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Mail Date 12/21/07

Decision 07-12-058 December 20, 2007

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of California-American Water Company (U 210 W) for an Order Authorizing it to Increase its Rates for Water Service in its Los Angeles District to Increase Revenues by $2,020,466 or 10.88% in the Year 2007; $634,659 or 3.08% in the Year 2008; and $666,422 or 3.14% in the Year 2009.	Application 06-01-005 (Filed January 9, 2006)

ORDER MODIFYING DECISION 07-08-030 AS MODIFIED BY DECISION 07-11-014, AND DENYING REHEARING

I. INTRODUCTION

Decision (D.) 07-08-030 is the Phase I decision in the California-American Water Company's (Cal-Am) general rate case (GRC) for its Los Angeles District for test year 2007 and attrition years 2008 and 2009. Cal-Am is a Class A water utility with approximately 27,200 customers in its Los Angeles District. The Los Angeles District is served by wells and irrigation water utilizing Cal-Am's groundwater rights and by purchases from municipal wholesalers.

Cal-Am filed its GRC application (A.) 06-01-005 with the Commission on January 9, 2006. Our Division of Ratepayer Advocates (DRA or staff) timely filed a protest on January 30, 2006 and an initial pre-hearing conference (PHC) was held on February 16, 2006. Intervenor status was later granted to the City of San Marino, the City of Duarte and the Utility Workers Union of America, AFL-CIO. Three public participation hearings (PPH) were held in April 2006. At a May 2006 PHC, the parties agreed to bifurcate the proceeding. Cal-Am noticed an all-party settlement meeting for May 23, 2006.

Additional PPHs were held on May 31 and June 1, 2006 and evidentiary hearings on revenue requirement issues were conducted on June 13-15 and 28-29, 2006. On June 26, 2006, Cal-Am and the DRA filed a motion for adoption of a proposed settlement. On July 6, 2006 the City of Duarte filed a protest of the settlement. DRA and Cal-Am filed opening briefs on July 31, 2006; and on August 14, 2006, reply briefs were filed by DRA, Cal-Am, and the cities of Duarte and San Marino. Thereafter, various motions were filed and on February 22, 2007 the assigned Administrative law Judge (ALJ) directed Cal-Am to supplement its February 15, 2007 motion requesting the assigned ALJ reopen the record to accept an amended settlement agreement, which Cal-Am did on February 27, 2007. DRA filed a response on March 7, 2007. As part of its Phase 2 settlement with the DRA, Cal-Am proposed two methods for increasing conservation and reducing its financial risk: a Water Revenue Adjustment Mechanism (WRAM) and a Modified Cost Balancing Account (MCBA) which were to be addressed in Phase 2 of the proceeding.

The presiding ALJ's initial proposed decision (PD) was filed on May 7, 2007. In part the PD determined that if the proposed WRAM and MCBA are adopted in Phase 2, then there should be a corresponding reduction of .50% in Cal-Am's rate of return (ROE). The DRA and Cal-Am filed comments on the PD on May 29 and reply comments on June 4, 2007. The PD was revised four times and version five was emailed to the parties on August 22, 2007 and also made available on the Escutia table at the Commission's meeting on August 23, 2007.

Commission President Peevey filed an alternate decision (alternate) on July 24, 2007. The alternate removed the WRAM and WCBA from consideration, not wanting to prejudge it in a GRC, stating the mechanisms encourage conservation and should be under consideration in an industry-wide proceeding as should any discussion of a ROE reduction. The alternate also included a section that noted that the Commission preferred a conservation loss adjustment mechanism (CLAM) that is focused solely on cost under-and over-

recovery caused by conservation policies because it supports conservation goals and will not require continuous litigation of a ROE adjustment. DRA and Cal-Am filed comments on the alternate on August 13 and reply comments on August 20, 2007. Numerous ex parte communications regarding the proposed WRAM were had with some of the Commissioners' offices before the issuance of D.07-08-030. As part of those communications, Cal-Am objected to the PD's determination that a WRAM should lead to a downward return on equity, arguing that the PD prejudges the issue.

We adopted D.07-08-030 at our August 23, 2007 meeting and mailed the decision on August 24. The discussion at pages 32 to 37 of D.07-08-030 concerning the WRAM and WCBA proposal and the preference for a CLAM is very similar to the alternate.[1] D.07-08-030 acknowledges our concern with the imputed capital structure and the rate base sections of the proposed settlement and we noted that those issues will be further examined in the next GRC. However, D.07-08-030 finds that in weighing the partial settlement between Cal-Am and DRA as "an integrated agreement," it is reasonable in light of the whole record, consistent with the law and in the public interest and adopts it. D.07-08-030 authorizes a ROE for the Los Angeles District of 10.0% for the three-year GRC. D.07-08-030 also adopts, on a pilot basis, a Distribution System Infrastructure Charge (DSIC). In addition, D.07-08-030 fines Cal-Am a total of $11,000 for violation of Commission Rules of Practice and Procedure, rule 3.2(b) for its failure to provide notice of its rate increase applications for 20 years to the City of Inglewood and for 10 years to the County of Los Angeles.

On August 29, 2007 Cal-Am filed a petition to modify D.07-08-030 to include additional tables that would allow Cal-Am to implement the revenue

[1] D.07-08-030 rejects Cal-Am's proposal for a WRAM and a MCBA. D.07-08-030 determines that it would be premature to approve a WRAM for one company's GRC. D.07-08-030 determines that a discussion of these issues and other possible tools to encourage conservation should happen in an industry-wide proceeding, as should a discussion of whether a reduction in ROE is warranted in light of the conservation and financial risk lowering proposals.

requirement adopted by D.07-08-030 under Cal-Am's existing rate design until the Commission completes Phase 2 of this proceeding. By D.07-11-014 we granted Cal-Am's petition, finding good cause existed to grant the petition because in D.07-08-030 we removed from consideration the proposed WRAM and WCBA components of a pending settlement between Cal-Am and the DRA, thereby changing the scope and schedule of Phase 2.

DRA timely filed an application for rehearing of D.07-08-030 on September 24, 2007, taking issue with the Commission's announced policy preference for a CLAM and for stating that adoption of a CLAM for Cal-Am would not require an adjustment to the company's ROE. Specifically, DRA contends that dicta expressing a policy preference in the text of D.07-08-030 for use of a CLAM in Phase 2 and the declaration that a CLAM would not require a ROE adjustment are unsupported by the record and arbitrary. DRA contends that these statements amount to a violation of the staff's procedural and substantive due process rights.

In response to DRA's application for rehearing, we shall make modifications to D.07-08-030 for purposes of clarification and to alleviate certain concerns raised by the DRA. We have reviewed each and every allegation of error raised by our DRA and, as set forth herein, have determined that the allegations are without merit in light of the modifications made by this decision.

II. DISCUSSION

Whether there should be a downward adjustment of ROE if we were to adopt the WRAM and WCBA accounting mechanisms proposed in this proceeding has been an unresolved issue between DRA and Cal-Am throughout A.06-01-005. DRA has counseled that there should be an adjustment to Cal-Am's ROE, and Cal-Am has argued that there should not.

D.07-08-030 contains language noting a preference for a CLAM. It also encourages the DRA and Cal-Am to modify the WRAM proposal with a more narrowly focused WRAM, which is what it infers a CLAM is. D.07-08-030

declares that for policy reasons we prefer the more narrow mechanism, i.e., CLAM, for Cal-Am's Los Angeles District pilot conservation program and that modified mechanism should ensure that Cal-AM does not under-collect due to conservation rate design and new conservation programs and does not over-collect from its ratepayers.

Although the staff does not question our authority to encourage parties to consider and negotiate alternate mechanisms, it believes that in D-07-08-030 we exceed our authority by: "…unambiguously adopt[ing] conclusions that (1) advocate use of a specific regulatory accounting mechanism, a CLAM, to the exclusion of the parties' proposed WRAM, and (2) determine that a CLAM should be considered to have no impact on a company's ROE." (DRA application for rehearing at p. 4.)

The language DRA terms "conclusions" exists only in text and language in a decision's text is generally considered dicta. It was presented to assist the parties in Phase 2 and does not constitute determinations of material issues. There are no findings of fact or conclusions of law or ordering paragraphs in D.07-08-030 regarding our stated policy preference for a CLAM or on the question of whether it would affect Cal-Am's ROE. Thus, the Commission did not make any determinations regarding a CLAM or its effect on Cal-Am's ROE.

The challenged dicta was meant to encourage the parties in Phase 2 to consider a CLAM, which the decision suggests is a modified version of the proposed WRAM, rather than the proposed WRAM. We also suggested that the parties might be more successful in pursuing that mechanism. That encouragement for the parties to consider a CLAM does not necessarily prejudge how the Commission will respond to a WRAM if the parties continue to pursue it.

As demonstrated by DRA's rehearing application, the dicta involving the suggested CLAM and its possible effect on Cal-Am's ROE is subject to be

misinterpreted as a determination or prejudgment. Accordingly, we modify the challenged dicta as proposed below.[2]

Further, we note that the statement: "[i]f Cal-Am and DRA modify their pending Phase 2 settlement to replace the proposed WRAM with a … [CLAM] that meets the criteria discussed here, an ROE adjustment would not be necessary," appears to be more than mere opinion. (See D.07-08-040 at p. 37.) Because there is no record to support that conclusion it should not be included in D.07-08-030, even in the text. Accordingly, we shall modify the challenged decision as follows to remove suggestive language from the text.

On page 35 of D.07-08-030 in first full paragraph of the section entitled Commission's Preference for a Conservation Loss Adjustment Mechanism for Los Angeles District, the third sentence is modified to delete the words: "… and will not require continuous litigation of an ROE adjustment" so that the paragraph reads as follows:

> We encourage Cal-Am and DRA to modify their pending Phase 2 settlement to include a conservation loss adjustment mechanism that is focused solely on cost under- and over-recovery caused by our conservation policies. The objective of this mechanism should be to ensure Cal-Am does not undercollect its authorized fixed costs due to conservation rate design and new conservation programs and to ensure ratepayers are protected from any over-recovery of authorized costs that are due to shifting more cost recovery to the volumetric rate under a conservation rate design. We prefer this approach because it directly supports our conservation goals and it will not require continuous litigation of an ROE adjustment.[footnote omitted] Such a mechanism should provide….

In first full paragraph on page 37 of D.07-08-030, continuing in the section entitled Commission's Preference for a Conservation Loss Adjustment

[2] As noted above, D.07-08-030 was modified by D.07-11-014. Our modification to D.07-08-030 shall be to D.07-08-030 as modified by D.07-11-014.

Mechanism for Los Angeles District, the second sentence is deleted in its entirety so that the paragraph reads as follows:

> For the reasons discussed here, a Phase 2 adoption of a conservation loss adjustment mechanism (CLAM) rather than the proposed WRAM is the Commission's policy preference for Cal-Am's Los Angeles District pilot conservation program. If Cal-Am and DRA modify their pending Phase 2 settlement to replace the proposed WRAM with a conservation loss adjustment mechanism that meets the criteria discussed here, an ROE adjustment would not be necessary.

The first full paragraph on page 61 of D.07-08-030 in the section entitled Comments on the Proposed Alternate Decision is modified to delete the third sentence: "However, if a CLAM can be negotiated, the rate design in Phase 2 is likely to proceed smoothly" in its entirety, and the words "That said," in the fourth sentence are also deleted so that the forth sentence becomes the third sentence and begins with the word "It" so that the paragraph reads as follows:

> The CLAM was suggested to encourage the development of conservation rates in Phase 2 of this proceeding. It is not a requirement that Cal-Am and DRA need to agree to a CLAM to move Phase 2 forward. However, if a CLAM can be negotiated, the rate design in Phase 2 is likely to proceed smoothly. That said, iIt was not the intent to provide sweeping generalizations about the benefits of a CLAM. We intended that the preference for a CLAM was limited to this GRC only, primarily for the benefit of ensuring an expeditious rate design phase.

In view of the above discussed modifications we find the DRA's allegations to be without merit and deny the application for rehearing of D.07-08-030 as modified by this decision.

III. CONCLUSION

For the reasons set forth above, the Commission's Division of Ratepayer Advocates has failed to demonstrate grounds for rehearing of D.07-08-030 as modified herein.

THEREFORE, IT IS ORDERED that:

1. D.07-08-030, as modified by D.07-11-014, is modified as follows:
   a. On page 35, in first full paragraph of the section entitled Commission's Preference for a Conservation Loss Adjustment Mechanism for Los Angeles District, the third sentence is modified to delete the words: "… and will not require continuous litigation of an ROE adjustment."
   b. In first full paragraph on page 37, continuing in the section entitled Commission's Preference for a Conservation Loss Adjustment Mechanism for Los Angeles District, the second sentence is deleted in its entirety.
   c. The first full paragraph on page 61 in the section entitled Comments on the Proposed Alternate Decision is modified to delete the third sentence: "However, if a CLAM can be negotiated, the rate design in Phase 2 is likely to proceed smoothly" and the words "That said," in the fourth sentence are also deleted so that the forth sentence becomes the third sentence and begins with the word "It."
2. The application for rehearing of D.07-08-030 filed by the Commission's Division of Ratepayer Advocates is denied.

This order is effective today.

Dated December 20, 2007, at San Francisco, California.

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