks then applies a 12% reduction to the resulting sales forecast for each year and customer class (its "drought adjustment") to reflect that the SCVWD asked customers within its district to reduce consumption through June of 2010 by 15%.¹⁷ DRA disagrees with Great Oaks, asserting that the regression analysis data used in the sales forecast already includes the results of conservation efforts made by Great Oaks' customers and the Rate Case Plan methodology does not permit inclusion of additional reductions unless the utility is under a government mandated production limitation in the forecasted GRC period.¹⁸ Further, DRA asserts that the only Class A water utility authorized by the Commission to make this sales adjustment is California-American Water Company's Monterey District, which is

¹⁷ A table of the customer usage forecast differences is found in Great Oaks' Opening Brief at 12.

¹⁸ DRA also responds effectively to counter Great Oaks' counsel's statement that the Governor's call for 20% conservation by 2020 should be viewed as a mandatory production limit for the upcoming GRC period. (See DRA's Opening Brief at 9.)

under an order by the State Water Resources Control Board to limit production from the Carmel River.¹⁹

Great Oaks' witness testifies that while SCVWD has no authority to order mandatory restrictions, the district has contracted with an advertising agency to conduct a conservation campaign and has budgeted for conservation programs. Should these programs be successful, the Great Oaks witness stated that this will likely affect the level of water use for Great Oaks' customers into the test year whether or not the water restrictions are still in place in that year. Great Oaks' witness makes this prediction based on the utility's experience after the 1991 drought when consumption per customer dropped 28% in approximately two years and then took five to six years to recover to a stable, but lower level.²⁰ Great Oaks' witness relies on the following two provisions in the Rate Case Plan to support the drought adjustment:

Should an unusual event occur, or be expected to occur, such as the implementation or removal of limitation on the number of customers, then an adjustment to the five-year average will be made...

And

Water sales for all classes of customers for utilities that are under government mandated production limitations will be determined based on that limitation and consideration of unaccounted for water and historical production reserves while under the imposed limitations....²¹

¹⁹ Exhibit 16 at 2-2.

²⁰ See Exhibit 1, Chapter 4 at 2 -4 and Figure 1 at 4.

²¹ The full text of these provisions is in D.07-05-062, Appendix A at A-23, footnotes 4 and 5.

We find that the first Rate Case Plan section relied on by Great Oaks for its drought adjustment relates to changes in the number of customers, not conservation mandates.²² Further, we find that Great Oaks does not qualify for the adjustment referenced in the second section because it is not under a government mandated production limitation. At the hearing, Great Oaks' witness testified that SCVWD's conservation requirement is not mandatory and also testified that this is the first proceeding involving a Class A water utility's proposed drought adjustment since 1991.²³

Finally, we find that while Great Oaks' witness relies on SCVWD's advertising of its conservation mandate for its claim that customers will significantly reduce water consumption in this GRC period, the record shows that Great Oaks has not been warning its customers of a drought or helping them prepare to significantly reduce their consumption. Great Oaks has not mailed customers conservation material and has only informed a customer of SCVWD's free conservation audit and other conservation programs if the customer calls and asks. Further, at the PPH in this proceeding and in its mailed water report, Great Oaks informed customers that it does not face any shortage of water, but rather has ample supply.²⁴ The public testimony at the PPHs also indicates that

²² The section begins with the following sentences: "Forecast customers using a five-year average of the change in the number of customers by customer class. Should an unusual event occur, or be expected to occur, such as the implementation or removal of limitation on the number of customers..."

²³ See Transcript Vol. 2 at 124 (TR 2:124).

²⁴ At the PPH, Guster stated that "I don't want to discourage conservation use, but reality is in this area where we have water service, that there's plenty of groundwater." (TR at 60.) And in its 2009 Water Quality Report mailed to customers, under the caption Drought Concerns it states: "In the last several months, we have all heard about

Footnote continued on next page

the primary reason for any decrease in sales Great Oaks may experience is due to economic conditions rather than SCVWD's conservation mandate.

Based on the record, we find that Great Oaks does not meet the criteria set forth in the Rate Case Plan for the Commission to adopt a sales forecast based on "government-mandated production limitations." DRA uses the Rate Case Plan methodology and supports its position. The record does not show an increase in number of residential, multifamily, or business customers, so consistent with the Rate Case Plan, DRA does not change the sales forecast for the escalation years.²⁵ Therefore, we will adopt DRA's sales forecast for residential, multifamily, and business customers.

We next address the differences between the two parties on the sales forecast for industrial, public authorities, schools, and private landscaping. For these categories of customers, the Rate Case Plan does not require the same regression analysis methodology used for residential, multifamily, and business, but instead states the forecasts should be based on "the best available data."²⁶ Great Oaks and DRA both agree that multiple regression analysis should be used for industrial and public authorities, and historical averages should be used for private landscaping. The parties differ on whether Great Oaks' "drought adjustment" should be applied. We find that Great Oaks has not met its burden

potential water shortages in California. This is a situation created primarily by environmental concerns related to the San Francisco Bay-Delta. In Santa Clara County, it is surface water in reservoirs that is in short supply. Customers of Great Oaks are fortunate to have water supplied from bountiful underground aquifers." (Ex. 13 and TR 2:139-149.)

²⁵ *Id.* at Appendix A, paragraphs 8 and 9 at A-20.

²⁶ *Id.* at Appendix A at A-23, footnote 5.

of proof to establish that the Commission should deviate from existing sales forecasting practice to adopt the drought adjustment and adopt a different sales forecast for the escalation years. Therefore, we adopt DRA's sales forecast for industrial, public authorities, and private landscaping.

For schools, Great Oaks uses regression analysis and DRA uses historical average. In assessing which methodology uses the best available data, DRA asserts that in using the historical water sales for 2004 through 2008 to derive the average water sales for schools it has used the most recent sales data, which includes any recent conservation efforts made by the schools. DRA also questions whether Great Oaks' use of 10 year regression analysis, which is not required under the Rate Case Plan for schools, is appropriate because rainfall and temperature (two of the three variables necessary for regression) may not necessarily affect the operations of this class.²⁷

Great Oaks supports its use of regression analysis by incorrectly claiming it is required under the Rate Case Plan for this customer class. Its evidence regarding how well regression analysis explains the water usage for this customer class has unexplained contradictions.²⁸

We find DRA's data meets our standard of "best available data" and its methodology is consistent with our findings for all other customer classes on the issues of a drought adjustment and the escalation years. Therefore, we adopt DRA's sales forecast for the schools.

²⁷ See DRA's Opening Brief at 10-11.

²⁸ See Exhibit 1, Section E, Chapter 4 at 9 and TR 2:113.

Great Oaks and DRA are in agreement on the sales forecast for Agricultural customers and we adopt it. For Private Fire Protection Services, Great Oaks and DRA agree on the test year forecast but differ on whether the sales forecast should be increased for the escalation years. Consistent with our findings for the other customer classes, we adopt DRA's use of the same sales level for all three years.

5.2. Other Revenue Issues

Great Oaks proposes to increase the reconnection charge during regular business hours from \$10.00 to \$25.00, and from \$15.00 to \$40.00 for reconnection of service at other than regular working hours. DRA testifies that it has reviewed Great Oaks' costs for reconnection of services as well as the current charges imposed for the same service provided by other Class A water utilities and agrees with the proposed increase.²⁹ In response to a question about the effect these increased charges might have on low-income customers, Great Oaks provided data in Exhibit 9 showing that in 2007 four low income customers were disconnected, in 2008 eight low income customers were disconnected, and in 2009 fifteen low income customers were disconnected. The level of disconnections and the rise in disconnections do not raise a serious concern as Great Oaks had 76 low income customers in 2007 and had 220 low income customers in 2009.³⁰ Therefore, we adopt Great Oaks proposed increase in disconnection charges.

²⁹ Exhibit 16 at 2-10 and 2-11.

³⁰ For the coming GRC period, DRA testifies it will be monitoring any increase or decrease in disconnections for low-income customers as part of its conservation rate design review. TR 4:360.

In its application, Great Oaks initially proposed a credit card convenience fee of \$5.00 per transaction for credit or debit card payments from customers. DRA recommended Great Oaks explore the methods of processing credit or debit card payments that are used by other Class A water utilities to determine if there is a more efficient and least costly method for doing this. In response, Great Oaks withdrew its request from this proceeding.

Great Oaks' projection of unaccounted for water at 4.04% of water sales using a five-year average is supported by DRA. Therefore, we adopt it here.³¹

5.3. Non-Labor Operations and Maintenance Expenses

The major differences between Great Oaks and DRA in non-labor operations and maintenance (O&M) expenses are in purchased power expenses and groundwater charges. These two expenses are directly tied to our adopted sales forecast. Since we are adopting DRA's water sales forecasts for all customer classes, we also adopt its level of purchased power and groundwater charges.³² Our adopted expenses for these two categories for each year are \$5,924,160 for groundwater charges and \$683,200 for purchased power.

³¹ Exhibit 16 at 2-12.

³² We note that Great Oaks asserts that DRA made a rounding error in its calculations. However, DRA demonstrates that it correctly calculated these expenses. See Great Oaks Opening Brief at 45-47 and DRA Reply Brief at 14-16.

For all other non-labor O&M expenses, both parties agree on the following expenses for the GRC period:

Expense	2010-2011	2011-2012	2012-2013
Maintenance of Pumping Equipment, Wells, Account 711	\$16,503	\$16,936	\$17,154
Chemicals and Filtering, Account 744	\$54	\$55	\$56
Meter Expense, Account 754	\$1,435	\$1,472	\$1,491
T&D Maintenance and Supervision, Accounts 753 and 758	\$773	\$793	\$803
Maintenance of Reservoirs and Tanks, Account 760	\$0	\$0	\$0
Maintenance of T&D Mains, Account 761	\$33,805	\$34,690	\$35,138
Maintenance of Services, Account 763	\$33,313	\$34,186	\$34,628
Maintenance of Meters, Accounts 764	\$7,309	\$7,500	\$7,597
Maintenance of Hydrants, Account 765	\$16,020	\$16,439	\$16,652
Maintenance of General Plant, Account 805	\$32,519	\$33,370	\$33,802

5.4. Labor Expenses

Great Oaks has seventeen employees: four management, five general office employees and eight field staff.³³ It is requesting an additional field employee for this GRC period, a field technician whom Great Oaks initially stated would staff a new bacteriological testing lab. After Great Oaks withdrew its lab request, it asserted that the new employee would be used to coordinate Great Oaks' conservation efforts.

For test year 2010/2011, Great Oaks requests management salaries of \$927,498, an 18.1 % increase over the last authorized 2006/2007 test year level of \$785,328, and a 26.1 % increase over actual calendar year 2007 salaries of

³³ Exhibit 8 at 15. We note that Great Oaks' workpapers, Exhibit 20 at A-7 show 19 employees: 4 management, 5 general office and 10 existing field staff.

\$735,553.³⁴ Great Oaks requests general office salaries of \$301,423 and field staff salaries of \$826,932 for test year 2010/2011, a 74.4% increase over the last authorized 2006/2007 test year level of \$647,021 and a 30.4% increase over actual calendar year 2007 salaries of \$865,094.³⁵

In its report, DRA recommends \$859,387 for test year 2010/2011 management salaries, \$266,380 for general office employee salaries and \$709,184 for field employees.³⁶ For management salaries, this recommendation represents a 9.4 % increase over last authorized 2006/2007 test year levels and a 16.8% increase over actual 2007. For non-management salaries, DRA's recommendations represent a 50.8% increase over last authorized 2006/2007 test year levels and a 12.8% increase over actual 2007 salaries.

At hearing, Great Oaks testified that its management employees spend considerable time litigating the utility's lawsuits, primarily against SCVWD, and managing property and tenant relations for an office building owned by Great Oaks LLC. To assist the Commission in determining the ratemaking treatment to apply in this situation, both parties were specifically requested to brief whether any ratemaking adjustments should be made for these activities.³⁷ In briefs, Great Oaks asserts that no ratemaking adjustments should be made for these

³⁴ See Resolution W-4594 and Exhibit 20 at A-7b.

³⁵ Great Oaks request includes two new non-management employees. See Exhibit 20 at 1-7b and Resolution W-4594.

³⁶ Exhibit 16 at 3-6.

³⁷ The briefing request to parties was: "In the last GRC decision, which was by resolution, there were adjustments made to management salaries for ratemaking purposes. For this GRC, should any adjustments be made and, if so, why and how; (and) specifically discuss in that management time spent in litigation and property management. " See TR. 4:399.

activities and DRA asserts that the management time spent on these activities should be tracked and disallowed.

5.4.1. Management Salaries

Great Oaks testifies that its management team is well qualified, performs a broad range of duties, works long hours, and should be fully compensated in customer rates at the requested salaries. It does not present a survey of comparable compensation and staffing levels at other utilities or explain differences in the proposed raises for individual employees. In support of the salary level for its current General Counsel, Great Oaks references that he is paid less than its former General Counsel.

DRA applies labor escalation factors based on its October 20, 2009 Compensation Per Hour Annual Rate of Change memorandum (October 2009 labor escalation memorandum) to adjust Great Oaks' 2009 base management salaries and then escalate the salaries for the 2010/2011 test year period.³⁸ DRA also compared Great Oaks' management salaries to two other Class A water utilities, Valencia Water Company and San Jose Water Company, and found that Great Oaks' requested management salaries were high for a water company of its size. DRA testifies that Great Oaks provided management salary increases in 2009 - 2010 of 5.6 - 12.5% for its employees and that, given the economic downturn since the fall of 2008, only labor escalation factors based on inflation estimates should be applied. The resulting differences between DRA and Great Oaks are:

³⁸ These memorandums are issued monthly by DRA's Energy Cost of Service Branch.

Recommended Management Salaries for Test Year 2010/2011

Great Oaks Title	Great Oaks	DRA
Chairman, CEO	\$351,630	\$332,505
Treasurer, CFO	158,583	138,964
General Counsel	228,359	209,250
Reg. Affairs/ Attorney	188,925	178,668

Based on the record, we find that Great Oaks does not adequately support the management salary increases it requests here.³⁹ DRA adjusts these salaries using its October 2009 labor escalation memorandum and also uses this memorandum to support its rate of change for 2010 and 2011. This memorandum is a regularly released study and Great Oaks used the April 2009 memorandum in preparing its filing. Great Oaks questions why the June 2009 memorandum was not used and DRA states it used the most current data.

We find both the use of DRA's memorandum and the choice of the most current of these memorandums to be reasonable. Supporting our finding is the current economic recession, which began in the fall of 2008, and our requirement in the Rate Case Plan that in preparing its escalation year Advice Letter requests, Great Oaks use "the most recent labor inflation factors as published by the

³⁹ See Exhibit 16 at 3-4. As reflected in DRA's report, Great Oaks workpapers show salary increases in 2009-2010 of 5.6% for the Chief Executive Officer, 8.5% for the lead counsel, 12.5% for the Chief Financial Officer, and 5.6% for a second in-house attorney. DRA states that Great Oaks increased field worker salaries an average of 3% in 2009.

DRA.”⁴⁰ Therefore, as the starting point for our salary analysis, we will use DRA’s base level of management salaries.⁴¹

We next address the number of management employees that Great Oaks requests be compensated through customer rates. As the utility stated at the PPH, its rate base has declined over the years and is projected to decline further and it does not expect a lot of development in its service territory.⁴² However, the record also reflects that it is only since the middle of 2005 that two full-time attorneys have been employed, and in 2006 the Commission found that only a portion of the new attorney’s salary should be paid by customers.⁴³ Since its 2006 GRC proceeding, Great Oaks has had a stable level of customers, no large construction projects, and continues to be privately owned, thereby requiring no Securities and Exchange filings or investment community relationships. The only additional management tasks since 2006 are the use of its General Counsel rather than outside attorneys as chief counsel/lead trial counsel in the SCVWD litigation and various property management duties related to an office building recently acquired by Great Oaks LLC.

The Commission in Resolution W-4534 (Res. W-4534), issued May 5, 2005, approved Great Oaks’ request to establish a memorandum account to track litigation expenses Great Oaks incurs in suing SCVWD over the pump tax it is charged. The terms of the memorandum account, attached to this decision as Appendix C, provide that (1) Great Oaks must record litigation expenses

⁴⁰ See D.07-05-062, Appendix A at A-19.

⁴¹ Exhibit 16 at 3-5.

⁴² January 12, 2010 PPH, Transcript at 35.

⁴³ See Exhibit 13 at A-7b, and Resolution W-4594 at 4.

incurred at the end of each month, up to a maximum of \$100,000, in accordance with the accounting procedure set forth in the Division of Water and Audits' Standard Practice U-27, (2) if Great Oaks loses the litigation, its ratepayers will pick up \$100,000 of litigation costs booked into the memorandum account, subject to a reasonableness review, and (3) if Great Oaks is successful, then \$100,000 in the memorandum account, plus a maximum of \$300,000 which may have accrued at the utility's risk, may be recovered from ratepayers, subject to a reasonableness review and an immediate flow-through of 100% of the net benefits to ratepayers.

In its briefs, Great Oaks asserts that the provisions of Resolution W-4534 do not apply to SCVWD litigation expenses at issue here because:

1. Great Oaks amended its SCVWD lawsuit authorized under Res. W-4534 to include an additional cause of action; and
2. Great Oaks is now using an in-house attorney rather than outside counsel in pursuing the SCVWD litigation.

We do not find the first argument persuasive. First, the Santa Clara County District Court's Phase One and Phase Two decisions in *Great Oaks Water Co. v. Santa Clara Valley Water District, Case No. 1-05-CV053142 (Amended)*⁴⁴ are rendered on the complaint filed November 22, 2005. By adding an additional cause of action, Great Oaks does not change the terms specified in Res. W-4534

⁴⁴ See Attachments B and C to DRA's March 19, 2010 Motion to Reopen the Record and Great Oaks April 12, 2010 Response, attachments (Exhibits 1 and 2) to the Declaration of Timothy S. Guster.

for the recovery of litigation expenses, the memorandum cap, or the full flow-through of net benefits received.⁴⁵

Great Oaks' second claim, that it should receive reimbursement because it is now using an in-house attorney rather than outside counsel in pursuing the SCVWD litigation deserves our consideration. In its brief, Great Oaks asserts that using its in-house attorney costs far less than outside counsel for this work and that the resources it spends are likely to lead to significant customer benefits in the form of lower water rates in the future.

Resolution W-4534 addresses all SCVWD litigation expenses, but it does not specifically mention in-house attorney fees. DRA recognizes this when it recommends that the Commission modify the terms of the memorandum account and require Great Oaks to track and record all employee time spend on the litigation in the coming GRC period. Another avenue of recovery for Great Oaks is to include these costs in its motion to the court for claimed attorney fees and other costs.

We find that Great Oaks should be allowed to use its existing employees to pursue the SCVWD litigation over the coming GRC period. We make this determination because Great Oaks' General Counsel, in consultation with its CEO, has been successful at the trial court level in the litigation and because all net benefits will be immediately passed through to its customers if Great Oaks is ultimately successful.⁴⁶ We recognize that normal utility operations do not

⁴⁵ We discuss this case further in a later section of this decision when we address Great Oaks' request for outside legal fees.

⁴⁶ Great Oaks should not include any employee costs in its court motion to recover costs.

support two full-time attorney positions, and we will closely review this issue in the next GRC proceeding. We expect Great Oaks to include these costs in its motion to the court for claimed attorney fees and other costs.

A management task that does require a ratemaking adjustment is the time spent on property management. Since the last GRC, Great Oaks' subsidiary, Great Oaks LLC, purchased an office building. The utility rents approximately 1/6 of the building for utility operations. Great Oaks' CEO and its regulatory attorney handle all the tenant relations, including negotiating leases and working with the owner of an adjacent property that shares the parking lot used by tenants. The record does not indicate any rental income or other monetary consideration is received by the utility for these services. Therefore, a ratemaking adjustment to the salaries of the CEO and regulatory attorney should be made, as well as the Chief Financial Officer who handles the accounting for the property and is also keeping records and preparing taxes for Great Oaks LLC.

DRA recommends that the Commission require Great Oaks to submit a late filed exhibit documenting employee time spent on property management and then make a ratemaking adjustment for the test year based on this exhibit. Another method the Commission has used in previous cases is to estimate the proportion of each employee's time that will be spent on non-utility business and from this estimate, adjust the proportion of each employee's salary that is included in rates. At hearing, the CEO testified that he spent 30% of his time on SCVWD litigation and property management, and that he spent more time on property management than other employees. While the regulatory attorney spent less time than the CEO initially, it is the regulatory attorney who has tenant relations as part of his job description.

Therefore, using the base salaries discussed earlier, we find the following to be reasonable adjustments for property management tasks:

Therefore, we adopt:

Title	Test Year Base Salary⁴⁷	Adjustment	Authorized
Chairman, CEO	\$332,505	10%	\$299,255
Treasurer/CFO	138,964	5%	132,016
General Counsel	209,250	no adjustment	209,250
Reg. Affairs/ Attny	178,668	10%	160,801
Total	\$859,387		\$801,322

5.4.2. Non-management Salaries

Great Oaks supports its requested salary increases for general office employees by stating that its employees perform multiple functions at a very high level of competence and that its general office payroll per 1000 customers is the lowest for Class A water companies in its region. Great Oaks also references the average salary for a customer service employee manager in Santa Clara county to show that the salary of Great Oaks' office supervisor, whose job duties include customer service, is below this average.⁴⁸

For field employees, Great Oaks relies on its table of salaries included in its application and its assertion that DRA's use of the Commission's October 20, 2009 labor escalation memorandum is inappropriate because the data is highly

⁴⁷ *Id.* at 3-6.

⁴⁸ See Exhibit 8 at 15.

variable month to month and DRA's witness was not able to explain the specific calculations for underlying data referenced in the memorandum.⁴⁹ In support of its request for a new Field Technician, Great Oaks' rebuttal testimony justifies the employee as a dual-purpose lab technician/field representative. Great Oaks later asserted the position would be used for any conservation coordination that may be needed in the upcoming GRC period, combined with regular field technician responsibilities.⁵⁰

DRA does not support Great Oaks' request for an additional field technician position because the bacterial lab request has been withdrawn, Great Oaks has provided no justification for additional personnel to perform field work, and the request for a new employee to coordinate conservation efforts is not necessary at this time.

On the issue of salary increases for existing employees, DRA testifies that field worker salaries increased an average of 3% in 2009, far in excess of the 0.4% labor escalation figure shown in the Commission's October 2009 labor escalation memorandum. Further, general office employees' annual salaries increased an average of 5% in 2009, ranging from 2.08% to 8.6%. Great Oaks states that it hired a more qualified customer service representative when a prior employee moved out of the area, but otherwise does not address the increases. Using the Commission's October 2009 labor escalation memorandum, DRA recommends that 2009 base salaries be adjusted by 0.4% and the test year 2010- 2011 salaries be escalated 2.3%.

⁴⁹ See Opening Brief at 41-42.

⁵⁰ See Exhibit 8 at 19-20 and Opening Brief at 32 -34.

The resulting differences between DRA and Great Oaks are:

Recommended General Office and Field Salaries for Test Year 2010/2011

	Great Oaks	DRA
General Office Staff	\$301,423	\$266,380
Existing Field Staff	759,509	709,184
New Field Technician	67,423	none

Based on the record, we find that Great Oaks has not justified its level of salary increases for general office and field employees. While the average customer service employee manager for Santa Clara companies may well be higher than Great Oaks, we do not have a record of the annual revenues and types of businesses for these companies, nor do we have job descriptions of the specific customer service work performed by these managers. In addition, the record shows that Great Oaks has added one and a half new customer service employees since 2007 even though it has not had an increase in the number of customers served.⁵¹

We find that DRA's recommendations for salary increases are reasonable and should be adopted. Great Oaks challenges DRA's reliance on its October 2009 labor escalation memorandum but use of these memorandums, published monthly, is routine in Commission proceedings and DRA used the most recent memorandum in preparing its testimony. In adopting DRA's recommendations we also use the same labor escalation for all employees, including management.

⁵¹ See Exhibit 13 at A-7a.

In considering Great Oaks' request for an additional field technician, we do not find that the utility has met its burden of proof. In its application and rebuttal testimony, Great Oaks justified this position on the grounds that the new employee would provide the necessary expertise to operate the in-house bacteriological laboratory it intended to construct. After Great Oaks withdrew its request for the new lab, it asserted that this employee will do field technician work and perform any additional conservation activities the Commission directs Great Oaks to do in the GRC period. As will be discussed in a later section, the Commission is not requiring Great Oaks to undertake new conservation programs, only to better inform its customers of SCVWD's existing programs. Further, we find that Great Oaks has not provided any justification for an additional field technician. Therefore, we deny Great Oaks' request for a new employee position.

5.5. Administrative and General Expenses

The largest issue in dispute in this category is Outside Services Employed, Account 798. Parties also differ on the level of rate case expenses and uncollectibles. We discuss all disputed issues later in this section, after we discuss Miscellaneous General Expenses, Account 799, and Rents, Account 811.

While DRA does not take issue with any of Great Oaks' proposed expenses in Miscellaneous General Expenses, Account 799, we find that certain types of expenses included by Great Oaks should be disallowed. It is established Commission policy that dues, donations, charitable contributions, and political contributions are not permitted to be recovered from ratepayers.

In support of these expenses, Great Oaks testifies that its charitable and political contributions are beneficial to its customers.⁵² However, this is not the standard the Commission applies for these expenses. In its April, 1965 decision in *Pacific Telephone and Telegraph Company v. Public Utilities Commission of the State of California* (62 C.2d 634; 44 Cal.Rptr. 1, 401 P.2d 353), the California Supreme Court upheld the Commission's finding that:

The Commission in its decision observes that dues, donations and contributions, if included as an expense for rate-making purposes, become an involuntary levy on ratepayers, who, because of the monopolistic nature of utility service, are unable to obtain service from another source and thereby avoid such a levy. Ratepayers should be encouraged to contribute directly to worthy causes and not involuntarily through an allowance in utility rates. [Pacific] should not be permitted to be generous with ratepayers' money but may use its own funds in any lawful manner.

The Commission further points out that, conceding worthiness of the donees and benefits in good will reaped by Pacific, many ratepayers may not approve various of the donations made and they should be permitted to exercise their own free choice in such matters. Assuming that as argued by Pacific many of the objects of its bounty might otherwise require or receive support from taxpayers and that it is thus helping to keep taxes from rising, nevertheless Pacific is not authorized to exact from its customers payments in lieu of taxes.⁵³

⁵² See TR 3:202-208.

⁵³ 62 C.2d 634, 668- 669.

Therefore, based on our long-standing policy, as affirmed by the California Supreme Court, we disallow Great Oaks' charitable and political contributions and the expenses included under the category of "dues and subscriptions."⁵⁴

We next address Account 811, Rents. In the last GRC, Great Oaks was authorized \$98,805 and in this proceeding it requests \$174,005 for the test period, \$179,225 for 2011/2012, and \$181,673 for 2012/2013. DRA takes no issue with this level of rent.

In its report, DRA states that Great Oaks moved into a new office building in June, 2009, spent \$420,000 to renovate the space specific to its needs, and has a lease for 1/6 of the building. DRA does not mention in its report that the office building is wholly owned as a non-utility asset by Great Oaks' subsidiary. While DRA in another section of its report compares the usable space and renovation costs to a recent study performed by San Jose Water Company, it does not analyze the underlying lease agreement or report that the dealings on the rent and renovations were not arms-length transactions.

At the evidentiary hearing, the underlying lease agreement was admitted into evidence and questions were asked by the ALJ of DRA and Great Oaks. Based on the testimony, we conclude that a more comprehensive showing is required in the next GRC.

We do not have sufficient evidence to determine if we should disallow a portion of the rent or the capitalized renovation costs. Therefore, we will

⁵⁴ We also note that the expenses in each of these categories have risen substantially since the last GRC. The Commission adopted \$34,273 for all Miscellaneous General Expenses shown in Account 799 for the test period 2006 - 2007. In Exhibit 20 at A-12, Great Oaks shows \$52,781 in 2006 recorded expenses for Account 799 and it requests \$69,866 for test year 2010 - 2011.

approve the requested level of rent expense in this proceeding and direct that in its next GRC application, Great Oaks must provide a comprehensive showing to support the rental expense it requests and to establish that it has fully complied with all Commission accounting and reporting requirements in transactions with its subsidiary.

Based on the above discussion, we adopt the following A&G expense levels:

Expense	2010-2011	2011-2012	2012-2013
Customer Records & Collection, Account 773	\$132,392	\$135,859	\$137,615
Office Supplies & Other Expenses, Account 792	\$45,104	\$46,286	\$46,884
Property Insurance, Account 793	\$76,183	\$78,178	\$79,189
Injuries & Damages, Account 794	\$49,179	\$50,467	\$51,119
Employee Pensions & Benefits, Account 795	\$415,077	\$431,550	\$464,802
Franchise Requirements, Account 796	\$248,485	\$246,855	\$246,105
Miscellaneous Expenses, Account 799	\$50,804	\$52,134	\$52,808
Rents, Account 811	\$174,005	\$179,225	\$181,873
Transportation Expenses, Account 903	\$76,175	\$78,170	\$79,181

5.5.1. Rate Case Expenses

Great Oaks requests \$75,000 per year for rate case expenses for the next three years, based on the fact it now is required to undergo two major Commission proceedings for ratemaking purposes, a GRC and a separate cost of capital proceeding.

DRA recommends the Commission authorize \$26,900 annually, for a total of \$80,700 over the coming three years. This amount is based on a five year average from Great Oaks' recorded years 2004-2008 and reflects that the utility

has an in-house regulatory attorney, a general counsel, and a chief financial officer who is a certified public accountant.⁵⁵

We agree with DRA that \$80,700 is a reasonable estimate for Great Oaks' costs related to its GRC and cost of capital proceeding, and therefore will adopt it.

5.5.2. Uncollectibles

Great Oaks and DRA are quite close on their recommendations for this expense. Great Oaks requests \$43,148 for the test year, \$44,278 for 2011/12 and \$44,279 for 2012/13 and justifies these levels by the substantial increase in this expense in 2008, from \$19,478 in 2007 to \$39,928 in 2008. Great Oaks asserts that "with no end to the economic difficulties in sight," it is projecting a 2.62% increase each year, the average increase of its operating expenses over the five-year period from 2004 through 2008.⁵⁶

In its report, DRA recommends that the Commission adopt \$40,000 per year for uncollectibles. This represents a rate of 0.34% as a percentage of water service revenues and DRA testifies that San Jose Water Company, serving the same geographic area, has a lower percentage of water service revenues for its uncollectibles, its forecast for 2010 was lower than its actual 2008 uncollectibles, and it escalates future years at a lower rate.

We find that DRA presents a better documented proposal and, therefore, adopt its recommendation.

⁵⁵ We authorize for ratemaking purposes 2 attorney positions, an increase from the last GRC.

⁵⁶ See Opening Brief at 48.

5.5.3. Outside Services

Outside Services, Account 798, is for recording the fees and expenses of professional consultants and other outside services used by the utility. Great Oaks requests \$396,588 for test year 2010/2011, \$379,884 for 2011/2012, and \$383,269 for 2012/2013. The largest dollar items in this account are for SCVWD litigation (\$100,000 each year), litigation against the City of San Jose (approximately \$75,000 each year), water testing (\$96,000 in test year, dropping to \$75,000 if an in-house biological testing lab is approved), and other legal expenses (\$37,000 each year).

In its report, DRA recommends not approving GRC recovery of the \$174,657 in litigation expenditures for the SCVWD and City of San Jose litigation. DRA testifies that based on the information it received from Great Oaks, the City of San Jose case has been dismissed and expenses for the SCVWD litigation should be recovered in a memorandum account pursuant to Resolution W-4534.

In rebuttal testimony, Great Oaks asserts that its SCVWD litigation is broader than that authorized for memorandum account treatment in Resolution W-4534, issued May 5, 2005 because the case at issue was amended to include an additional cause of action, violation of the California Constitution (Proposition 218). For its initial cause of action, SCVWD's violation of its Water District Act, Great Oaks asserts that under the terms of Resolution W-4534 it must wait for all litigation to be complete before booking any expenses and requesting recovery from the Commission and, therefore it is premature for it to make entries into this memorandum account.⁵⁷

⁵⁷ Exhibit 8 at 11-14.

In regards to its City of San Jose litigation, Great Oaks testifies that DRA misunderstood the nature of the case. It is not related to contamination issues but rather to decades-old service area disputes and the city and Great Oaks have agreed to set aside the litigation while they try to resolve their differences through settlement discussions. Great Oaks states that the current case has been dismissed but if litigation were to resume, the legal expenses estimated for the test period would be significantly higher.⁵⁸

At the conclusion of evidentiary hearings, the parties were asked to brief the following: What is the position of each party on (1) the status and the eligible balances of litigation memorandum accounts that have been previously authorized and (2) should the Commission authorize use of any further or new memorandum accounts for litigation and, if so, under what terms and conditions.⁵⁹

In response to this request, Great Oaks asserts that its litigation expenses should be recovered in current rates because it is incurring these expenses in order to benefit its customers. It further states that the current SCVWD litigation is not covered by Resolution W-4534 and, since Great Oaks needs to file a similar lawsuit for each new year unless SCVWD changes its behavior, the Commission should authorize this litigation as a routine expense under Account 798. For its City of San Jose legal expenses, Great Oaks again states that ratepayers will benefit if it prevails, and cites to its hearing testimony to support this assertion.⁶⁰

⁵⁸ *Id.* at 10-11.

⁵⁹ TR 4:399-400.

⁶⁰ Great Oaks cites to Guster's testimony on January 22, 2010. In this testimony, he states that its litigation with the City of San Jose over its service area has been going on

Footnote continued on next page

Great Oaks does not support the Commission establishing new memorandum accounts in this proceeding for any existing litigation.

DRA asserts that in accordance with D.02-08-058, Great Oaks is required to track its future litigation expenses in a memorandum account rather than requesting expense recovery in a GRC proceeding. For its SCVWD litigation, DRA asserts that Great Oaks has a memorandum account but since it has failed to properly record its litigation expenses in this account, there is no eligible balance. Finally, DRA states that all of Great Oaks' lawsuits against SCVWD are essentially the same, and therefore all SCVWD litigation expenses should be tracked in the same account.

For the City of San Jose litigation, DRA does not recommend a memorandum account be established because Great Oaks has failed to meet the four conditions for memorandum accounts set by the Commission in D.02-08-054. These conditions, also reflected in Standard Practice U-27-W, are:

- a) The expense is caused by an event of an exceptional nature that is not under the utility's control;
- b) The expense cannot have been reasonably foreseen in the utility's last General Rate Case and will occur before the utility's next scheduled rate case;
- c) The expense is of a substantial nature in the amount of money involved; and

for some time. Currently, the case has been dismissed subject to an agreement to refile if a settlement cannot be reached. Great Oaks anticipates having discussions with the city later this year, but nothing has been scheduled. If a settlement is reached, Great Oaks anticipates it will require Commission approval. (See TR 3:294-296.)

- d) The ratepayers will benefit by the memorandum account treatment.⁶¹

Discussion

We affirm here our earlier finding in Section 4.1 of this decision that Great Oaks' SCVWD litigation expenses are addressed in full in Resolution W-4534, attached to this decision as Appendix C.

First, the Santa Clara County District Court's Phase One and Phase Two decisions in *Great Oaks Water Co. v. Santa Clara Valley Water District, Case No. 1-05-CV053142 (Amended)*⁶² are rendered on the complaint filed November 22, 2005. By amending Case No. 1-05-CV053142, to add an additional cause of action, the California Constitutional argument based on Proposition 218, Great Oaks does not change the terms specified in Res. W-4534 for the recovery of litigation expenses, the memorandum cap, or the full flow-through of net benefits received.

Second, Great Oaks' SCVWD lawsuits in subsequent years should also be included under the terms and conditions of Resolution W-4534. As noted in Attachment 1 to the Declaration of Timothy S. Guster, submitted on April 12, 2010 in response to DRA's March 19, 2010 Motion (Guster Declaration), the Santa Clara Superior Court (Court) in Phase 1 of Case No. 1-05-CV053142 (Lead Case), ruled in favor of Plaintiff Great Oaks, finding that SCVWD violated Article XII of the California Constitution as well as the Santa Clara Valley Water District Act.

⁶¹ D.02-08-054, issued August 22, 2002, *mimeo.* at 3.

⁶² See Attachments B and C to DRA's March 19, 2010 Motion to Reopen the Record and Great Oaks' April 12, 2010 Response, attachments (Exhibits 1 and 2) to the Declaration of Timothy S. Guster.

The Court considered all relevant factors, including the overcharges, in arriving at a value for damages due to SCVWD's violation of the District Act.⁶³

As noted in Attachment 2 to the Guster Declaration, Great Oaks and SCVWD stipulated and agreed to a continuance of Case No. 108CV119465, to a date determined by the Court which is after March 8, 2011, or until the date final judgment is rendered in the Lead Case, whichever is earlier. The Stipulation and Order Granting Continuance and Staying Case, issued January 21, 2010 by Hon. Kevin J. Murphy, Judge of the Superior Court, in Case No. 108CV119465, references a series of related cases, Case No. 108CV123064 and Case No. 109CV146018, and states that: "Suffice it to say that there is substantial overlap between the issues in the Lead Case and the issues in the other cases, including this case." (Stipulation, at 1.) This Stipulation and Order further states that: "This stipulation shall only become effective if the Court grants the orders attached to each of the stipulations filed in the above referenced actions." (Stipulation at 2.) Each of the two other stipulations and orders staying cases, issued in Case No. 108CV123064 and Case No. 109CV146018, includes identical language noting the substantial overlap between the issues in the Lead Case and in the other referenced cases, and tying the effectiveness of the stipulation to the granting of the orders attached to each of the other stipulations regarding these clearly related cases.

We find that Great Oaks voluntarily entered into a series of stipulations regarding the Lead Case and several related cases, and since each stipulation and order explicitly acknowledges the overlapping issues in these cases, Great Oaks

⁶³ See Guster Declaration, Attachment 1 at 2.

is estopped by its own conduct from effectively arguing that these cases are unrelated.

Since the Lead Case and subsequent related cases all address substantially overlapping legal issues, and since this Commission has already adopted, at Great Oaks' own request, a memorandum account process, for recording for eventual potential recovery the costs of litigating the issues raised in these cases, there is no persuasive reason to characterize each separate but clearly related case as requiring a entirely unique litigation cost recovery process. Great Oaks has not requested this be done previous to this proceeding and does not request it here.

Third, Great Oaks' Resolution W-4534 tariff pages, specifically section F.4.a., clearly provide that any expense eligible for memorandum account treatment must be recorded on a monthly basis. We agree with DRA that Great Oaks' failure to comply with this requirement and properly track its SCVWD litigation expenses means that there is presently no eligible balance in this account.

Based on the above discussion, we disallow all SCVWD litigation expenses included in Outside Services Employed, Account 798 and find that Great Oaks must use the memorandum accounting procedures established in Resolution W-4534 for any SCVWD litigation expenses it seeks to recover from ratepayers.

We recognize that the SCVWD litigation expenses Great Oaks asserts it has accrued are much greater than it projected when requesting its memorandum account. However, Great Oaks has never requested the Commission modify the terms of Resolution W-4534 and does not do so here. Rather, Great Oaks appears to have decided it can unilaterally choose, without notifying the Commission or properly disclosing its actions in this application, to apply a different ratemaking

treatment.⁶⁴ We strongly disagree. We affirm that Resolution W-4534 remains in force and requires that if Great Oaks is ultimately successful in its SCVWD litigation, it must immediately file by Advice Letter to pass-through the net benefits to its ratepayers.⁶⁵

Finally, we decline to adopt DRA's recommendation to modify Resolution W-4534 to include recording management time spent on SCVWD litigation. Great Oaks strenuously objects to tracking its managers' time and we have made the appropriate ratemaking adjustments in a different manner.

We next address the City of San Jose litigation expenses forecasted for the coming GRC period. DRA states that Commission policy is to establish memorandum account treatment for future litigation expenses and Great Oaks disagrees.

The Commission has authorized the establishment of memorandum accounts when certain types of projected costs and/or ratepayer benefits are uncertain. Memorandum account treatment requires litigation expenses to be tracked on a going forward basis and when the litigation is concluded, allows the

⁶⁴ The Rate Case Plan requires Great Oaks to explain in its testimony under both basic information and Results of Operation Report all significant changes between last adopted figures and recorded amounts that the utility is requesting be included in rates and to provide a list of the major controversial issues included in its GRC filing. The amounts recorded for SCVWD legal expenses for 2007 and 2008 under Account 798, as shown at A-12 of Exhibit 20, meet the Rate Case Plan's definition of a significant expense and significant change. See D.07-05-062, Appendix A at A-21 to A-24.

⁶⁵ As discussed in Section 4.4.1., Great Oaks' tariff states that the utility has established the "Santa Clara Valley Water District Memorandum Account to track the costs related to litigation against the Water District." The tariff provides for this to be done through the memorandum account and also through any offset expenses of the litigation addressed by the Court in a final judgment, with the reasonableness of the expenses subject to review by the Commission when benefits are flowed-through to ratepayers.

utility to seek cost recovery in a GRC proceeding or by Advice Letter with a showing of reasonableness and ratepayer benefit. This is the procedure set forth in D.02-08-058 and its applicability goes beyond water quality litigation. In the Great Oaks' 2003 GRC decision, the Commission applied this broader standard when it stated:

Great Oaks requests recovery of forecasted expenses related to its litigation with the City of San Jose over water contamination issues. ORA [Office of Ratepayer Advocates] objects because Great Oaks has not justified this expenditure with any description, analysis, or need for the litigation, nor has it shown the probability of prevailing in such a lawsuit. Instead, ORA recommends these expenses should not be authorized but could be tracked in a memorandum account and recovered in the future when Great Oaks demonstrates it has incurred the legal fees and adequately justifies them. ORA's recommendation is consistent with the process we have used for future legal expenses. We have required companies to track legal fees in memorandum accounts in order to review the amounts incurred and the outcome of the litigation. (*Re San Gabriel Water Co.*, D.02-10-058, Cal PUC LEXIS 727 **22-23.) We will require Great Oaks to similarly record these amounts for any future recovery.⁶⁶

DRA also raises the concern that Great Oaks has not established the need for a City of San Jose service territory dispute litigation memorandum account based on the four criteria set forth in D.02-08-054. However, these criteria are generally used when water utilities are between GRC filings and the Commission, therefore, does not have an evidentiary record within which to review the request. The circumstances in D.02-08-054 were that California Water Service Company had filed its GRC application, A.01-09-071, but needed to begin recording contamination treatment costs for four wells immediately, and the

⁶⁶ See D.03-12-039, issued December 18, 2003, *mimeo.* at 11.

estimated costs were substantial. Lacking an evidentiary record, these four criteria were applied. In authorizing the memorandum account, the Commission stated “the ratepayers will benefit from creating this memorandum account because the account will only allow Cal Water to record these costs, and the costs will be subject to ratemaking review by the Commission.”⁶⁷

While we find the four factors cited by DRA to be useful in guiding our deliberation, the Commission has not applied a fixed set of factors in considering whether to establish memorandum accounts for water utilities. We have discussed above our findings in D.02-08-054, D.02-10-058 and D.03-12-039. We have also articulated factors to be considered in Resolution W-4276, and D.04-06-018, and Standard Practice U-27-W, paragraphs 25 and 44 contain similar lists of factors. When the Commission has applied these factors, we have 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.

In this proceeding, (1) there is considerable uncertainty regarding the level of projected litigation expenses, especially as the pending case has been dismissed and no settlement discussions have been scheduled, and (2) Great

⁶⁷ D.02-08-054, issued August 22, 2002, *mimeo.* at 3.

Oaks asserts that a settlement may provide ratepayer benefits but cannot detail them and affirms that a final resolution of the dispute will need to be brought before the Commission for its review and approval.

Therefore, we find that Great Oaks should be authorized to file by a Tier 2 Advice Letter to establish a memorandum account for outside legal expenses related to this litigation, with a cap of \$225,000 for expenses over the coming GRC period. As with its SCVWD memorandum account, Great Oaks must record in the memorandum account on a monthly basis any expenses that may be eligible for recovery and be subject to ratemaking review when it seeks recovery. Great Oaks should bear the burden when it requests recovery of the recorded costs, to show that separate recovery of the types of costs recorded in the account is appropriate, that it acted prudently when it incurred these costs, and that the level of costs is reasonable. Great Oaks may seek recovery of the costs in this memorandum account in its next GRC or through a Tier 3 Advice Letter filing.

5.6. Capital Additions, Rate Base and Depreciation

In their comparison exhibit filed after hearings, Exhibit 27, Great Oaks and DRA reflect agreement on special plant additions in the coming GRC period. An item not included is the Country View Tank. Both parties agree that Great Oaks may submit this project, when complete, by advice letter and there should be a cost cap of \$385,000. DRA further states that Great Oaks should recover the cost of construction of this tank from future customers through a service fee assessed

on future customers when they connect to Great Oaks water service.⁶⁸ The other special plant additions are reflected below:

Year	Description	Plant Addition
2009	Levin Tank Circulation Equipment	\$25,700
2009	Security System	\$160,000
2009	GIS System	\$175,000
2009	Billing and Database Software	\$120,000
2009	Office Furniture	\$11,408
2009	Small Tools	\$1,878
2009	Storage Shelving	\$2,536
2009	Well Rehab (22 & 24)	\$17,712
2009	Calero Booster Pump Rehab & Replacement	\$6,354
2009	New Office Improvement	\$420,000
2010	Well Generators: W2; 12; 23	\$195,000
2010	Country View Dr. Pressure Reducer	\$26,000
2010	Ashmont repipe/refurbish tank	\$20,000

Both parties also agree on developer/customer funded projects totaling \$2,444,001 for 2009/2010, as set forth in Exhibit 16 at 7-12. The costs of these projects are paid for by the developer or customers and tracked in the Contribution in Aid of Construction (CIAC) budget, which is amortized and deducted from rate base. The company collects an advance for the main extensions and new services and reimburses the contributors over a 40-year schedule set forth under Tariff Rule 15. DRA agrees that Great Oaks' proposal is in accordance with Rule 15 and we make that finding here.

Great Oaks and DRA came to fairly close agreement in the comparison exhibit on depreciation expense for the test year and net rate base. For the test

⁶⁸ See Exhibit 16 at 7-9 to 7-11. See Great Oaks' agreement at Opening Brief at 63.

year, we accept Great Oaks' recommendation and will authorize \$1,156,392 in depreciation expense and adopt a net rate base of \$11,069,738.

5.7. Taxes

There are substantive disagreements between Great Oaks and DRA on taxes, both income taxes and taxes other than income. These disagreements go beyond the tax differences arising from each party's recommendations on operating revenues, expenses, and plant. In general, we find that neither Great Oaks nor DRA presents a clear and comprehensive presentation on tax issues and we have had to look to the Commission's established tax policy, referenced legislation, and the relevant tax codes to fully understand and resolve the disputed issues.

5.7.1. Taxes Other Than Income

For taxes other than income, Great Oaks includes \$10,389 for Department of Motor Vehicles license fees. These fees are an expense item, not a tax. Great Oaks also includes an unexplained "Payroll Expense" item of \$533 in its opening brief. This is also not a tax.

In its application, Great Oaks uses a flat projection of 2% per year for payroll taxes, and in its brief asserts that its most current calculation at Exhibit 20, page A-12c is correct without further explanation.⁶⁹ DRA testifies that the current statutory rates for Federal Insurance Contributions Act (FICA), Federal Unemployment Tax Act (FUTA), and State Unemployment Insurance (SUI) should be applied, recognizing that there are two components for FICA taxes –

⁶⁹ Opening Brief at 59. Exhibit 20 at A-12c does not reflect current payroll tax rates, only the statement: "est. increase @ 6.66%."

FICA Social Security and FICA Medicare. We agree with DRA and apply the current state and federal payroll tax rates.⁷⁰

For property (Ad Valorem) taxes, both parties use the projected assessed value of Great Oaks' net utility plant in service (UPIS) for the test year and multiply it by the average Ad Valorem tax rate paid by Great Oaks. Great Oaks requests an amount of \$223,013 but does not show how it derives this figure. DRA states it uses a tax rate of 1.23% that is calculated using Great Oaks' actual tax payments over the UPIS for the 2008-2009 tax year.⁷¹ We find that DRA has provided better support for its recommendation, and therefore adopt its recommendation of \$177,500.

5.7.2. Income Taxes

A water utility is allowed to recover federal income tax (FIT) in rates. This tax is estimated at 34% of net income, based on current test year income and expenses, and the expenses reflect tax depreciation, California Corporate Franchise Tax (CCFT), and any reduction for a claimed Domestic Production Activities Deduction (DPAD). The parties disagree on interest and depreciation expense, CCFT and DPAD.

Great Oaks asserts in its rebuttal testimony that DRA does not include the proper deduction for the difference between Commission-allowed depreciation and federal and state depreciation and erroneously includes \$301,000 in interest

⁷⁰ For federal rates, see http://www.irs.gov/publications/p15/ar02.html#en_US_publink1000202541. For state rates, see http://www.edd.ca.gov/payroll_taxes/rates_and_withholding.htm.

⁷¹ See Exhibit 19, between A-7b and A-8.

expense.⁷² In its reply brief, DRA accepts Great Oaks' methodology in capturing the difference between Commission-allowed depreciation (booked depreciation) and federal and state depreciation. For both state and federal depreciation, Great Oaks uses 113.38% of the ratemaking depreciation. DRA states that adjusting the agreed booked depreciation of \$1,154,200 by this factor results in a tax depreciation of \$1,308,632. We accept this calculation.

For interest expense, DRA is correct that if the Commission imputes a debt component into Great Oaks' capital structure, it then allows an interest expense for ratemaking purposes. We should reflect in final rates here any interest imputed into Great Oaks' capital structure in our cost of capital decision in A.09-05-007.⁷³

For CCFT, the Commission in D.89-11-058, issued on November 22, 1989, requires that for ratemaking purposes the prior year's CCFT should be used in the calculation of the test year's FIT. Great Oaks uses this methodology. DRA does not. DRA testifies that Assembly Bill (AB) 1843, passed in 2000, amended the California Revenue and Taxation Code to provide that corporations are no longer required to make estimated CCFT payments to the state one year in advance and, therefore, there is no need to follow D.89-11-058 because the timing difference of the current year's CCFT payments as a deduction in the current year's FIT calculation is no longer an issue. Further, DRA testifies that Section 813 of the 2008 Guidebook to California Taxes, published by California Clearing House, reflects this change.

⁷² Exhibit 8 at 21.

⁷³ We use the interest expense in the last GRC here.

Based on the above, DRA asserts that the Commission should re-examine its methodology and find that use of the current year's CCFT as a deduction in the current year's FIT calculation better matches revenues and expenses for the same period. DRA uses this revised methodology in its rate calculations.

A reading of AB 1843 shows that the bill changed the terminology of the tax code so that "income year" and "taxable year" have the same meaning but did not change the actual amount of state tax required to be paid or the timing of the payments. This is confirmed in the bill's summary statement that AB 1843 has no fiscal or tax impact.⁷⁴

We do not find DRA has presented sufficient cause for the Commission to deviate in this proceeding from the CCFT methodology we adopted in D.89-11-058. The Commission adopted D.89-11-058 in a generic proceeding that examined the methods to be utilized by the Commission to establish the proper level of CCFT expense for all utilities, Investigation (I.) 86-11-019. Therefore, we will apply D.89-11-058's calculations in this proceeding.

Our last tax issue is DPAD. Section 199 of the Internal Revenue Code, enacted as part of the American Jobs Creation Act of 2004, allows a taxpayer a federal tax deduction for certain domestic production activities. This deduction is allowed when the taxpayer fulfills conditions specified in Section 199. A water utility is allowed this deduction if its domestic production activities include the acquisition, collection, and storage of raw water (untreated water), transportation of raw water to a water treatment facility, and treatment of raw water at such a facility.

⁷⁴ The text of the chaptered bill may be found at <http://www.leginfo.ca.gov>.

We agree with DRA that Great Oaks is engaged in these production activities and is allowed a DPAD, which reduces the FIT. In its rebuttal, Great Oaks testifies that it does not take issue with proper application of the DPAD, but does disagree with DRA's proposed application. However, Great Oaks does not propose a different application.⁷⁵

In its opening brief, Great Oaks states that the Domestic Production Gross Receipts used in calculating the Qualified Production Activities Income (QPAI) does not include gross receipts derived from the transmission or distribution of potable water, suggesting that because Great Oaks does not have receipts derived from these activities, it does not qualify for a DPAD deduction. DRA responds that as a practical matter, Great Oaks is a utility with 100% pumped water and generates revenue from the sale of its water only after ratepayers receive and use the water; therefore, it has properly calculated the revenues from its production activities in the QPAI. We agree. Great Oaks is not selling anything other than the potable water it produces.

We find DRA has properly calculated the DPAD under the provisions of Section 199 of the IRS Code and its related regulations (1.199), as explained in DRA's report.⁷⁶ Therefore, a DPAD deduction using DRA's methodology should be adopted.

5.8. Rate Design

In our December 15, 2005 Water Action Plan (Water Action Plan), the Commission set as one of its objectives the strengthening of water conservation

⁷⁵ Exhibit 8 at 21.

⁷⁶ Exhibit 16 at 6-6 through 6-6.

programs to a level comparable to those of energy utilities. In order to consider policies to achieve this objective, the Commission opened I.07-01-022 to examine increasing block rates, water revenue adjustment mechanisms (WRAMs), rebates and customer education, conservation memorandum accounts, and rationing programs for all Class A water utilities. Great Oaks is a respondent to I.07-01-022 but has never actively participated in any phase of the proceeding.

We agree with the assigned Commissioner's determination in the scoping memo to place a particular emphasis on establishing conservation programs and rate design that are consistent with (1) the Commission's conservation objectives set forth in our Water Action Plan and (2) the practices being implemented for other Class A utilities in I.07-01-022.

Great Oaks proposes to retain a uniform single rate for all customers rather than beginning to move toward conservation rate design. The Commission generally defines a conservation rate design as an increasing (inverted) block rate design with at least 70% of projected sales revenues collected in the commodity rather than fixed customer charge.⁷⁷ All of Great Oaks' customers are metered and billing is done on a bi-monthly basis.

Great Oaks did not sponsor a conservation rate design in this proceeding, either in its application or in the additional opportunity provided it to submit supplemental testimony. Instead, Great Oaks stated it would work cooperatively with DRA on its proposal, which was submitted on December 9, 2009. In its rebuttal, Great Oaks testified that it opposed DRA's inverted block rate design unless DRA agreed to use Great Oaks' drought adjustment sales

⁷⁷ The Commission has also considered conservation rate design proposals that were based on seasonal rates.

forecast as the starting point for the rate design.⁷⁸ In its opening brief, Great Oaks states that it will accept DRA's conservation rate design proposal only if the Commission adopts all of the following:

- (1) Great Oaks' water sales forecasts, including the so-called "drought adjustment";
- (2) tiered rate design consistent with DRA's trial program, with Great Oaks' requested revenue requirement (Ex 16, pp. 14-1 – 14-15);
- (3) a Monterey-style WRAM as proposed by DRA;
- (4) a true revenue decoupling WRAM account that tracks revenues and expenses lost or gained due to conservation programs; and
- (5) a memorandum account tracking administrative expenses incurred by Great Oaks in implementing new conservation programs.⁷⁹

In its report, DRA recommends a three-tier increasing block rate design for Great Oaks' single-family residential customers and uniform rate design for all other customers. Single-family residential customers represent 94% of Great Oaks' total customers and use approximately 60% of the total metered water consumed.⁸⁰

Because Great Oaks was unable to provide monthly billing data for all residential customers, citing the deficiencies of its current customer record and billing systems, and due to errors DRA found in the data supplied, it

⁷⁸ For illustrative purposes, DRA used Great Oaks' sales forecast and proposed revenue requirement to develop its increasing block rate design but stated that its rate design is independent of the water sales forecast and the Commission should update the rate design model with our adopted revenue requirement in the final decision. See Exhibit 16 at 14-4 to 14-5 and DRA's Opening Brief at 37.

⁷⁹ See Opening Brief at 68.

⁸⁰ Exhibit 16 at 14-2.

recommends that the proposed rate design, combined with a Monterey style WRAM, be a trial program and that Great Oaks develop a billing system that will easily track and maintain records of customer use and billing for each class of service.⁸¹ DRA provides a recommendation on specific information Great Oaks should track and report on annually in the advice letter that it files to true-up the balance in the WRAM.

Finally, DRA recommends that if its proposal is adopted, the Commission make the trial program effective within 90 days of a decision in this proceeding, and that the conservation rate design and WRAM be implemented on the same date.

5.8.1. Rate Design Proposals

Great Oaks is the only Class A water utility without a conservation rate design, and the scoping memo made consideration of this issue a priority since early in this proceeding. As the Commission determined in D.08-08-030, the second phase decision in I.07-01-022, “conservation rate designs will advance our Water Action Plan’s conservation objectives and will be reviewed to determine whether they meet targeted reductions in consumption.”⁸²

DRA sponsors the only conservation rate design. In evaluating this proposal, we are mindful of the data limitations DRA encountered, particularly in assessing the impact of its proposal on low-income households that might include numerous residents using large amounts of water per month, and on customers with high summer irrigation usage who may need time to fully

⁸¹ In this application Great Oaks requests, and DRA supports, authorization to purchase a new billing and customer record system. See Exhibit 16 at 14-12.

⁸² D.08-08-030, issued August 25, 2008, Conclusion of Law 2, *mimeo.* at 40.

respond to the conservation price signals. We are also mindful that DRA provided only a three tier conservation rate design, rather than providing us both a two tier and a three tier proposal.

DRA proposes to collect 25% of the fixed costs in the meter charge and the remaining revenue requirement in commodity rates.⁸³ This is consistent with the Best Management Practice (BMP) established by the CUWCC, which requires that at least 70% of the total annual revenues be collected through the quantity charge. DRA testifies that reducing the service charge further, and thereby increasing quantity rates, would harm low-income customers, because Great Oaks' low-income program provides a 50% discount in the meter charge.⁸⁴ In its three tiered rate design, the break point between Tier 1 and Tier 2 is 13 hundred cubic feet (Ccf) per month, which is the mid-point between the annual monthly average use and the winter average use based on 10 years of data, and the break-point between the second and third tier is 32 Ccf, a level 10 Ccf above the ten year historical average summer usage.⁸⁵ For single-family residential customers, DRA's proposal results in 41% of total water sales and 17% of customer bills in Tier 1, 38% of total water sales and 46% of customer bills in Tier 2, and the remaining 21% of total water sales and 36% of customer bills in Tier 3 on an annual basis.

⁸³ Best Management Practice 11 of the California Urban Water Conservation Council (CUWCC) is that at least 70% of the total costs be recovered through the quantity, or commodity, portion of the rate.

⁸⁴ Exhibit 16 at 14-14.

⁸⁵ Exhibit 16 at 14-4.

DRA's rate differentials between tiers are 11% between Tiers 1 and 2 and 19% between Tiers 2 and 3. We find that the differentials between tiers are too high given the limited data. A rate differential of 8% between Tiers 1 and 2 and a rate differential between Tiers 2 and 3 of 15% would lessen the rate shock for large water users while still providing a strong price signal in the trial period. Therefore, we will make this modification to DRA's proposal. With this modification, we adopt DRA's conservation rate design for single-family residential customers, and calculate the resulting rates using the rate design principles set forth in Appendix B.

We expect Great Oaks to work with DRA to ensure that its new customer record and billing system is tracking the proper data during the coming GRC period so that the Commission can properly assess the effectiveness of the conservation rate design in the next GRC and consider extending the rate design to other customer classes.

5.8.2. Water Revenue Adjustment Mechanism (WRAM) Proposals

As discussed earlier, DRA is proposing a Monterey-style WRAM be adopted with its rate design proposal, while Great Oaks is requesting that the Commission first adopt its "drought-adjusted" sales forecast and then authorize both a Monterey-style WRAM and a full WRAM.

While DRA strongly supports the Commission's conservation objectives, it does not agree with Great Oaks' requests. Rather, it recommends the WRAM balancing account styled after California-American Water Company's Monterey District (generally referred to as a Monterey-style WRAM) as this is sufficient to ensure Great Oaks does not have a financial disincentive to implement the conservation rate design DRA proposes. The Commission has previously

adopted the Monterey-style WRAM for San Jose Water Company in D.08-08-030, for Suburban Water Systems in D.08-02-036, and most recently for the Fontana and Los Angeles County divisions of San Gabriel Valley Water Company in D.10-04-031. The Monterey-style WRAM corrects for the difference between revenue collected under conservation rates and revenue that would have been collected under uniform rate design. DRA recommends that Great Oaks' supply cost balancing accounts for purchased power and the pump tax should remain as they are currently established since there is not a full decoupling of revenues from sales under the Monterey-style WRAM.

DRA asserts that the Monterey-style WRAM is appropriate for Great Oaks as it removes the utility's disincentive to implement an increasing block rate design to encourage water conservation while, consistent with the Commission's standard rate design, leaves Great Oaks at risk for lost revenues from decreased sales and allows Great Oaks to retain excess revenues from increased sales.

DRA does not support a "full" WRAM that would decouple sales from revenues because it asserts that Great Oaks is not under a production limitation, has not implemented a conservation program, does not actively encourage its customers to conserve, and its recorded consumption data do not show its customers have significantly conserved. DRA does support authorizing Great Oaks a memorandum account to track any additional expenses it incurs to increase customer education and participation in SCVWD's conservation programs in the GRC period.

We agree with DRA that a Monterey-style WRAM is the appropriate mechanism for Great Oaks to adopt in conjunction with the Commission's introduction of conservation rate design. As discussed above, we have modified DRA's conservation rate design proposal to make it more moderate so that

customers will have time over the coming GRC period to adjust their consumption in response to the price signals. A Monterey-style WRAM will decouple revenue from rate design to prevent Great Oaks from gaining or losing revenue as a result of conservation rates.

Great Oaks has not provided evidence of additional conservation measures its customers are making that would support consideration of a full WRAM mechanism. As we have previously discussed, SCVWD's call for a 15% reduction in consumption is not mandatory, is set to expire shortly, and does not qualify Great Oaks to deviate from the sales forecasting methodology specified in the Rate Case Plan. In addition, Great Oaks does not obtain any of its water supply from SCVWD and it has informed its customers in its 2009 Water Supply Report and at the PPH in this proceeding that it has ample water supply to serve them.

While Great Oaks has made several requests to introduce updated data into this record to support a claim of recently declining sales, even if we were to deviate from our Rate Case Plan requirements to allow consideration of the data, it would still not qualify Great Oaks for a full WRAM unless the utility could clearly show any decline in sales is due to conservation programs rather than the continuing economic downturn that began in 2008. We have clearly stated in other decisions that the WRAM is not intended to compensate water utilities for sales losses due to changes in the economy.

We discuss here our basis for concluding that Great Oaks has not actively promoted conservation in its service territory to a degree that would warrant consideration of a full WRAM. In its application, Great Oaks provides information on the conservation measures it has taken. (See Exhibit 1, Chapter 9 of Exhibit E.) As discussed in its last GRC, the Division of Water and Audits

recommended that Great Oaks work in cooperation with CUWCC to develop an effective conservation incentive program which would be attractive to its customers. Great Oaks did not apply for membership in the CUWCC until April 30, 2007 and still has not begun to offer conservation programs that meet CUWCC's Best Management Practices (BMP). Great Oaks states that if the Commission authorizes it an appropriate memorandum account and cost recovery mechanism in this proceeding, it will develop the programs.⁸⁶

DRA testifies that it supports Great Oaks promoting SCVWD's existing conservation programs and that this can be done at little cost using existing personnel through bill inserts, office posters, a link on Great Oaks' website to SCVWD's programs, and having its customer service representatives recommend conservation measures and participation in SCVWD's programs when they assist customers who call about their bills or make other service requests.⁸⁷

DRA supports authorizing a memorandum account for costs associated with these actions. DRA presents a table showing SCVWD's record of Great Oaks' customers requesting Water Wise House Calls, appliance rebates, and technical assistance from July 2007 through May 2009 and concludes that "it is

⁸⁶ The Commission made a general finding in its last GRC that the conservation measures outlined in Great Oaks' 2005 Water Management Plan were satisfactory but recommended the development of an effective conservation incentive program that would be attractive to its customers. The Commission did not adopt Great Oaks' proposed Conservation Gold Seal Program as it did not find it offered customers an incentive to make conservation investments.

⁸⁷ Another proposal raised at hearing is for Great Oaks to print on the bottom of customers' bill a line that states free water audits are available from SCVWD and include a phone number to call. Great Oaks' CEO at first voiced concerns but then stated he would be willing to do this. TR 2:140-142.

clear that Great Oaks' customers are not taking full advantage of the conservation programs currently offered."⁸⁸

In this application, Great Oaks proposed to offer a Conservation Service Charge Discount (CSCD) Program that would give residential customers who request and receive SCVWD's free Water Wise audit a 50% discount on their monthly service charges if the customers provides written confirmation that they would implement the recommendations provided by SCVWD in its Water Wise audit. As part of this program, Great Oaks requested establishment of a memorandum account to track all administrative expenses and a CSCD WRAM mechanism to track the impacts of the CSCD Program on quantity revenues for future disposition.⁸⁹ At hearings and in briefs, Great Oaks did not pursue this proposal.

Based on the discussion above, we find that adoption of a Monterey-style WRAM is the appropriate mechanism for Great Oaks. Therefore, we adopt DRA's recommendation and direct that Great Oaks file tariff pages consistent with the mechanism we have previously approved for other water utilities and implement the Monterey-style WRAM and the conservation rate design on the same date, a date that is within 90 days of issuance of this decision.

Great Oaks may also file by a Tier 2 Advice Letter a request for memorandum account treatment of conservation expenses in the coming GRC period if it first meets and confers with DRA and proposes specific programs and expenditure caps in its filing.

⁸⁸ Exhibit 16 at 13-4.

⁸⁹ See Exhibit 1, Exhibit E, Chapter 9, Exhibit 9-1.

5.9. Revenue Requirement and Rate Tables

Our adopted revenue requirement of \$12,594,260 for the test year beginning July 1, 2010 is attached as Appendix A and rate tables are attached as Appendix B. Great Oaks is authorized to file within 10 days of this decision by a Tier 1 advice letter, revised tariff pages to implement these rates on a going-forward basis.

Great Oaks is also authorized to file a Tier 1 advice letter to recover, by a surcharge amortized over a 12 month period, the difference between the interim rates established in AL 196C-W and the final rates adopted here. Great Oaks should use the methodology set forth in D.07-12-055 for this Advice Letter and amortize the surcharge over the following twelve months. Great Oaks should earn interest at the 90-day commercial paper rate on the surcharge balance.

For escalation years 2011/2012 and 2012/2013, Great Oaks must file Tier 2 advice letters in conformance with General Order 96-B proposing new revenue requirements and corresponding revised tariff schedules as set forth in the Commission's Rate Case Plan (D.07-05-062) for Class A Water Utilities and shall include appropriate supporting workpapers. The revised tariff schedules shall take effect no earlier than July 1, 2011 and July 1, 2012, respectively and shall apply to service rendered on and after their effective dates. The proposed, revised revenue requirements and rates shall be reviewed by the Commission's Division of Water and Audits. The Division of Water and Audits shall inform the Commission if it finds that the revised rates do not conform to the Rate Case Plan, this order, or other Commission decisions, and if so, reject the filing.

6. Division of Water and Audits' Verification Report

On June 21, 2010, the assigned Commissioner and ALJ issued a ruling in response to learning that Great Oaks had been withholding monthly payments

to SCVWD of ratepayer-provided pump tax funds since April 2009. The June 21, 2010 ruling granted in part DRA's March 19, 2010 "Motion to Reopen the Record to Admit Great Oaks' Nondisclosure of Lack of Payment of Groundwater Charges and Request that the Commission Issue an Order to Show Cause for Violation of Rule 1.1. and Possible Violation of Section 2114" and directed our Division of Water and Audits to:

- verify Great Oaks' assertion that the ratepayer provided funds are being held in a separate bank account and that the provisions of the account require approval by the Santa Clara Superior Court for any of these funds to be dispensed to an entity other than the SCVWD,
- verify that Great Oaks' accounting entries reflect the utility's assertions that ratepayers are not liable for late payment interest and penalty charges relating to the withheld payments, and
- determine whether Great Oaks' failure to inform the DRA and the Commission of its actions in withholding the funds from SCVWD violates any GAAP or Commission accounting or reporting requirements.⁹⁰

⁹⁰ Great Oaks takes exception with the ruling's statement that Great Oaks' asserted "ratepayer provided funds are being held in a separate bank account and that the provisions of the account require approval by the Court for any of these funds to be dispersed to an entity other than the SCVWD." We clarify here that the actual assertion by Great Oaks' Chief Financial Officer is that she precisely followed the instructions of Great Oaks' CEO to "establish a separate bank account (the 'groundwater charge account') for the purpose of depositing and securely holding, groundwater charges imposed by the Santa Clara Valley Water District until a legal determination is made on the disposition of the funds" and the actual statement by Great Oaks' General Counsel is "Of course, if DRA had conducted an investigation it would also have learned that Great Oaks has deposited all of the disputed groundwater charges into a secure account under instructions that the funds remain in the account until a court of competent jurisdiction, along with the Commission, approve the final disposition of the funds."

Footnote continued on next page

Pursuant to the June 21, 2010 ruling, Division of Water and Audits served its Financial and Compliance Verification of Great Oaks Water Company for the Period March 1, 2009 through June 30, 2010 (Verification Report) on the service list to this proceeding on August 20, 2010. The verification assignment was performed by Division of Water and Audits' Utility Audit, Finance and Compliance Branch (UAFCB) and its Verification Report is attached to this decision as Appendix D. In the executive summary, UAFCB summarizes its findings as follows:

1. Great Oaks deposited its ratepayer-provided pump tax funds in an "escrow-type account" (a money market mutual fund account) with Waddell & Reed Services (W&R), rather than a banking entity. As of June 30, 2010, deposits in the escrow-type account total \$5,363,124.01, including interest earned.⁹¹ (Refer to Section IV, Goal of this report for details.)
2. Great Oaks did not make any withdrawals from the aforementioned "escrow-type account" during the verification period. Great Oaks is setting aside its SCVWD pump tax payments in the escrow-type account pending the outcome of a lawsuit. (Refer to Section IV, Goal 2 of this report for details.)
3. Great Oaks did not hold ratepayers liable for the late payment interest and penalty charges imposed by SCVWD on the withheld pump tax payments. Great Oaks recorded the interest and penalty charges in its Income Statement as the expense of its shareholders. (Refer to Section IV, Goal 3 of this report for details.)
4. Great Oaks used the Financial Accounting Standard Statement #5 (FAS #5) to support its action of not disclosing to DRA and the

See Great Oaks' April 12, 2010 response at 9 and the attached Declaration of Vicki Morse at 1.

⁹¹ Per W&R's July 28, 2010 confirmation letter.

Commission that it withheld pump tax payments to SCVWD and the establishment of an escrow-type account. With regard to the disclosure requirements, UAFCB is unaware of Great Oaks being out of compliance with Generally Accepted Accounting Principles (GAAP) requirements. However, UAFCB found that Great Oaks is not in compliance with Public Utilities Code §§ 451 and 794, the Uniform System of Accounts (USOA) for Class A Water Utilities, and D.04-06-018. (Refer to Section IV, Goal 4 of this report for details.)

Based on the above findings, Division of Water and Audits provides recommendations as to how Great Oaks should bring its procedures into compliance with the Commission's accounting and reporting requirements. The June 21, 2010 ruling did not direct Division of Water and Audits to reach any conclusions as to whether fines or other penalties should be assessed, and Division of Water and Audits does not do so. Division of Water and Audits' recommendations are:

- **Separate Bank Account** – Great Oaks should provide the Commission's DRA with the conditions, requirements, agreements, instructions, etc. for the separate escrow-type account opened with W&R which Great Oaks was not able to provide during UAFCB's verification fieldwork. Great Oaks should be required to transfer the entire balance in its W&R escrow-type account into a secured and separate "bank escrow" account or to a regular standard bank account.

Great Oaks should propose as part of its next GRC rate design filing a method to separate out the total pump tax component collected as revenue via surcharges, service charges, and quantity charges if pump tax is still an operating expense.

- **Withdrawals from Separate Bank Account** – To the extent that Great Oaks continues to maintain its escrow-type account with W&R, Great Oaks should be required to establish a specific withdrawal provision with W&R to ensure that any withdrawals made to entities other than SCVWD must require an approval of the Superior Court of Santa Clara County or the Commission.

- **SCVWD Interest & Penalty Charges** – No recommendation.
- **Accounting Compliance** – Great Oaks should be required to submit to the Division of Water and Audits a written proposal for its accounting of pump tax revenues, expenses, cash, receivables, and payables in compliance with the USOA. To avoid future confusion and problems, Great Oaks should be required to advise the Commission with information relating to any new accounting approaches, unusual accounting treatment or items, relevant procedures and records especially involving significant amounts.

Pursuant to the schedule set in the June 21, 2010 ruling, both Great Oaks and DRA filed comments on August 30, 2010 and reply comments on September 7, 2010.

In its opening comments, Great Oaks states that based, in part, on the Verification Report it has decided to remit to SCVWD all the payments it has withheld and to continue to make payments to SCVWD when due, under protest; further, Great Oaks commits that it will not withhold future payments unless it first notifies the Commission. Great Oaks requests that the Commission correct the Verification Report in the manner specified in its comments and declare the Verification Report moot as to the issues in this proceeding, due to Great Oaks' decision to pay groundwater charges under protest to SCVWD.

In the remainder of its comments, Great Oaks focuses on whether (1) Division of Water and Audits exceeded the scope of the June 21, 2010 ruling when it investigated the type of account holding ratepayer funds and the terms and conditions of the account, (2) Division of Water and Audits properly cites to the latest Rate Case Plan decision, and (3) Division of Water and Audits improperly presents legal conclusions rather than compliance findings. We do not find these issues to have substantive merit. In the instances where Great

Oaks directly addresses whether its nondisclosure to the Commission and DRA of the approximately \$5,000,000 in ratepayer-provided funds it was withholding violated any of the Commission's accounting and reporting requirements, we do not find Great Oaks' positions persuasive.

In its comments, DRA generally supports Division of Water and Audits' findings and recommends that the Commission admit the Verification Report into the record, adopt Division of Water and Audits' recommendations, hold an additional hearing if necessary, and issue a decision in this proceeding, not in a separate proceeding. DRA continues to recommend that Great Oaks be fined; it does not agree with Great Oaks' assertion that the issues raised in its motion and the June 21, 2010 ruling are "moot" due to Great Oaks having released the withheld funds.

DRA's comments reflect its comprehensive understanding of the Commission's accounting and reporting requirements and provide strong support for Division of Water and Audits' findings in its Verification Report. In addition to Division of Water and Audits' recommendations, DRA requests the Commission make a specific finding that Great Oaks' shareholders will be responsible for all interest, penalties, and legal expenses associated with the nonpayment of groundwater production charges. DRA makes this recommendation due to the current size of the interest and penalties, approximately \$500,000, and because it asserts that Great Oaks could make adjustments to its operating and maintenance recorded expenses to include these

interest and penalty charges in its next or future GRCs and there is no mechanism in place to prevent this.⁹²

Based on a review of Division of Water and Audits' Verification Report and parties' comments, we find that good cause exists to further investigate Great Oaks' actions and whether to impose fines. However, we are not clear on why DRA recommends that further investigation be done here rather than in an adjudicatory proceeding.

We find that Commission staff should prepare an Order Instituting Investigation (OII) to further review whether Great Oaks' actions in not informing the Commission and its staff that it was withholding payment to SCVWD of the pump tax revenues collected from its customers violated any of the following: the Commission's Rule 1.1., our Uniform System of Accounts (USOA) for Class A Water Companies, our Rate Case Plan, or Public Utilities Code Sections 451 and 794, and that as part of the OII Great Oaks should be ordered to show cause why penalties should not be imposed for any violations.

Based on Great Oaks' actions we also find that good cause exists to routinely require Great Oaks to timely report to the Commission any significant changes it makes in its accounting approaches or treatment. We will also ensure that the Commission carefully reviews Great Oaks' operations within the next three years under our Rate Case Plan application procedures. We should not grant a waiver of Great Oaks' triennial filing requirement, an extension of time for filing, or a request to file by advice letter rather than application.

In addition to finding that an OII should be prepared, we find that:

⁹² See Reply at 10.

- Great Oaks must advise by a letter to the directors of the Division of Water and Audits and the Division of Ratepayer Advocates, with copies sent to the branch chief of the Utility Audit, Finance and Compliance Branch and the service list of this proceeding or its subsequent GRC, within 60 days when it adopts any new accounting approaches, unusual accounting treatment or items, and changes to relevant procedures and records, especially any event involving a change that represents a difference of 10% or more between the new accounting approach or treatment and the prior accounting approach or treatment.
- The shareholders of Great Oaks shall be solely responsible for all interest, penalties, and legal expenses associated with the nonpayment of groundwater production charges.
- Great Oaks shall timely file its next GRC request as an application, not as an Advice Letter, and shall do so under the schedule adopted in Decision 07-05-062 and in compliance with all filing requirements set forth in that decision's Rate Case Plan.

7. Comments on Alternate Proposed Decision

The alternate proposed decision of the assigned Commissioner was mailed to the parties in accordance with Public Utilities Code Section 311(d) and both parties filed comments and reply comments on the alternate proposed decision pursuant to our requirements as set forth in Rule 14.3 of the Commission's *Rules of Practice and Procedure*. Based on our review of the comments, we correct the revenue requirement table on page 2, add language to Conclusion of Law 12, add an ordering paragraph on Resolution W-4534, and make minor changes to the text for clarification and to correct typographical errors.

8. Assignment of Proceeding

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

Findings of Fact

1. By letter dated May 4, 2009, the Commission's Executive Director granted Great Oaks permission to delay submitting its general rate case application from July 1, 2009 to September 1, 2009.
2. Great Oaks submitted an updated and corrected application on October 19, 2009. The primary change in this application is the reflection of an interim rate increase of 1.75%, subject to refund, granted by Advice Letter 196C-W, effective September 1, 2009.
3. Great Oaks failed to timely provide its customers written notice of its request to raise rates, as required by Rule 3.2(d) of our *Rules of Practice and Procedure*. Great Oaks later provided this notice between November 5 and December 17, 2009.
4. Great Oaks' water system was last inspected by the California Department of Public Health in July 2009 and our record reflects that between 2006 and September 2009 Great Oaks has been in compliance with all state primary drinking standards and does not have any violations.
5. Great Oaks has not been warning its customers of a drought or helping them prepare to significantly reduce their consumption.
6. DRA correctly uses the Rate Case Plan methodology of D.07-05-062 to forecast sales for residential, multifamily, and business customers.
7. DRA's sales forecasts for industrial, public authorities, private landscaping, schools, agricultural, and private fire protection services use the "best available data" and apply the proper forecasting methodology.

8. Great Oaks' proposed increase in the reconnection charge from \$10.00 to \$25.00 during regular business hours and from \$15.00 to \$40.00 at other than regular working hours is reasonable and is not projected to have a significant impact on low-income customers; DRA intends to monitor the actual impact on low income customers as part of its conservation rate design review.

9. Great Oaks' projection of unaccounted for water at 4.04% of water sales is reasonable.

10. DRA's projections of purchased power expenses and groundwater charges are directly tied to our adopted sales forecast.

11. Since Great Oaks' last general rate case, its subsidiary Great Oaks LLC purchased an office building and the utility rents 1/6 of the building for utility operations.

12. We find that Great Oaks should be allowed to use its existing employees to pursue the Santa Clara Valley Water District litigation over the coming GRC period because its General Counsel, in consultation with its Chief Executive Officer, has been successful at the trial court level in the litigation and because all net benefits will be immediately passed through to its customers if the utility is ultimately successful. We recognize that normal utility operations do not support two full-time attorney positions, and we will closely review this issue in the next GRC proceeding.

13. Great Oaks has not adequately justified its request for an additional field technician.

14. In its next general rate case application, Great Oaks should provide a comprehensive showing to support the rental expense it requests and to establish that it has fully complied with all Commission accounting and reporting requirements in its transactions with its subsidiary Great Oaks LLC.

15. Great Oaks does not adequately support its request for an increase in rate case expenses and uncollectibles.

16. DRA's recommendations for rate case expenses and uncollectibles are reasonable.

17. Great Oaks' tariff pages implementing Resolution W-4534 specifically require that any expense eligible for memorandum account treatment must be recorded on a monthly basis. Great Oaks has not recorded any expenses into this memorandum account.

18. The Commission has authorized the establishment of memorandum accounts when projected costs and/or ratepayer benefits are uncertain.

19. Great Oaks' recommendations for \$1,156,392 in test year depreciation expense and a net rate base of \$11,069,738 are very close to DRA's recommendations and should be used for ratemaking purposes.

20. Great Oaks' Department of Motor Vehicle license fees and \$533 "payroll expense" are not taxes.

21. Current state and federal payroll tax rates should be used in tax calculations for ratemaking purposes.

22. Great Oaks does not provide sufficient support for its recommended Ad Valorem tax amount of \$223,013. DRA's recommendation of \$177,500 is adequately supported and we find it reasonable.

23. Interest expense should be imputed for ratemaking purposes if the Commission imputes a debt component in its cost of capital determination.

24. DRA's rate design proposal to collect 25% of the fixed costs in the meter charge and the remaining revenue requirement in commodity rates is reasonable and consistent with the Best Management Practices established by the California Urban Water Conservation Council.

25. A conservation rate design will advance our Water Action Plan conservation objectives.

26. We find the rate differentials between tiers in DRA's conservation rate design proposal too high given the limited data and initial implementation.

Conclusions of Law

1. We should deny Great Oaks' August 20, 2010 "Motion to Reopen Record for Limited Purpose of Updating and Revising Water Sales Data and Addressing Conservation Water Revenue Adjustment Mechanisms" as the relief requested would violate:

- (a) the Rate Case Plan's adopted procedure for ratemaking adjustments during the Rate Case Plan's transition period and for updates during the scheduled proceeding;
- (b) The interim relief authority granted Great Oaks in Advice Letter 196C-W; and
- (c) The scope of this application.

2. We should deny Great Oaks' October 12, 2010 "Motion to Reopen the Record for Limited Purpose of Admitting Evidence Relevant to Water Sales Forecasts and Conservation Issues" as the relief requested would violate the Rate Case Plan's adopted procedure for updates during the scheduled proceeding and Great Oaks has not met the standards established in the Rate Case Plan for an extraordinary circumstance that would warrant the Commission deviating from its normal procedures.

3. Great Oaks' water system and water quality is in compliance with the requirements of the California Department of Public Health.

4. Santa Clara Valley Water District (SCVWD) does not have authority to order mandatory conservation restrictions for Great Oaks Water Company and

its directives do not impose a “government mandated production limitation” as defined in D.07-05-062’s Rate Case Plan at Appendix A.

5. We should adopt DRA’s sales forecasts for residential, multifamily, business, industrial, public authorities, private landscaping, schools, agricultural, and private fire protection services.

6. Great Oaks has not met its burden of proof to justify its proposed salary levels for employees.

7. DRA’s use of its October 20, 2009 Compensation Per Hour Annual Rate of Change memorandum to adjust Great Oaks’ 2009 base salaries for employees by 0.4% and then escalate test year salaries by 2.3% is reasonable and should be adopted.

8. Under the terms of Resolution W-4534, Appendix C to this decision, Great Oaks should not include in its revenue requirement any costs related to its SCVWD litigation. We find good cause exists, however, to allow Great Oaks to use its existing employees to pursue the SCVWD litigation over the coming GRC period.

9. Resolution W-4534 remains in force for all SCVWD litigation, to include the lead case, Case No. 109CV146018 (amended) and all subsequent related cases, and requires that if Great Oaks is ultimately successful it must immediately file an advice letter to pass-through the net benefits to its ratepayers.

10. All outside services litigation expenses related to the SCVWD litigation should be removed from Great Oaks’ revenue requirement.

11. An adjustment to management salaries for ratemaking purposes should be made to reflect management time spent on non-utility property management.

Reasonable disallowances are:

- (a) A ten percent disallowance for the chief executive officer;
- (b) A five percent disallowance for the treasurer; and
- (c) A ten percent disallowance for the regulatory affairs attorney.

12. Recognizing that normal utility operations do not support two full-time attorney positions, the Commission should closely review management staffing levels in the next GRC proceeding. Great Oaks should bear the burden when it requests inclusion of two full-time attorney positions in utility rates, to provide a comprehensive showing of its two full-time attorneys' time spent on utility activities, non-utility activities as well as time spent on all litigation on behalf of Great Oaks or on litigation which purpose is to advance Great Oaks' managers' or its ratepayers' interests. Great Oaks should provide DRA with a full description of all litigation involving Great Oaks in the next GRC.

13. Based on Commission policy, as affirmed by the California Supreme Court, dues, donations, and contributions are not recoverable in rates. Therefore, Great Oaks' charitable and political contributions and the expenses included in its "dues and subscriptions" should not be recovered from ratepayers.

14. Great Oaks should be authorized to file by a Tier 2 advice letter to establish a memorandum account for outside legal expenses related to litigation with the City of San Jose over its service territory. This memorandum account should have a cap of \$225,000 for expenses, require expenses to be recorded on a monthly basis, and require ratemaking review when Great Oaks seeks recovery. Great Oaks should bear the burden when it requests recovery of the recorded costs, to show that separate recovery of the types of costs recorded in the account is appropriate, that it acted prudently when it incurred these costs, and that the level of costs is

reasonable. Great Oaks may seek recovery of the costs in this memorandum account in its next GRC or through a Tier 3 Advice Letter filing.

15. Great Oaks should be allowed to submit a Tier 2 advice letter to recover the costs of the County View Tank when the project is completed and it is used and useful. Construction costs should be capped at \$385,000 and Great Oaks should be allowed to recover the costs from future customers through a service fee.

16. Great Oaks' ratemaking proposal for developer/customer funded projects is in compliance with Tariff Rule 15.

17. DRA has not presented sufficient cause for the Commission to deviate from the ratemaking methodology adopted in D.89-11-058 for computing California Corporate Franchise Tax.

18. DRA has properly calculated the Domestic Production Activities Deduction for Great Oaks.

19. We should adopt DRA's conservation rate design proposal for single family residential customers with the following modification: the rate differential between Tiers 1 and 2 should be 8% and the rate differential between Tiers 2 and 3 should be 15%.

20. Great Oaks should meet and confer with DRA regarding the details of the customer data that will be tracked and reported during the coming GRC period for purposes of assessing the effectiveness of the conservation rate design and should then be allowed to request a memorandum account to track the estimated costs.

21. Great Oaks should be authorized a Monterey-style water revenue adjustment mechanism that tracks and corrects for the difference between revenue collected under conservation rates and revenue that would have

been collected under uniform rate design. Great Oaks' supply cost balancing accounts should not be converted to full-cost balancing accounts since there is no full decoupling of revenues from sales.

22. Great Oaks should be allowed to file a Tier 2 advice letter requesting memorandum account treatment for conservation expenses if it first meets and confers with DRA and in its advice letter proposes specific programs and expenditure caps. Great Oaks Water Company will bear the burden when it requests recovery of the recorded costs, to show that separate recovery of the types of costs recorded in the account is appropriate, that the utility acted prudently when it incurred these costs and that the level of costs is reasonable.

23. Based on the Verification Report submitted on August 20, 2010 by the Division of Water and Audits, attached to this decision as Appendix D, and the comments filed by parties, good cause exists to further investigate Great Oak's actions and whether fines should be imposed. Therefore, the Commission should open an OII to further review whether Great Oaks' actions in not informing the Commission and its staff that it was withholding payment to SCVWD of the pump tax revenues collected from its customers violated any of the following: the Commission's Rule 1.1., our Uniform System of Accounts (USOA) for Class A Water Companies, our Rate Case Plan, or Public Utilities Code Sections 451 and 794. As part of the OII Great Oaks should be ordered to show cause why penalties should not be imposed for any violations.

24. Based on the Verification Report and comments:

- (a) Great Oaks should be required to advise by a letter to the directors of the Division of Water and Audits and the Division of Ratepayer Advocates, with copies sent to the branch chief of the Utility Audit,

Finance and Compliance Branch and the service list of this proceeding or its subsequent general rate case, within 60 days when it adopts any new accounting approaches, unusual accounting treatment or items, and changes to relevant procedures and records, especially any event involving a change that represents a difference of 10% or more between the new accounting approach or treatment and the prior accounting approach or treatment; and

- (b) the shareholders of Great Oaks should be solely responsible for all interest, penalties, and legal expenses associated with the nonpayment of groundwater production charges.

O R D E R

IT IS ORDERED that:

1. Great Oaks Water Company's August 20, 2010 and October 12, 2010 motions to reopen the record are denied.
2. All motions not addressed in this decision are denied.
3. The revenue requirement and rate tables to today's decision at Appendices A and B are adopted.
4. Great Oaks Water Company is authorized to file in accordance with General Order 96, and to make effective on not less than five days' notice, revised tariff sheets that are consistent with the test year July 1, 2010 – June 30, 2011 revenue requirement and adopted rates at Appendices A and B of this decision. The revised tariff sheets shall include the conservation rate design adopted in this decision and shall apply to service rendered on and after their effective date.
5. Great Oaks Water Company is authorized to request a surcharge to true-up the interim rates authorized in Advice Letter 196C-W, effective September 1, 2009, to the final rates adopted here using the methodology set forth in

Decision 07-12-055 and to be collected over a twelve-month period. The tariff implementing the surcharge may be included in the filing authorized in Ordering Paragraph 4.

6. Great Oaks Water Company (Great Oaks) is authorized to file by a Tier 2 advice letter to establish a memorandum account for outside legal expenses related to litigation with the City of San Jose over its service territory. This memorandum account shall have a cap of \$225,000 for expenses, require expenses to be recorded on a monthly basis, and require ratemaking review when Great Oaks seeks recovery. Great Oaks shall bear the burden when it requests recovery of the recorded costs, to show that separate recovery of the types of costs recorded in the account is appropriate, that it acted prudently when it incurred these costs, and that the level of costs is reasonable. Great Oaks may seek recover of the costs in this memorandum account in its next General Rate Case or through a Tier 3 Advice Letter filing.

7. Great Oaks Water Company (Great Oaks) may submit a Tier 2 advice letter to recover the costs of the County View Tank when the project is completed and it is used and useful. Construction costs are capped at \$385,000 and Great Oaks shall recover the costs authorized by the Commission from future customers through a service fee.

8. Great Oaks Water Company (Great Oaks) may file a Tier 2 advice letter requesting memorandum account treatment for conservation expenses if it first meets and confers with the Division of Ratepayer Advocates and in the advice letter proposes specific programs and expenditure caps. Great Oaks shall bear the burden when it requests recovery of the recorded costs, to show that separate recovery of the types of costs recorded in the account is appropriate, that the

utility acted prudently when it incurred these costs and that the level of costs is reasonable.

9. Great Oaks Water Company (Great Oaks) shall file a Tier 2 advice letter with implementing tariff pages to create a Monterey-style water revenue adjustment mechanism that tracks and corrects for the difference between revenue collected under conservation rates and revenue that would have been collected under uniform rate design. Great Oaks' supply cost balancing accounts shall not be converted to full-cost balancing accounts since the water revenue adjustment mechanism approved here today does not fully decouple revenues from sales. The effective date of this advice letter shall be within 90 days of this decision and shall be the same date as the effective date of Great Oaks' conservation rate design. Great Oaks shall meet and confer with Division of Ratepayer Advocates and include in its request the details of the customer data that will be tracked and reported during the coming General Rate Case period for purposes of assessing the effectiveness of the conservation rate design and a request for a memorandum account to track the estimated costs.

10. For escalation years 2011/2012 and 2012/2013, Great Oaks Water Company shall file Tier 1 advice letters in conformance with General Order 96-B proposing new revenue requirements and corresponding revised tariff schedules as set forth in the Commission's Rate Case Plan (Decision 07-05-062) for Class A Water Utilities and shall include appropriate supporting workpapers. The Advice Letter for escalation year 2011/2012 must be filed no later than May 16, 2011 and the Advice Letter for escalation year 2012/2013 must be filed no later than May 16, 2012. The revised tariff schedules shall take effect no earlier than July 1, 2011 and July 1, 2012, respectively, and shall apply to service rendered on and after their effective dates. The proposed, revised revenue requirements and

rates shall be reviewed by the Commission's Division of Water and Audits. The Division of Water and Audits shall inform the Commission if it finds that the revised rates do not conform to the Rate Case Plan, this order, or other Commission decisions, and if so, reject the filing.

11. Great Oaks Water Company shall file its next general rate case by application pursuant to the schedule established in Decision 07-05-062.

12. Based on the Verification Report submitted on August 20, 2010 by the Division of Water and Audits, attached to this decision as Appendix D, and the comments filed by parties, good cause exists to further investigate Great Oak Water Company's (Great Oaks) actions and whether fines should be imposed. Therefore, the Commission's Consumer Protection and Safety Division shall prepare an Order Instituting Investigation (OII) to further review whether Great Oaks' actions in not informing the Commission and its staff that it was withholding payment to Santa Clara Valley Water District of the pump tax revenues collected from its customers violated any of the following: the Commission's Rule 1.1., our Uniform System of Accounts for Class A Water Companies, our Rate Case Plan, or Public Utilities Code Sections 451 and 794. The draft OII shall order Great Oaks to show cause why penalties should not be imposed for any violations.

13. Great Oaks Water Company must advise by a letter to the directors of the Division of Water and Audits and the Division of Ratepayer Advocates, with copies sent to the branch chief of the Utility Audit, Finance and Compliance Branch and the service list of this proceeding or its subsequent general rate case, within 60 days when it adopts any new accounting approaches, unusual accounting treatment or items, and changes to relevant procedures and records, especially any event involving a change that represents a difference of 10% or

more between the new accounting approach or treatment and the prior accounting approach or treatment.

14. The shareholders of Great Oaks Water Company shall be solely responsible for all interest, penalties, and legal expenses associated with the nonpayment of groundwater production charges.

15. In accordance with Resolution W-4534, if Great Oaks is ultimately successful in its Santa Clara Valley Water District litigation, it must immediately file by Advice Letter to pass-through the net benefits to its ratepayers.

16. This proceeding is closed.

This order is effective today.

Dated November 19, 2010, at San Francisco, California.

MICHAEL R. PEEVEY

President

DIAN M. GRUENEICH

JOHN A. BOHN

TIMOTHY ALAN SIMON

NANCY E. RYAN

Commissioners

[D1011034 Appendices A-E](#)