

**BEFORE THE PUBLIC UTILITIES COMMISSION**

**OF THE STATE OF CALIFORNIA**

Application of California-American Water Company (U210W) for Authorization to Increase its Revenues for Water Service by \$34,559,200 or 16.29% in the year 2018, by \$8,478,500 or 3.43% in the year 2019, and by \$7,742,600 or 3.03% in the year 2020.

A.16-07-002  
(Filed July 1, 2016)

**CALIFORNIA-AMERICAN WATER COMPANY'S  
OPENING COMMENTS ON PROPOSED DECISION**

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## Subject Index of Recommended Changes to the Proposed Decision

California-American Water Company (“CAW”) recommends that the California Public Utilities Commission (“CPUC”) make the following changes to the Proposed Decision of Administrative Law Judges Park and Lau, issued November 13, 2018 (“PD”), prior to adoption:

- **Labor Expenses**
  - The CPUC should revise the PD to restore funding for key positions in CAW’s existing workforce by (1) using CAW’s 2016 budgeted labor expense as the base labor figure and (2) escalating the base labor figure using the separate escalation factors for union and non-union labor recommended by CAW to calculate the test year labor expense.
- **Proposed Settlements**
  - The CPUC should revise the PD to instead find that the Monterey Settlement and the San Diego Settlement are reasonable in light of the whole record, consistent with law, and in the public interest; the CPUC should adopt both proposed settlements.
- **Water Customers, Consumption, and System Delivery**
  - The CPUC should revise the PD to find that CAW met public notice requirements and presented substantial evidence regarding its request for a moratorium in the Laguna Seca Subarea; the CPUC should grant CAW’s request for a moratorium or, in the alternative, authorize CAW to seek a moratorium through a publicly noticed advice letter process.
- **Revenues, Rate Design, and Consolidation Issues**
  - The CPUC should revise the PD to find that CAW’s Southern Division Consolidation Proposal as presented in the San Diego Settlement is reasonable and in the public interest; the CPUC should adopt the Southern Division Consolidation Proposal as part of the San Diego Settlement.
- **District Expenses**
  - The CPUC should revise the PD to base transmission and distribution system expenses in the Sacramento District based on the escalated five-year 2011-2015 historical average to account for the likelihood of meter conversion projects in new system acquisitions.
  - The CPUC should revise the PD to expressly account for already-filed purchased water offsets in its forecast of test year purchased water expense.

- The CPUC should revise the PD to adopt CAW’s methodology for chemical expense to provide a more accurate forecast of test year chemical expense.
- The CPUC should revise the PD to include Test Year Monterey Leak Adjustment expenses of \$2.6 million as provided for in the Monterey Settlement; the CPUC should establish the one-way Advanced Metering Infrastructure /Leak Adjustment Balancing Account provided in the Monterey Settlement; the CPUC should include leak adjustment expenses directly in CAW’s revenue requirement rather than unnecessarily delay recovery until Test Year 2024; the CPUC should eliminate the requirement to propose a new leak adjustment policy in light of the already-filed leak adjustment policy guidelines in CAW Advice Letter 1173.
- The CPUC should revise the PD to adopt the revised 7.0% target for the Non-Revenue Water reward/penalty mechanism in the Monterey District; the CPUC should do so though the adoption of the Monterey Settlement.
- **CAW Company Expenses**
  - The CPUC should revise the PD to use the Willis Towers Watson actuarial pension expense projection for 2018 as a basis for the test year pension expense because it takes into account the most up-to-date information.
  - The CPUC should revise the PD to restore group insurance expenses by (1) using the 2017 weighted average (union/non-union) budgeted group insurance expenses as the base group insurance figure and (2) escalate that figure by 7.5%, as recommended by Willis Towers Watson, to calculate the test year group insurance expense.
- **Service Company Expenses and Rate Base**
  - The CPUC should revise the PD to restore funding for key Service Company services by (1) using the 2015 recorded percentage allocation factors to reflect increasing use of direct charging for Service Company expenses to CAW; (2) use the composite escalation factors meant for “contracted services” to escalate in calculation of test year Service Company expenses; and (3) restore funding for business development function expenses, consistent with CPUC and State policy promoting consolidation.
  - The CPUC should revise the PD to allow CAW record the full \$1,869,468 and \$2,243,632 it incurred in 2014 and 2015, respectively, related to information technology expenditures; or, in the alternative, only disallow \$3,064,632 in recognition of the earlier partial

authorization in D.15-04-007 rather than the full amount; and avoid a normalization violation by not reallocating already-completed and booked Business Transformation Project expenses.

- **Taxes**

- The CPUC should revise the PD to allow CAW to continue to implement the 2018 Tax Accounting Memorandum Account to track the impacts of the 2017 Tax Cuts and Jobs Act instead of directing CAW to implement a new and overly burdensome two-way Tax Memorandum Account.
- The CPUC should revise the PD to change the impossible 30-day implementation of the 2018-2020 Excess Protected Accumulated Deferred Income Tax (“ADIT”) balances to separate advice letter filing consistent with when those balances can be determined; the CPUC should revise the PD to add language to ensure protected balances are not returned faster than allowed under the Average Rate Assumption Method; the CPUC should also provide a mechanism to acknowledge the increase in rate base caused by the return of excess ADIT balances.
- The CPUC should revise the PD to eliminate the vague and unnecessarily burdensome requirement for CAW to report any material tax changes via Tier 1 advice letter.
- The CPUC should revise the PD to instead allow CAW to track implementation costs associated with the 2017 Tax Cuts and Jobs Act in a memorandum account.

- **Plant**

- The CPUC should revise the PD to allow CAW to move forward with AMI implementation, giving it the necessary tools to encourage and prioritize efficient water use now, allowing it to further State water policy objectives, and making CAW better equipped to respond to future droughts; in the alternative, the CPUC should modify the PD to allow CAW to recover the costs that it has already expended to develop its AMI proposal.
- The CPUC should revise the PD to grant CAW’s request for additional initial planning dollars for its three proposed recycled water projects, consistent with CPUC and State policy promoting such increased usage of recycled water in support of water conservation.
- The CPUC should revise the PD to put construction costs for the Arden Intertie carryover capital project back into rate base in recognition of the likely completion of the project in 2019.

- The CPUC should revise the PD to grant CAW \$221,846 in 2018 and \$2,118,532 in 2019 to purchase groundwater rights in the Los Angeles District given the scarcity of such opportunities and in recognition of the ratemaking protections that the CPUC would retain over such purchases; in the alternative, the CPUC should allow CAW to seek the costs for such purchase through an advice letter process.
- **Depreciation Expenses**
  - The CPUC should revise the PD to adopt CAW's unopposed forecasted annual depreciation expense of \$23.9 million based upon the 2015 depreciation study completed by Alliance Consulting Group, rather than adopt an outdated depreciation figure based upon the 2010 by the same consultant.
- **Memorandum and Balancing Accounts**
  - The CPUC should revise the PD to clarify that CAW is to prospectively remove double-counted uncollectible costs for the San Clemente Dam Balancing Account in recognition of the fact that CAW historically collected such costs only through a surcharge.
- **Special Requests**
  - The CPUC should revise the PD to further increase the cap on annual recovery of Water Revenue Adjustment Mechanism/Modified Cost Balance Account ("WRAM/MCBA") balances to 17% to eliminate intergenerational inequity and financial harms from lingering regulatory assets; the CPUC should use the \$7.1 million in Excess Unprotected ADIT as a net reduction to the remaining WRAM/MCBA balances that CAW still needs to recover.
- **Other Issues**
  - The CPUC should revise the PD to adjust the compliance deadlines for the filing of particular advice letters as shown in **Appendix A** to account for the fact that many of those timelines are not feasible.
  - The CPUC should revise the Findings of Fact, Conclusions of Law, and Ordering Paragraphs of the PD as shown in **Appendix A**.

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## I. INTRODUCTION

Pursuant to Rule 14.3 of the California Public Utilities Commission's ("CPUC") Rules of Practice and Procedures, Applicant California-American Water Company ("CAW"), submits opening comments on the Proposed Decision of Administrative Law Judges ("ALJs") Park and Lau, issued November 13, 2018 ("PD"). CAW acknowledges the efforts to resolve its General Rate Case ("GRC"). However, the PD contains factual and legal errors that the CPUC should correct.<sup>1</sup> Many of the PD's errors are recurring and, when compounded, significantly undermine CAW's goal of deliver clean, safe, reliable and affordable water and wastewater services and the CPUC's mission to ensure that rates are just and reasonable:

- The PD repeatedly claims that CAW failed to meet its burden of proof or presenting evidence substantiating or justifying its requests, but it often completely ignores such evidence supporting and in the few areas where evidence is mentioned, it is disregarded without a satisfactory explanation of why it was deficient.
- The PD denies CAW's requests in several policy areas that the CPUC has recently encouraged water utilities to make progress, including on recycled water investment, rate consolidation, and implementation of Advanced Metering Infrastructure ("AMI").
- The PD too frequently attempts to shift appropriate rate recovery in this GRC cycle to future recovery, which may suppress rates in the short-term, but deepens generational inequities, presents significant cash flow risks for CAW, and ultimately leads to rate shock for future customers.

Therefore, CAW respectfully requests that the CPUC address these and other issues by making the recommended changes to the PD described below and as shown in **Appendix A**. CAW also includes **Appendix B** addressing issues related to the results generated by CAW's Results of Operations model.

## II. THE PD EFFECTIVELY ELIMINATES EXISTING KEY POSITIONS IN CAW'S WORKFORCE

The PD's adopted 2018 labor expenses significantly underfunds CAW's workforce on payroll, effectively reducing the workforce headcount significantly.<sup>2</sup> The PD would take away funding for multiple existing employees, including long-standing union positions, who provide water quality, conservation, customer service and other critical functions. The PD errs by adopting the proposal by the Office of Ratepayer Advocates ("ORA") (now known as the Public Advocates Office) to escalate the 2015 actual labor expenses by 2.5% annually to forecast the 2018 labor expenses, or \$20,570,668.<sup>3</sup> This figure is unsupported by the evidence because (1) the 2015 recorded labor expenses fails to account for changes in the labor headcount in 2016 and (2) it mistakenly applies the same escalation factor to both union and non-union employees.

### 1. The PD errs by using 2015 recorded labor expenses

The PD use of the recorded 2015 expense is an inappropriate basis for the forecast because it does not reflect the various staff changes and accounting changes that occurred in 2016. The CPUC has previously noted that it "generally accept[s] that use of the best information available is preferred, and total reliance on historical

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<sup>1</sup> CAW is unable to address all of the factual and legal errors in the PD within the 25 page limit allowed for comments in GRCs under Rule 14.3(b). *California-American Water Company's Motion to Increase Page Limits n Comments* (November 26, 2018) would have allowed CAW to full address all of the errors in the 325 page long PD (which is even longer when counting the appendices as well), but the CPUC did not grant CAW's motion. Therefore, CAW's silence on any issue in these comments should not interpreted as its acquiescence on any errors not addressed here.

<sup>2</sup> Exh. CAW-25, Linam Rebuttal, p. 16.

<sup>3</sup> PD, p. 74.

costs will be flawed in at least some areas.”<sup>4</sup> Essentially, by creating a forecast based upon the staffing levels in 2015, the PD develops its labor estimates based on a historical 2015 test year, contrary to the Rate Case Plan.<sup>5</sup>

The PD acknowledges that these staff and accounting changes occurred.<sup>6</sup> However, it inaccurately claims that “there is inadequate record evidence regarding these new and transferred positions.”<sup>7</sup> This is incorrect. CAW presented substantial evidence demonstrating that each of these new and transferred positions is reasonable:

- CAW transferred one employee from the Service Company payroll to the CAW’s payroll.<sup>8</sup> Even though the PD disallows this transfer, it does not make the required corresponding adjustment to the Service Company expense, thereby double-counting this reduction in expenses.
- CAW includes funding for employees added through acquisitions recently approved by the CPUC.<sup>9</sup> The PD’s failure to fund these positions is inconsistent with the prior authorizations of those consolidations.
- The PD approves CAW’s proposed budgets for conservation staffing, including the conversion of four conservation intern positions into full-time positions, but rejects CAW’s proposal to move these employees from the conservation budget (which is funded via surcharge) to the district labor budgets.<sup>10</sup> The CPUC should allow these positions to be recovered in base rates under the district labor budgets.
- CAW provided evidence regarding new positions in the Monterey District for one distribution department crew foreman, two distribution department utility workers, one treatment operator and one administrative assistant,<sup>11</sup> which are necessary to fulfill key operational, safety, and water quality.<sup>12</sup> CAW adjusted its overtime expenses downward since these employees eliminate some overtime needs.<sup>13</sup> While the PD effectively disallows these positions, it errs by then failing to make a corresponding increase to the overtime expenses, which further compounds the disallowance and results a double penalty.

CAW also presented a compensation study by Willis Towers Watson demonstrating that its employees are not overcompensated and instead are slightly below the comparable market medians.<sup>14</sup> The removal of reasonable funding for the positions described above by the PD would further put CAW’s compensation below market medians. The PD’s disallowance of many of CAW’s “at-risk” compensation components further exacerbates this problem.<sup>15</sup>

The PD’s use of the 2015 recorded costs is also inconsistent with the CPUC’s long-standing mandate for CAW to “present a comprehensive, position-by-position description of all district personnel in its future GRCs, including comparisons of authorized versus actual positions and all proposed changes.”<sup>16</sup> Despite this requirement for a position-by-position headcount-oriented approach, the PD does not do the required “comparison of authorized

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<sup>4</sup> D.12-11-051, p. 14.

<sup>5</sup> See D.07-05-062, Appendix A (adopting a *future* test year approach).

<sup>6</sup> PD, p. 73.

<sup>7</sup> *Id.*

<sup>8</sup> Exh. CAW-29, Pray Rebuttal – Public, p. 3.

<sup>9</sup> *Id.*

<sup>10</sup> PD, p. 256.

<sup>11</sup> Exh. CAW-11, Sabolsice Direct, p. 19-21.

<sup>12</sup> See *Opening Brief of California-American Water Company* (June 6, 2017) (“CAW Opening Brief”), pp. 53-54 (summarizing the need for these five Monterey District employees as demonstrated in CAW’s testimony).

<sup>13</sup> Exh. CAW-11, Sabolsice Direct, p. 20; Exh. CAW-10, Pray Direct, pp. 6-7. Consequently, if labor expenses for these positions is denied (they should be granted), a corresponding increase in overtime expenses is required.

<sup>14</sup> Exh. CAW-7, Mustich Direct – Confidential, pp. 6-8, Attachment 1.

<sup>15</sup> PD, pp. 74-76, 80-81 (the PD orders unwarranted reductions to CAW’s annual performance plan, long-term incentive plan and employee stock purchase plan benefits by 50%, 85% and 100%, respectively).

<sup>16</sup> D.09-07-021, p. 156, Ordering Paragraph 21.

versus actual positions” and ignores the “proposed changes” from the earlier 2015 headcount.<sup>17</sup> The record shows that CAW’s total headcount and vacancy rate has remained relatively stable over time, even with more customers, and increasing legal, regulatory, environmental, conservation and policy requirements.<sup>18</sup> Thus, the inclusion of the existing funded positions into expenses fairly allows CAW to recover its actual employee costs while removing vacancies. Therefore, the CPUC should instead use CAW’s 2016 budgeted labor expense as the base labor figure for its calculation of the 2018 labor expense.

## **2. The PD’s errs by conflating union and non-union labor escalation factors**

The PD adopts “ORA’s use of 2.5% to annually escalate the 2015 actual expenses to the 2018 forecast,”<sup>19</sup> which the PD asserts is “consistent the 2.5% escalation factor that the 2015 GRC decision adopted for all employees.”<sup>20</sup> This result improperly conflates union and non-union compensation attributes, which significantly underestimates the required 2018 non-union labor expenses. As a preliminary point, the PD fails to acknowledge that the 2.5% escalation factor utilized in CAW’s 2015 GRC was determined through a settlement agreement<sup>21</sup> and therefore affords no precedential value.<sup>22</sup> To the extent that the PD finds the earlier settlement relevant, the CPUC should keep in mind that both CAW **and** ORA in the 2015 GRC had recommended **separate** escalation factors for union and non-union employees – the final 2.5% factor utilized was a negotiated compromise.<sup>23</sup>

The PD’s uniform 2.5% escalation factor is contradicted by evidence regarding the different compensation aspects of union and non-union employees.<sup>24</sup> For example, the union employees may have opportunities for certification pay or overtime, which are not available to non-union employees.<sup>25</sup> Therefore, while the salary escalation for union employees may be lower, these employees may have the opportunities to earn more in other ways.<sup>26</sup> These options are not available to non-union employees; thus, to stay competitive, non-union salaries must escalate at a higher rate. Indeed, the PD recognizes that “union positions and management positions have different incentive mechanisms.”<sup>27</sup> At minimum the PD errs by failing to explain why the substantial evidence presented regarding these differences in union and non-union compensation mechanisms is insufficient. The CPUC should instead adopt the separate escalation factors recommended by CAW.

### **III. PROPOSED SETTLEMENTS**

#### **A. The PD errs in rejecting the two proposed settlement agreements**

Under Rule 12.1(d), settlements, whether contested or uncontested, must be “reasonable in light of the

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<sup>17</sup> *Id.*

<sup>18</sup> Exh. CAW-28, Pray Rebuttal – Confidential, p. 4, Confidential Attachment 3.

<sup>19</sup> PD, p. 74.

<sup>20</sup> *Id.*, p. 72.

<sup>21</sup> D.15-04-007, Attachment A, p. 55.

<sup>22</sup> Rule 12.5.

<sup>23</sup> D.15-04-007, Attachment A, p. 55 (ORA’s “projection was based on 80 corporate and 210 district employees, and reflecting actual wage rates for 2012 and using a 2.1% inflation factor for 2013 and then using a 1.5% inflation factor for 2014 and 2015 for the non-union employees and 2.25% and 1.5% increases for the union employees for 2014 and 2015.”).

<sup>24</sup> Exh. CAW-29, Pray Rebuttal – Public, p. 5.

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*

<sup>27</sup> PD, p. 74.

whole record, consistent with law, and in the public interest.” The parties to the Monterey Settlement<sup>28</sup> and the San Diego Settlement<sup>29</sup> have demonstrated that the agreements meet this standard.<sup>30</sup> CAW is therefore troubled by the PD’s rejection of both of the proposed settlement agreements its insistence the agreements do not represent the affected interests or reflect fair compromises.<sup>31</sup>

For example, the PD claims that the Monterey Settlement, signed by the Monterey Peninsula Water Management District (“MPWMD”) and the Los Palmas Wastewater Committee (“LPWC”) is not fairly representative of affected interests.<sup>32</sup> As MPWMD has explained, it is a directly elected agency charged with integrated management of water resources in Carmel, Monterey, Pacific Grove, Seaside, Del Rey Oaks, Sand City, and unincorporated areas of Monterey County.<sup>33</sup> The LPWC represents the interests of active wastewater customers of CAW. Combined, these two entities represent water and wastewater interests in CAW’s Monterey District. The PD’s claim that these two entities do not represent ratepayer interests belittles the efforts made by these parties.

The PD also states that neither settlement agreements represent a reasonable compromise by the parties.<sup>34</sup> In particular, the PD finds fault with the fact that the settlement agreements cover issues that were not litigated by all of the settling parties.<sup>35</sup> The CPUC has never limited reasonable compromise to litigated positions, however, and has specifically mentioned considering the more general “interests” of the settling parties.<sup>36</sup> The PD inappropriately and unjustifiably narrows the applicability of a reasonable compromise in a way that could discourage settlements and unfairly limit the ability of intervenors to participate in CPUC proceedings.

The CPUC recently held several workshops to improve accessibility of CPUC proceedings,<sup>37</sup> recognizing that the CPUC’s processes can make participation challenging.<sup>38</sup> Intervenors may not have the ability to litigate every issue that affects their constituents or members. For such parties, preparing testimony and presenting witnesses may be cost-prohibitive, and participating in settlement discussions may be the best way to deploy their limited resources. The PD’s dismissal of the settlement agreements devalues the participation of such parties.

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<sup>28</sup> *Joint Motion for Adoption of a Partial Settlement Agreement between California-American Water Company, Las Palmas Wastewater Committee, and Monterey Peninsula Water Management District, on Monterey Issues in the General Rate Case* (June 12, 2017), Exhibit A (“Monterey Settlement”).

<sup>29</sup> *Joint Motion for adoption of a Partial Settlement Agreement between California-American Water Company and the City of Coronado on San Diego Issues in the General Rate Case* (August 18, 2018), Exhibit A (“San Diego Settlement”).

<sup>30</sup> *Reply Comments in Support of Motion for Adoption of a Partial Settlement Agreement between California-American Water Company, Las Palmas Wastewater Committee, and Monterey Peninsula Water Management District, on Monterey Issues in the General Rate Case* (July 27, 2017), pp. 2-4; *Reply Comments in Support of Motion for Adoption of a Partial Settlement Agreement Between California-American Water Company and the City of Coronado on San Diego Issues in the General Rate Case* (October 3, 2017) (“CAW San Diego Settlement Reply”), pp. 2-5.

<sup>31</sup> PD, pp. 15, 17-18.

<sup>32</sup> *Id.*, p. 15.

<sup>33</sup> *Motion of the Monterey Peninsula Water Management District for Party Status* (July 29, 2016), p. 2.

<sup>34</sup> PD, pp. 15, 18.

<sup>35</sup> PD, p. 15.

<sup>36</sup> D.07-03-044, p. 259, cited by the PD, p. 15.

<sup>37</sup> See, e.g., CPUC Committee on Policy and Governance, *Report from Policy and Governance Committee Workshops to Improve the Accessibility of CPUC Proceedings* (November 28, 2018).

<sup>38</sup> CPUC Committee on Policy and Governance, *Agenda for Workshop to Address the Accessibility of CPUC Proceedings* (November 7, 2018), p. 2.

The PD's "cherry-picking" of the settlement agreements also concerns CAW. The CPUC is required "to evaluate a settlement **as a whole**."<sup>39</sup> As part of the settlement process, the parties compromise on certain issues in order to achieve benefits regarding other issues. This back and forth is why both of the settlement agreements in this proceeding (and most CPUC settlement agreements generally), state that the parties are agreeing to the settlement agreements as integrated packages, and as opposed to agreeing to specific elements.<sup>40</sup>

The PD, however, despite rejecting the settlement agreements, adopts certain specific compromise positions. For example, CAW and MPWMD reached a compromise on the non-revenue water ("NRW") level for the Monterey District. The PD adopts this compromise position as the upper threshold above which a penalty calculation will be determined.<sup>41</sup> In doing so, the PD undermines the settlement, since the NRW position may also reflect other compromises that were not adopted. If the CPUC adopts this cherry-picking it will create disincentive for parties to participate in settlement negotiations, due to the fear that a final decision may adopt a concession without the corresponding negotiated benefit.

#### **IV. WATER CUSTOMERS, CONSUMPTION, AND SYSTEM DELIVERY**

##### **A. The PD improperly denies CAW's moratorium in the Laguna Seca Subarea**

The PD erroneously suggests that CAW failed to provide adequate public notice of its request to implement a moratorium on new connections for the Laguna Seca Subarea.<sup>42</sup> CAW provided notice of its GRC to its customers and the public in compliance with CPUC Rule 3.2.<sup>43</sup> The PD asserts additional notice is necessary because the "proposed moratorium is not a proposal that merely affects rates but in this specific instance, potentially affects property interests."<sup>44</sup> There is no precedent or basis for requiring of notice above and beyond what is required in Rule 3.2 for a proposal that "potentially affects property interests." Should the CPUC decide to change the requirements for public notice for GRCs, it should do so prospectively on a CPUC-wide basis.

The PD also erroneously finds that CAW does not present sufficient evidence supporting the moratorium,<sup>45</sup> disregarding the substantial evidence presented in this proceeding that a moratorium is necessary. The moratorium is now ripe for consideration by the CPUC because the amount of water allocated to the Laguna Seca Subarea by the Seaside Groundwater Basin Adjudication is insufficient.<sup>46</sup> The operating yield for the Laguna Seca Subarea systems was to be reduced to 0.00 acre feet ("AF") and MPWMD recently approved its Quarterly Water Budget with a target of zero AF for the Laguna Seca Subarea.<sup>47</sup> General Order 103-A requires a utility to request a service

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<sup>39</sup> D.07-03-044, p. 258 (emphasis added).

<sup>40</sup> See, e.g., Monterey Settlement, p. 2 ("the Settlement Agreement is being presented as an integrated package...").

<sup>41</sup> PD, p. 60.

<sup>42</sup> *Id.*, pp. 23-24.

<sup>43</sup> See *California-American Water Company's Comments Regarding Notice of Laguna Seca Subarea Moratorium* (March 20, 2018), p. 3.

<sup>44</sup> PD, p. 23.

<sup>45</sup> *Id.*, p. 24.

<sup>46</sup> Exh. CAW-11, Sabolsice Direct, pp. 8-11. The PD also conflates the term "water shortage emergency" under Water Code §§ 350 *et seq.* (which is not applicable here) versus the shortage in the amount of water that is **allotted** to CAW here under the Seaside Basin Adjudication. PD, p. 24.

<sup>47</sup> Exh. CAW-11, Sabolsice Direct, p. 10; *California-American Water Company's Comments Regarding Notice of Laguna Seca*

connection moratorium where a system does not have the source capacity required by the Waterworks Standards.<sup>48</sup> While CAW's system has the physical capacity to provide the necessary amount of water, the amount of water legally allotted is insufficient.<sup>49</sup> The PD also inexplicably finds since CAW has already been forced to operate in excess of the available operating yield, "it is unclear that a moratorium is strictly necessary."<sup>50</sup> The PD argues that CAW can continue to replenish the excess production either through payment of a replenishment assessment to the Watermaster or through the importation of non-native water to the Seaside Basin.<sup>51</sup> The replenishment assessments are meant to be an enforcement mechanism to ensure that producers in the basin (including CAW) work to bring the amount of groundwater drawn to within safe operating yields. The PD's suggestion to use such replenishment assessments to support new service connections is contrary to the objectives of the Seaside Basin Adjudication.<sup>52</sup> Therefore, the CPUC should revise the PD to find that CAW has met the notice requirements and that a moratorium is necessary. The CPUC should grant CAW's request for a moratorium or, in the alternative, allow for CAW to seek a moratorium through a publically noticed advice letter process.

**V. REVENUES, RATE DESIGN, AND CONSOLIDATION ISSUES**

**A. The PD errs by failing to evaluate the settlement Southern Division consolidation proposal**

The PD denies CAW's proposal to consolidate its Southern Division and rejects CAW's proposed rate design for the consolidated Southern Division.<sup>53</sup> The principal error in the PD is that it continues to evaluate the original Southern Division consolidation proposal in CAW's original Application ("Original Southern Consolidation Proposal") rather than the Southern Division consolidation proposal presented in the San Diego Settlement ("Settlement Southern Consolidation Proposal").

CAW entered into the San Diego Settlement after extensive negotiations with each of the parties in this proceeding. In re-crafting its consolidation proposal for the Southern Division with Coronado, CAW also took into account each of the concerns raised by parties who were not ultimately part of the San Diego Settlement.<sup>54</sup> As a result, under the Settlement Southern Consolidation Proposal, the average proposed customer bill is lower than the average proposed customer bill under stand-alone ratemaking in *all* districts:<sup>55</sup>

District	Average Proposed Bill Standalone Application <i>Without</i> Consolidation	Average Proposed Bill Under <i>Original</i> Southern Consolidation Proposal	Average Proposed Bill Under <i>Settlement</i> Southern Consolidation Proposal
Ventura	\$113.81	\$126.74	\$110.79
San Diego	\$67.83	\$61.88	\$66.34
Baldwin Hills	\$83.23	\$64.24	\$74.64

*Subarea Moratorium* (March 20, 2018), p. 2.

<sup>48</sup> General Order 103-A § II.2.B.(3).a, p. 11. See also Pub. Util. Code § 2708.

<sup>49</sup> Exh. CAW-11, Sabolsice Direct, p. 10.

<sup>50</sup> PD, p. 24.

<sup>51</sup> *Id.*

<sup>52</sup> *California American Water vs. City of Seaside*, Case No. M66343 (Monterey County Superior Court March 27, 2006).

<sup>53</sup> PD, p. 35.

<sup>54</sup> Each of ORA's and CTO's concerns regarding Original Southern Consolidation Proposal were addressed as shown in Attachments 1 and 2, respectively of the CAW San Diego Settlement Reply; see also *id.*, pp. 5-16 (explaining the manner in which the San Diego Settlement addresses all of the stated concerns of ORA and CTO regarding consolidation).

<sup>55</sup> The below table presents some of the information included in Table 2 of the CAW San Diego Settlement Reply, p. 12.

Duarte	\$78.01	\$72.25	\$75.74
San Marino	\$86.68	\$85.07	\$83.80

The PD claims that CAW “does not address the specific facts and circumstances for its Southern Division.”<sup>56</sup> After making the appropriate revisions to the earlier proposal, the Settlement Southern Consolidation Proposal builds upon CAW’s earlier testimony regarding consolidation<sup>57</sup> and additionally is specifically tailored to address the particular facts and circumstances in the Southern Division, including the issues raised identified in D.14-10-047: proximity, rate comparability, water supply, or operation of the districts.<sup>58</sup> It addresses the concerns of ORA in setting the tier 2 rate at 100% of the Standard Quantity Rate and modifies tiers 3 and 4 accordingly. CAW also presented the public interest benefits of the Settlement Southern Consolidation Proposal with respect to promoting water conservation.<sup>59</sup>

The PD notes that “[t]here are significant differences in water supply for the three districts in the Southern Division.”<sup>60</sup> Consequently, the PD concludes that “the Ventura and San Diego Districts are unlikely to ever benefit from the pooling of plant and infrastructure costs” because those districts would retain their variable costs, including the imported water costs.<sup>61</sup> That simply is not true. The Settlement Southern Consolidation Proposal is designed to try to mitigate the effects of immediate full rate consolidation during this GRC period because of the rate shock that would occur on the revenue requirements in the Los Angeles districts.<sup>62</sup> Instead, CAW recommends a stepwise approach towards achieving full consolidation over at least two GRC cycles in order to allow a more gradual transition that provides customers an opportunity to adjust to new price signals driven by both the revenue increase and modified rate design.<sup>63</sup> Accordingly, CAW has agreed under the San Diego Settlement to propose full consolidation in its next GRC, which at a minimum includes “full consolidation of all costs for ratemaking purposes in the Southern Division.”<sup>64</sup> Full consolidation is consistent with CPUC policy and will ultimately benefit CAW’s customers.<sup>65</sup> Addressing the concern raised in the PD, full consolidation will permit purchased water costs, which are particularly high in the Ventura District, to ultimately be spread among all the customers in Southern California.<sup>66</sup>

The PD also asserts that Ventura District customers would be worse off under a consolidation of the Southern Division as compared to without it.<sup>67</sup> The PD consequently finds that the Original Southern Consolidation Proposal “would result in Ventura District customers subsidizing customers of other districts and we do not find this

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<sup>56</sup> PD, p. 31.

<sup>57</sup> Exh. CAW-2, Chew Direct, pp. 27-35.

<sup>58</sup> D.14-10-047, p. 17, Finding of Fact 4.

<sup>59</sup> San Diego Settlement, p. 7; see also Exh. CAW-33, Stephenson Rebuttal - Public, p. 51.

<sup>60</sup> PD, p. 31.

<sup>61</sup> *Id.*, p. 32.

<sup>62</sup> San Diego Settlement, p. 7.

<sup>63</sup> Exh. CAW-2, Chew Direct, p. 35.

<sup>64</sup> San Diego Settlement, p. 10.

<sup>65</sup> See CAW San Diego Settlement Reply, pp. 7-8.

<sup>66</sup> Exh. CAW-33, Stephenson Rebuttal - Public, pp. 58-59

<sup>67</sup> PD, pp. 32-33.

subsidization to be justified.”<sup>68</sup> However, under the Settlement Southern Consolidation Proposal instead, the average Ventura District customer would see bill of \$110.79 as compared to an average bill of \$113.81 under the existing unconsolidated arrangement.<sup>69</sup> Consequently, CAW’s Ventura customers would have a higher average bill under the CTO position (*i.e.*, no consolidation) than under CAW’s Settlement Southern Consolidation Proposal.

Additionally, the public input from customers and representatives opposing the consolidation cited by the PD was taken in the early stages of this proceeding<sup>70</sup> and is unlikely to reflect the position of customers on the later Settlement Southern Consolidation Proposal (which was filed on August 18, 2017).<sup>71</sup> The CPUC should adopt the Settlement Southern Consolidation Proposal as part of the San Diego Settlement and authorize CAW to implement the proposed rate design provided for therein.

## VI. DISTRICT EXPENSES

### A. The PD’s forecast overlooks meter conversion projects in newly acquired systems

The PD properly rejects the blanket approach proposed by ORA for forecasting all O&M expenses and does not find justification for ORA’s recommendation to remove alleged “outlier years” from test year forecasts.<sup>72</sup> However, the PD adopts ORA’s recommendations for the “Misc. Maint. – Transmission & Distribution – Service” expense line item.<sup>73</sup> The PD asserts that CAW had “charged expenses for completing a conversion from flat rate to metered service to this line item in 2011 and 2012” and that “[t]here are no such conversions planned for this GRC cycle.”<sup>74</sup> However, the data request cited by the PD<sup>75</sup> explained, “Recent and anticipated acquisitions will cause the spend trend upward as CAW begins operations of these systems.”<sup>76</sup> Indeed, the CPUC has recently approved acquisitions for CAW that will require conversions from flat rate to metered service.<sup>77</sup> Water Code Section 527(a)(1) requires that urban water utilities like CAW to meter all municipal users by the year 2025. Therefore, the CPUC should use the escalated five-year 2011-2015 historical average as the basis for the test year forecast.

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<sup>68</sup> *Id.*, p. 35.

<sup>69</sup> *Motion of the City of Thousand Oaks to Set Aside Submission and Reopen the Record to Admit Discovery Responses of California-American Water Company as Exhibits CTO-16 and CTO-17* (September 14, 2017), Attachment B (CAW Response to Data Request 6, Question 3).

<sup>70</sup> CAW reviewed the correspondence formal file at the CPUC finding only 55 emails, letters, or calls on record, considerably less than the “over 800 letters, e-mails, and calls regarding the application” cited by the PD on page 4. CAW made a further data request to the Public Advisors Office to see if there are additional communications in its possession that are not yet in the correspondence formal file.

<sup>71</sup> PD, p. 8; *Joint Motion for Adoption of a Partial Settlement Agreement Between California-American Water Company and the City of Coronado on San Diego Issues in the General Rate Case* (August 18, 2017).

<sup>72</sup> PD, pp. 40-42.

<sup>73</sup> *Id.*, p. 42.

<sup>74</sup> *Id.*

<sup>75</sup> *Id.*, p. 42 fn.110 (citing “Exh. ORA-6, Attachment 3.”).

<sup>76</sup> Exh. ORA-6, Attachment 3, p. 40.

<sup>77</sup> See, e.g., D.15-11-012, p. 3 (“Dunnigan is a Class D public utility water company regulated by the California Public Utilities Commission (Commission), and provides drinking water and wastewater services to approximately 253 **non-metered** residential service connections...” (emphasis added); D.16-11-014, p. 2 (“[Geyserville Water Works]’s system is located in Sonoma County and consists of 318 service connections (279 metered and the remainder receiving **flat-rate service**.”) (emphasis added). CAW also has a currently pending application to acquire Fruitridge Vista Water Company, which, if authorized, will require the conversion of more than 3,000 unmetered connections to meters. See A.17-10-016, *Application for Order Authorizing Sale and Purchase of Utility Assets*, pp. 8-9, 17-18.

**B. The PD should take into account already implemented purchased water offsets**

The PD reviews CAW's purchased water forecasts for the test year and properly finds those requests to be reasonable with certain modifications for particular updated purchased water unit prices described therein.<sup>78</sup> While CAW supports the reasoning underlying these findings, the PD should also take into account several advice letters for purchased water offsets that CAW has already filed.<sup>79</sup> Each of these advice letters requested authority to offset costs resulting from increased charges for water that CAW purchases for certain service areas and some have already been approved and implemented.<sup>80</sup> Therefore, CPUC should ensure that the updated purchased water unit price information contained in these advice letters is accounted for in new base rates.

**C. The PD errs by adopting ORA's forecast for chemical expenses**

The PD errs by adopting ORA's methodology for forecasting CAW's chemical expenses in its water districts for test year 2018 over CAW's methodology.<sup>81</sup> CAW presented a superior granular chemical-by-chemical need analysis that better captures the evolution of regulatory standards and operational requirements in the recorded chemical expenses data.<sup>82</sup> The PD's error is caused by a misinterpretation of CAW's methodology.

The PD asserts that CAW "does not point to any line items in its chemicals expenses forecast where a one-year or two-year average would be appropriate based on new regulatory standards or operational requirements."<sup>83</sup> This critique is misplaced. One-year and two-year averages are not the primary way that CAW's methodology reflects new regulatory standards or operational requirements.<sup>84</sup> Rather, by beginning with the separate individual line items for historical chemical expenses, CAW is able to follow the trend in how much of a certain chemical (down to the size used) was historically used over the 2013-2015 period.<sup>85</sup> This is important because costs for different line items changed on a non-uniform basis to meet new regulatory standards or operational requirements.<sup>86</sup> CAW's methodology used this nuanced approach to forecast each line item separately before combining it to calculate the overall forecasted test year chemical expenses.

Having overlooked the value in CAW's methodology, the PD instead focuses on apparent overstatements of certain chemicals for which one-year or two-year averages were utilized.<sup>87</sup> CAW reviewed its calculations and

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<sup>78</sup> PD, pp. 45-47.

<sup>79</sup> See, e.g., Advice Letter 1212 (August 1, 2018) (purchased water offset for San Diego District), Advice Letter 1215 (October 25, 2018) (purchased water offset for Ventura District), Advice Letter 1216 (October 25, 2018) (purchased water offset for Larkfield District); Advice Letter 1217 (November 2, 2018) (purchased water offsets for Baldwin Hills, Duarte, and San Marino service areas).

<sup>80</sup> See, e.g., Advice Letter 1212 (August 1, 2018), p. 1 ("California American Water is seeking authority to offset purchased water expenses it incurs from the City of San Diego, the water supplier for its San Diego County District. The City of San Diego increased its wholesale rates to California American Water effective August 1, 2018. California American Water requests that the full increase be offset to account for the annual change in purchased water costs.").

<sup>81</sup> PD, pp. 47-49.

<sup>82</sup> *Id.*, p. 47.

<sup>83</sup> *Id.*, pp. 48-49.

<sup>84</sup> The inclusion of one-year or two-year averages in CAW's workpapers for a small number of line items occurs as CAW began the use of new sizes of particular chemicals or entirely new chemicals during the 2013-2015 timeframe.

<sup>85</sup> See RO Model "ALL\_CH04\_O&M\_WP\_Chemical.xlsx", tab WS-1, *cited by* Exh. ORA-4, Wei Testimony, p. 22 fn.47.

<sup>86</sup> See RO Model "ALL\_CH04\_O&M\_WP\_Chemical.xlsx", tab WS-2, *cited by* Exh. ORA-4, Wei Testimony, p. 22 fn.47.

<sup>87</sup> PD, p. 48.

found only three instances where an overstatement occurred.<sup>88</sup> The instances were shown not to impact the forecasted expense at all or only by *de minimis* amounts.<sup>89</sup> The increased accuracy gained by CAW's granular forecast outweighs the three negligible instances described above and is a reasonable estimate of test year chemical expenses. The CPUC should adopt CAW's methodology for its chemical expenses forecast.

#### **D. The PD ignores substantial evidence regarding leak adjustments**

The PD erroneously finds that CAW "failed to demonstrate the reasonableness of its leak adjustment practices or recorded leak adjustments in its Monterey District."<sup>90</sup> These findings are erroneous because they ignore substantial evidence that CAW presented substantiating its recorded leak adjustment expenses.

CAW presented three witnesses who discussed the leak adjustment program at length, with particular emphasis on the implementation of the program in the Monterey District including the need for the program in Monterey in particular,<sup>91</sup> the customer service center perspective,<sup>92</sup> and CAW's verification of leak adjustment cases to demonstrate that there was no abuse of the system,<sup>93</sup> which included 300 actual customer bills for leaks during 2013 and 2014.<sup>94</sup> Together these witnesses presented substantial evidence regarding the leak adjustment program in the Monterey District, demonstrating that both the program and the amounts recorded were reasonable.

The PD does not immediately authorize any leak adjustment expenses in CAW's current revenue requirement, but instead establishes a Monterey District leak adjustment balancing account with an annual budget of \$2,370,879, based upon the average recorded leak adjustment expenses over the five-year period between 2011 and 2015.<sup>95</sup> First, the five-year average is inappropriate because the rate design for this district changed significantly in late 2013,<sup>96</sup> making a two-year average of 2014-2015 superior. While the CPUC did make further changes to the Monterey District rate design in D.16-12-003, once new rates are adopted in this GRC, the top tier rates in this GRC period will be very similar to the top tier rates in the historical periods used for forecasting.<sup>97</sup> Second, by removing these expenses from base rates and waiting to review these expenses in the next GRC, the PD unnecessarily pushes out recovery of these costs for at least six years (Test Year 2024), causing significant cash flow issues and intergenerational inequities. There is no reason why the CPUC cannot simply provide for leak adjustment expenses in base rates now and direct CAW to maintain a balancing account to protect customers. The CPUC should authorize the Test Year Monterey Leak Adjustment expenses of \$2.6 million directly in CAW's revenue requirement pursuant to the Monterey Settlement.<sup>98</sup> The CPUC should also establish the one-way AMI/Leak Adjustment Balancing Account in the Monterey Settlement to track differences between the level of

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<sup>88</sup> CAW-29, Pray Rebuttal – Public, p. 27.

<sup>89</sup> *Id.*, pp. 27-28.

<sup>90</sup> PD, p. 53.

<sup>91</sup> Exh. CAW-30, Sabolsice Rebuttal, pp. 9-20.

<sup>92</sup> Exh. CAW-34, Teasley/Pallas Rebuttal, pp. 3-14.

<sup>93</sup> Exh. CAW-32, Stephenson Rebuttal – Confidential, pp. 24-27; Attachments 1-4.

<sup>94</sup> *Id.*, Attachment 3.

<sup>95</sup> PD, pp. 56-57.

<sup>96</sup> *Id.*, p. 50; Exh. CAW-10, Pray Direct, pp. 26-27.

<sup>97</sup> Exh. CAW-32, Stephenson Rebuttal – Confidential, pp. 32-33.

<sup>98</sup> *Id.*, p.4; Exh. CAW-5, Linam Direct, p. 31; Monterey Settlement, p. 15.

proposed leak adjustments authorized and actual costs incurred.<sup>99</sup>

Additionally, the PD directs CAW to “propose a leak adjustment policy for its Monterey District in its next GRC.”<sup>100</sup> CAW previously filed its Advice Letter 1173 to “assist customers in requesting a loss of water adjustment and to standardize the process and documentation for all customers,” as well as to “provide further clarification on our guidelines applicable to all districts,”<sup>101</sup> The supporting documentation for Advice Letter 1173 included a summary of the guidelines for CAW’s implementation of its leak adjustment program.<sup>102</sup> The CPUC reviewed and approved Advice Letter 1173 on September 7, 2017.<sup>103</sup> Because the CPUC has already reviewed and approved the leak adjustment program guidelines in Advice Letter 1173, which demonstrates CAW’s stringent and effective policies in place to address the concerns raise in the PD, the requirement to propose a leak adjustment policy in the next GRC is moot and should be removed.

**E. The PD’s NRW reward/penalty mechanism is unsupported by any evidence**

The PD revises CAW’s NRW reward/penalty mechanism in the Monterey District by first cherry-picking the 7.0% of total water production figure agreed upon in the Monterey Settlement, then establishing deadband between 5.0% and 7.0%, inclusive, for which NRW results will neither accrue a penalty nor earn a reward.<sup>104</sup> As explained above, the CPUC should respect the Monterey Settlement as a wholly integrated and thoroughly negotiated compromise – it should not pick and choose elements of that agreement to adopt. Moreover, the PD essentially creates a whole new record, without the input of any party, to establish a complex sharing mechanism featuring a deadband with numbers not in evidence. Therefore, the CPUC should reject this revision of CAW’s NRW reward/penalty mechanism because it is not supported by “substantial evidence in light of the whole record” and consequently cannot be sustained as a matter of law.<sup>105</sup> Instead, the CPUC should adopt the revisions to the NRW reward/penalty mechanism as part of the complete Monterey Settlement.<sup>106</sup>

**VII. OTHER CAW COMPANY EXPENSES**

**A. The PD’s pension expense forecast deviates from CPUC practice**

The PD determines the 2018 pension plan expense by averaging CAW’s 2013-2015 recorded costs, or \$1,740,148, and then escalating this average to 2018 dollars using the 2016 and 2017 escalation factors, approving a 2018 pension plan expense of \$1,799,788.<sup>107</sup> This methodology is erroneous because it completely disregards the results of an actuarial analysis completed by CAW’s actuary Willis Towers Watson, which CAW and ORA *both* recommend using (albeit with projections for different years).<sup>108</sup> In doing so, the PD deviates from the CPUC’s prior

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<sup>99</sup> Monterey Settlement, pp. 13-14.

<sup>100</sup> PD, p. 317, Ordering Paragraph 14.

<sup>101</sup> Advice Letter 1173 (July 27, 2017), p. 2, Supporting Workpapers 2-1 to 2-4.

<sup>102</sup> See *id*

<sup>103</sup> See Letter from Jennifer Perez (Division of Water and Audits - Water & Sewer Advisory Branch) to Jeffrey T. Linam (CAW) (September 7, 2017) (approving CAW Advice Letter 1173).

<sup>104</sup> PD, p. 60.

<sup>105</sup> See Pub. Util. Code § 1757(a)(4).

<sup>106</sup> Monterey Settlement, pp. 15-16.

<sup>107</sup> *Id.*, p. 80.

<sup>108</sup> *Id.*

practice on this issue without a satisfactory explanation. The CPUC previously relied upon the actuarial analysis from CAW's actuary to determine pension expense in D.12-06-016.<sup>109</sup> Rather than utilize the expert actuarial analysis of Willis Towers Watson, the PD inexplicably instead creates its own calculation of pension expenses that was never proposed by any party nor supported by any actual evidence.

Instead, both CAW and ORA agree that using actuarial projections provides a reasonable method to forecast the test year 2018 pension expense budget.<sup>110</sup> ORA recommends using CAW's 2016 actuarial expense projection by Willis Towers Watson and escalating to 2018.<sup>111</sup> CAW recommends using the most recent available data, which in this case is the actuarial projection for 2018 completed by the same consultant.<sup>112</sup> There is no reason to use a 2016 actuarial projection, escalated forward, when a 2018 projection completed by the same consultant is available. In D.12-06-016, the CPUC based rates on the **updated** actuarial projection because it included more recent information about the financial markets.<sup>113</sup> Therefore, the CPUC should adopt CAW's forecasted test year pension expense of \$2,085,650 based upon the 2018 actuarial projection completed by Willis Towers Watson.

#### **B. The PD's group insurance expenses analysis ignores substantial evidence**

The PD calculates CAW's group insurance costs by first approximating CAW's 2016 cost with its 2015 recorded costs and then inflating that figure by escalation factors for 2017 and 2018 it derived by taking the average of CAW and ORA's escalation estimates.<sup>114</sup> As explained below, this methodology leads to an inaccurate forecast of CAW's group insurance expenses because it ignores substantial evidence presented in this proceeding.

##### **1. The PD's use of 2015 recorded costs does not account for current employees**

The PD calculates CAW's group insurance expenses by first approximating the 2016 expenses using the 2015 recorded costs, and then escalating that figure to the 2018 test year.<sup>115</sup> However, the 2015 recorded costs do not account for the insurance costs of new positions that were added in 2016.<sup>116</sup> The PD asserts that this discrepancy is irrelevant because it does not approve the addition of those positions into the payroll expenses.<sup>117</sup> As explained in Section II above, these are current employees who have been on CAW's payroll, serve vital roles in CAW's operations and whose positions therefore should be authorized. Accordingly, the 2017 budgeted group insurance expense should be used.

Even if the CPUC decides not to include those current employees into the payroll expense (although it should), the use of the 2017 budget is more likely to be accurate because it only needs to be escalated for **one** year to calculate the forecasted 2018 test year expense. In contrast, the PD's more roundabout approach requires the CPUC to first assume that the 2015 recorded costs will approximate the 2016 expense based upon parent company

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<sup>109</sup> D.12-06-016, p. 57.

<sup>110</sup> PD, p. 79.

<sup>111</sup> *Id.*

<sup>112</sup> *Id.*

<sup>113</sup> D.12-06-016, p. 57.

<sup>114</sup> PD, pp. 83-84.

<sup>115</sup> *Id.*, p. 83.

<sup>116</sup> CAW-29, Pray Rebuttal – Public, p. 7.

<sup>117</sup> PD, p. 83.

information, and then escalate that figure **two** years to reach the 2018 test year. Consequently, any purported benefit of utilizing recorded costs over budgets forecasted by expert consultants is muted by the increased reliance on the accuracy of the annual insurance escalation factors, which can be highly variable and subject to many external factors. In fact, the PD itself references “the significant variability and volatility in insurance costs” in addressing the relevant escalation factors.<sup>118</sup> Therefore, the CPUC should instead use CAW’s 2017 weighted average (union/non-union) budget for group insurance expenses and escalate that figure to 2018.

## 2. The PD’s escalation factor for group insurance expenses is unsupported

The PD reviewed group insurance escalation factors proposed by CAW and ORA.<sup>119</sup> The PD finds that neither proposal is more persuasive than the other and instead adopts the average of ORA’s and CAW’s escalation estimates for each year.<sup>120</sup> This approach is unsupported because it ignores substantial evidence demonstrating that CAW’s proposed escalation factor is specifically tailored to CAW’s circumstances and therefore is more likely to produce accurate results than ORA’s recommended escalation factor. CAW’s expert consultant Willis Towers Watson developed its projected increase in health insurance costs by focusing on insurance plans that are similar to American Water’s.<sup>121</sup> Using survey data from more than 600 employers, Willis Towers Watson determined that the escalation rate is approximately 6%.<sup>122</sup> Willis Towers Watson then added 1.5% added to reflect expected significant prescription drug trend over the next several years<sup>123</sup> to reach the 7.5% factor that CAW used in developing its new test year 2018 group insurance estimate. In contrast, ORA uses inflation factors from IHG Global Insight that are not tied to the specifics of the American Water plan, but are instead more general inflation factors typically used to determine **non-labor and wage** escalation rates.<sup>124</sup> The CPUC recently found that relying on the IHS escalation rates “will tend to underestimate the cost of medical benefits.”<sup>125</sup> At minimum, the PD errs by failing to explain why CAW’s proposed escalation factor is not more accurate than ORA’s estimate in light of the evidence.

Instead, the PD cites to the fact that “ORA’s and CAW’s 2016 escalation forecasts are significantly different from the actual escalation rate American Water experienced in 2016.”<sup>126</sup> This is an unreasonable, if not impossible bar to meet. The PD itself recognizes the challenges associated with forecasting expenses, particularly with respect to insurance costs.<sup>127</sup> It is irrational to point to a specific instance where a forecast was incorrect as evidence that it cannot be relied upon. Rather than arbitrarily taking the average of CAW and ORA’s positions, the CPUC should instead use the best information available: the escalation factor recommended by Willis Towers Watson. Therefore,

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<sup>118</sup> *Id.*, p. 84.

<sup>119</sup> *Id.*

<sup>120</sup> *Id.*

<sup>121</sup> Exh. CAW-36, Willig Rebuttal, p. 3.

<sup>122</sup> *Id.*, pp. 2-3

<sup>123</sup> *Id.*, p. 6.

<sup>124</sup> Exh. CAW-25, Linam Rebuttal, p. 25.

<sup>125</sup> D.13-05-010, p. 886.

<sup>126</sup> PD, p. 84.

<sup>127</sup> *Id.* Accordingly, the PD therefore correctly grants, with appropriate modifications, CAW’s Special Request #2 to establish a two-way balancing account to track the difference between the total requested net group insurance costs on a per-employee basis and the actual level of new group insurance costs incurred on a per employee basis. See PD, pp. 225-228.

the CPUC should adopt the insurance escalation factors proposed by CAW.<sup>128</sup>

## VIII. SERVICE COMPANY (AMERICAN WATER) EXPENSES AND RATE BASE

### A. Service Company forecast expenses ignores evidence and contradicts CPUC/State policy

The PD ignores substantial evidence on CAW's request for \$12,703,945 to recover Service Company expenses for test year 2018.<sup>129</sup> CAW only forecasts a slight increase from historical Service Company expense:<sup>130</sup>

	2013	2014	2015	2016	2013-2016 average
Service Company	\$12,322,646	\$12,326,553	\$12,396,069	\$12,463,410	\$12,377,169

#### 1. The PD's Service Co. allocation factor ignores the trend of increasing costs

The PD incorrectly directs CAW to "use an average of the recorded percentage allocation factors from 2013-2015, instead of using the recorded 2015 percentage allocation factor, to derive its share of American Water's Service Company expenses."<sup>131</sup> The use of the 2013-2015 average is unreasonable because data in that period predates changes in allocation factors due to the sale of certain subsidiaries like Arizona American Water and New Mexico American Water from the American Water system, thus failing to reflect the increased allocation to CAW following the sale.<sup>132</sup> The PD also errs in using the 2013-2015 average because that approach ignores CAW's increasing allocation due to increased direct charges to CAW. As the data shows increasing direct charging and thus a larger allocation for CAW, the most recent allocation information (*i.e.*, the 2015 percentage allocation factors) is the most likely to reflect 2018 Test Year allocation of Service Company charges.<sup>133</sup> The PD incorrectly disregards the changing Service Company practices with respect to direct charging by asserting that there is "no clear trend exhibited by the historical recorded percentage allocation factors."<sup>134</sup> However, the PD entirely ignores and fails to mention evidence presented by CAW demonstrating increased direct charges to CAW in the areas of water testing in the Central Lab, Customer Service Center, and Health and Safety.<sup>135</sup> The PD also asserts that "American Water's recent acquisitions should lead to shifts in allocations."<sup>136</sup> However, the need to adjust for cost shifts due to acquisitions is in part muted by the fact that total customer counts have no impact on services to CAW that are directly charged.<sup>137</sup> The CPUC should reject the PD's allocation factors based on three-year averages and use CAW's recommended 2015 recorded percentage allocation factors.

#### 2. The PD use of labor inflation factors for Service Company expenses is inappropriate

The PD properly uses the 2016 recorded Service Company labor expenses as the base figure to be

<sup>128</sup> See also CAW Opening Brief, pp. 60-62; *Closing Brief of California-American Water Company* ("CAW Closing Brief"), pp. 27-28 (further explaining group insurance costs).

<sup>129</sup> PD, pp. 100-107.

<sup>130</sup> CAW-20, Chew Rebuttal – Public, p. 22.

<sup>131</sup> *Id.*, p. 103.

<sup>132</sup> Exh. ORA-2, Conklin Testimony, p. 25. The sale of those systems was completed in 2012, but the resulting increased allocation factors for CAW in rates were not implemented until CAW's next GRC decision in 2015, D.15-04-007.

<sup>133</sup> Exh. CAW-20, Chew Rebuttal – Public, pp. 23-27.

<sup>134</sup> PD, p. 102.

<sup>135</sup> Exh. CAW-20, Chew Rebuttal – Public, pp. 24-26.

<sup>136</sup> PD, p. 103.

<sup>137</sup> Exh. CAW-20, Chew Rebuttal – Public, pp. 23-24.

escalated to calculate the forecasted 2018 test year expense.<sup>138</sup> However, the PD incorrectly directs CAW to use “the 2017 and 2018 labor inflation factors published in ORA’s August 2018 Escalation Memo.”<sup>139</sup> The composite escalation factor recommended by CAW is superior and is appropriately used to escalate certain expenses, including “contracted services.”<sup>140</sup> The staffing services are provided pursuant to the Service Company contract and CAW receives bills for these services just like it does from any other vendor.<sup>141</sup> The PD asserts that “[e]ven though American Water provides services to CAW based on a contract, American Water is not an outside contractor for CAW but is CAW’s Parent Company.”<sup>142</sup> There is no basis for this assertion and the PD is unable to cite to any evidence in the record distinguishing the cost of Service Company services from those provided any other outside contractor. Moreover, the composite escalation factor is used to account for non-labor factors as well – the Service Company like any other contractor has both labor and non-labor costs and thus costs increases should reflect both factors. Therefore, the evidentiary record fails to substantiate the PD’s use of the labor escalation factor instead of the composite escalation factor. The CPUC should apply CAW’s recommended composite escalation factors.

### **3. The rejection of business development expenses is contrary to CPUC/State policy**

The PD rejects CAW’s request for funding for its Business Development unit.<sup>143</sup> The PD erroneously asserts that CAW has failed to demonstrate that “ratepayers obtain increased economies of scale and lower costs of capital as a result of the acquisitions that the Business Development unit promotes.”<sup>144</sup> This finding is contrary to the CPUC and State policy promoting consolidation of water systems. The CPUC has recognized that consolidation of water utilities can benefit customers with better service and lower rates, including in decisions for CAW’s recent acquisitions.<sup>145</sup> In the Public Water System Investment and Consolidation Act,<sup>146</sup> the California Legislature similarly found and declared that “[s]cale economies are achievable in the operation of public water systems”<sup>147</sup> and that “[p]roviding water corporations with an incentive to achieve these scale economies will provide benefits to ratepayers.”<sup>148</sup> The State Water Resources Control Board has also recognized the benefits of consolidation in spreading costs over a larger customer base.<sup>149</sup>

CAW’s Business Development unit seeks out and pursues acquisition opportunities to expand the customer base, which in turn achieves economies of scale by allowing CAW to spread shared costs over the larger customer

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<sup>138</sup> PD, p. 104.

<sup>139</sup> *Id.*, p. 105.

<sup>140</sup> *Id.*

<sup>141</sup> *Id.*

<sup>142</sup> *Id.*, p. 104.

<sup>143</sup> *Id.*, p. 107.

<sup>144</sup> *Id.*

<sup>145</sup> D.16-11-014, pp. 8-9.

<sup>146</sup> Pub. Util. Code §§ 2718-2720.

<sup>147</sup> Pub. Util. Code § 2719(c).

<sup>148</sup> Pub. Util. Code § 2719(d); *see also* Assembly Bill 2339 (2018) (finding and declaring that “Small fragmented water service providers are often unable to achieve efficiencies and economies of scale that are available to consolidated water systems with a broader customer base.”).

<sup>149</sup> State Water Resources Control Board, *Water System Partnerships and Voluntary Consolidation* (accessed November 21, 2018), available at [https://www.waterboards.ca.gov/drinking\\_water/certlic/drinkingwater/waterpartnership.html](https://www.waterboards.ca.gov/drinking_water/certlic/drinkingwater/waterpartnership.html).

base.<sup>150</sup> In fact, the PD itself cites “American Water’s recent acquisitions and the subsequent decrease in CAW’s proportion of American Water’s customers” and accordingly decreases the allocation ratio of CAW’s share of American Water’s 2018 IT-related plant costs.<sup>151</sup> The PD can’t have it both ways – it can’t find that the Business Development function fails to result in savings to customers here, then in the same decision reduce CAW’s allocated share of American Water’s costs due to exact acquisitions that the Business Development function is responsible for. Therefore, the CPUC should grant CAW’s requests for costs for its Business Development function.

#### **B. The PD errs in disallowing CAW’s business transformation expenses**

The PD disallows CAW from recording the entirety of the \$1,869,468 and \$2,243,632 it incurred in 2014 and 2015, respectively, related to CAW’s information technology (“IT”) enhancements and upgrades, including upgrades to the earlier Business Transformation (“BT”) Project.<sup>152</sup> The PD also “direct[s] CAW to use the 5.33% ratio to allocate American Water’s 2018 IT-related plant costs, including for the BT Project.”<sup>153</sup> The BT Project was supposed to encompass the original rollout and stabilization of the project as proposed in A.10-07-007 and was completed in 2014.<sup>154</sup> As CAW explained in its briefs, the \$1,869,468 and \$2,243,632 it incurred in 2014 and 2015, respectively, should not be subject to the cost cap for the implementation of the BT Project.<sup>155</sup> Instead, these IT-related plant costs incurred relate to continuing upgrades and enhancements, entirely separate from the implementation phase.<sup>156</sup>

However, the PD mistakenly asserts that CAW failed to explain why it did not forecast these costs in its previous GRC.<sup>157</sup> The PD unfairly singles out the testimony of CAW witness Sherrene Chew, who was not actively involved in the prior GRC.<sup>158</sup> However, CAW witness Mark Schubert (who was involved in the prior GRC) explained in his testimony that CAW “expected that additional unanticipated costs might be incurred to insure the success of the project following its implementation. These are new costs to address needs that became apparent *only after* the CPUC reviewed the requests in the previous California rate case, in A.13-07-002.”<sup>159</sup> This is why those costs could not have been incorporated in CAW’s forecast in A.13-07-002.

The PD next erroneously finds that CAW failed to demonstrate that these costs were prudently and reasonably incurred.<sup>160</sup> However, CAW provided breakdown of the specific costs incurred, including individual line items for various IT projects and vendors.<sup>161</sup> Other documents showed details demonstrating the actual spend on

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<sup>150</sup> Exh. CAW-10, Pray Direct, p. 22.

<sup>151</sup> PD p. 112.

<sup>152</sup> *Id.*, pp. 110-111.

<sup>153</sup> *Id.*, p. 112.

<sup>154</sup> Exh. CAW-20, Chew Rebuttal – Public, pp. 12-13.

<sup>155</sup> CAW Opening Brief, pp. 77-80; CAW Closing Brief, pp. 8-11.

<sup>156</sup> PD, p. 110.

<sup>157</sup> *Id.*, p. 110.

<sup>158</sup> Reporter’s Transcript (“RT”) 544:21-26 (CAW/Chew).

<sup>159</sup> Exh. CAW-12, Schubert Direct, p. 30 (emphasis added).

<sup>160</sup> PD, p. 110.

<sup>161</sup> Exh. CAW-20, Chew Rebuttal – Public, Attachment 4.

specific information technology items as compared to the previously requested and authorized amounts.<sup>162</sup> Moreover, the PD's strict adherence to the previously forecasted cost estimates is out of keeping with CPUC practice – the CPUC routinely grants costs above forecasted amounts due to new circumstances if they were reasonably and prudently incurred for used and useful assets.<sup>163</sup> Therefore, the CPUC should instead allow CAW to record the amounts incurred in 2014 and 2015 as just and reasonable additions to Service Company rate base.

Moreover, even if the 2014 and 2015 costs were subject to the cap (they are not), the PD goes beyond what even ORA had proposed. In addition to the \$4,573,200 BT Project adjustment noted in the PD,<sup>164</sup> D.15-04-007 further authorized (in the approval of a settlement agreement) IT Investment plant addition amounts for 2014 and 2015 of \$414,000 and \$634,800, respectively.<sup>165</sup> Even ORA only recommends a disallowance of \$3,064,632 in recognition of the fact that \$1,048,800 was previously authorized.<sup>166</sup> Thus, even if the CPUC disallows the BT Project amounts over the previously authorized amount (which it should not for the reasons described above), then the CPUC should at most disallow \$3,064,632 in recognition of the earlier partial authorization in D.15-04-007.

The PD also directs "CAW to use the 5.33% ratio to allocate American Water's 2018 IT-related plant costs, including for the BT Project."<sup>167</sup> In addition to the retroactive ratemaking concerns addressed in the PD,<sup>168</sup> the PD's prospective reallocation of such costs may result in a normalization violation.<sup>169</sup> Even though the BT Project implementation was a centrally-sponsored IT project, these assets now sit on CAW's books.<sup>170</sup> While the CPUC adjusted the allocation factor for the BT Project as it was being implemented, the implementation was completed in 2014 and the costs were allocated out to the individual subsidiaries.<sup>171</sup> Therefore, the CPUC should not reallocate the BT Project implementation expenses based upon the latest customer counts, even prospectively.

## **IX. TAXES**

### **A. The CPUC should allow CAW to maintain the existing 2018 Tax Accounting Memorandum Account instead of establishing a new two-way Tax Memorandum Account**

The PD orders CAW to "establish a two-way Tax Memorandum Account to track any revenue differences resulting from the differences in the income tax expense authorized in the GRC proceedings and the tax expenses it incurs."<sup>172</sup> The two-way Tax Memorandum Account described is similar to the existing 2018 Tax Accounting Memorandum Account, except that the latter is limited to the impacts of the 2017 Tax Cuts and Jobs Act ("TCJA").

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<sup>162</sup> *Id.*, Attachment 3, 5.

<sup>163</sup> See, e.g., D.10-04-034 pp. 34-35, Conclusion of Law 20 (acknowledging that utility may seek costs in excess of forecast for project as long as they were "appropriate, reasonable, and prudent").

<sup>164</sup> PD, p. 108.

<sup>165</sup> Exh. CAW-12, Schubert Direct, p. 30.

<sup>166</sup> Exh. ORA-2, Conklin Testimony, p. 30 ("The Commission should remove the \$3,064,632 combined 2014 and 2015 BT Project cost overruns from Cal Am's TY 2018 GO Rate Base because ratepayers should not bear the burden of Cal Am management's responsibility.").

<sup>167</sup> PD, p. 112.

<sup>168</sup> *Id.*

<sup>169</sup> See CAW Opening Brief, pp. 79-80.

<sup>170</sup> Exh. CAW-20, Chew Rebuttal – Public, p. 17 (explaining that the prior allocation must be retained to avoid a normalization violation).

<sup>171</sup> *Id.*, pp. 12-13.

<sup>172</sup> PD, p. 128.

The PD's two-way Tax Memorandum Account would be tremendously onerous and would require considerably more resources for CAW to maintain. The existing 2018 Tax Accounting Memorandum Account is sufficient to record all of the full tax impacts of the TCJA.<sup>173</sup> It is unclear why the PD finds it necessary for CAW to implement the broader two-way Tax Memorandum Account. The PD asserts that the CPUC has directed utilities to establish such memorandum accounts in "several recent general rate case proceedings," but all of the cases cited in support of that assertion are either GRC proceedings for considerably larger electric or gas utilities or for the electric service division of Liberty Utilities, CalPeco Electric.<sup>174</sup> The PD does not explain why CAW is being singled out as the only **water** utility that must comply with the obligations of a more onerous two-way Tax Memorandum Account.

Therefore, the CPUC should instead continue to have CAW use its 2018 Tax Accounting Memorandum Account.

**B. The PD's order to file a Tier 3 advice letter to refund the 2018-2020 Excess Protected ADIT is not possible and may violate normalization rules**

The PD directs "CAW to file a Tier 3 advice letter within 30 days of the issuance of this decision to refund the 2018 Excess Protected ADIT, which should have been recorded in the Tax Memorandum Account, 2019 Excess Protected ADIT, and the 2020 Excess Protected ADIT to ratepayers as a bill credit, based on the size of the customer's meter."<sup>175</sup> The PD further specifies that "[t]he refund shall be amortized evenly over the remaining GRC cycle."<sup>176</sup> This directive is not possible because CAW will not be able to calculate its 2018 Excess Protected ADIT balances based upon the timeline set forth by CAW witness John Wilde, who explained that it will be a 12- to 14-month process from start to finish.<sup>177</sup> As Mr. Wilde had anticipated, CAW has only recently been able to determine that it must use the Average Rate Assumption Method ("ARAM") for the protected balances.<sup>178</sup> The CPUC should provide until at least June 2019 to complete the return of the 2018 Excess Protected ADIT. Moreover, CAW will not be able to calculate or refund subsequent 2019 and 2020 Excess Protected ADIT balances until the tax return is prepared for those years. Additionally, the PD should provide a mechanism for adjustments to rate base caused by return of ADIT balance, which the CPUC has treated as reductions to rate base.<sup>179</sup> Therefore, the CPUC should revise the PD and the ordering paragraphs to instead order the Excess Protected ADIT Balances be refunded to customers in three separate advice letters as shown in **Appendix A**. CAW also respectfully reminds the CPUC that it would be a normalization violation for CAW to return Excess Protected ADIT balances faster than allowed under the IRS normalization rules. The CPUC should specify that refunds of Excess Protected ADIT balances should be returned no faster or sooner than allowed under ARAM to avoid violations.

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<sup>173</sup> Exh. CAW-51, Linam Tax Supplemental, pp. 2-3.

<sup>174</sup> PD, p. 128 fn. 325.

<sup>175</sup> *Id.*, p. 123.

<sup>176</sup> *Id.*

<sup>177</sup> RT 1440:10 to 1441:23 (CAW/Wilde); see also *Closing Brief of California-American Water Company on the Tax Cuts and Jobs Act* (May 14, 2018), p. 9.

<sup>178</sup> RT 1464:20 to 1465:8 (CAW/Wilde).

<sup>179</sup> Exh. CAW-53, Wilde Tax Rebuttal, p. 4; see also *Opening Brief of California-American Water Company on the Tax Cuts and Jobs Act* (May 4, 2018), p. 19.

**C. Notification the CPUC of future tax changes is vague, overly broad, and unreasonable**

The PD orders CAW to “notify the CPUC of any tax-related changes, any tax-related accounting changes, or any tax-related procedural changes that materially affect, or may materially affect, revenues by filing a Tier 1 advice letter with the Water Division.”<sup>180</sup> This language is vague and overly broad. The PD also asserts that this directive is “[s]imilar to the directives ordered in recent general rate case proceedings.”<sup>181</sup> However, the PD supports this assertion with the same reference to electric utility GRCs.<sup>182</sup> While the PD argues that the same proportion with respect to the utility’s revenue requirement is applied here as with the electric utilities,<sup>183</sup> the unreasonably low \$250,000 as an absolute figure is a substantiality lower materiality threshold that will result in more reporting with fewer resources to do so than with electric utilities. It is unreasonable for the CPUC to require CAW to immediately be aware of all of the ill-defined “tax-related changes” that may occur throughout the year given that CAW typically files its tax return once a year and does so as part of the larger American Waterworks Consolidated Group.<sup>184</sup> Therefore, the CPUC should remove the requirement in the PD to notify the CPUC of tax-related changes directly via a Tier 1 advice letter.

**D. The PD errs by failing to allow CAW to track its TCJA implementation costs**

The PD erroneously finds that “CAW has not sufficiently addressed why these implementation costs cannot be forecasted in this proceeding and why these costs are substantial in terms of the amount of money that CAW will incur.”<sup>185</sup> However, CAW presented evidence to show that the implementation of the TCJA may require significant changes to the PowerPlant fixed asset system and the PowerTax system, particularly regarding the excess ADIT balances.<sup>186</sup> At the time that the supplemental tax testimony was submitted (April 6, 2018), CAW was only at the point of working with two key vendors to create the system design plan and review statements of work for reach work stream.<sup>187</sup> CAW had not completed its initial remeasurement of the ADIT balance and the calculation of the impact of the TCJA on ADIT balances and actually then normalizing the resulting excess is a “complex and involved process.”<sup>188</sup> Most critically, Cal-am had not yet made the determination of whether it has the records and could develop a system to execute ARAM or if will need to use the Reverse South Georgia Method (“RSGM”) (it only recently was able to determine that it must use ARAM), which could greatly affect any forecast of costs.<sup>189</sup> Even once the methodology required by the IRS normalization rules is determined, CAW will need to set up the schema for ARAM to appropriately forecast the normalization, a task complicated by the fact that CAW has multiple rate

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<sup>180</sup> PD, p. 130.

<sup>181</sup> *Id.*

<sup>182</sup> *Id.*, p. 130 fn. 328.

<sup>183</sup> *Id.*, p. 130 fn. 329.

<sup>184</sup> Exh. CAW-52, Wilde Tax Direct, p. 6.

<sup>185</sup> *Id.*, p. 126.

<sup>186</sup> Exh. CAW-49, Linam Tax Direct, pp. 4-5; Exh. CAW-52, Wilde Tax Direct, pp. 6-8; Exh. CAW-51, Linam Tax Supplemental, p. 11.

<sup>187</sup> Exh. CAW-54, Wilde Tax Supplemental, p. 5.

<sup>188</sup> Exh. CAW-52, Wilde Tax Direct, p. 8 (“It is also a process that takes significant time, requires great care, and will likely go through several subsequent refinements before being considered an estimate that could be reasonably relied on.”).

<sup>189</sup> *Id.*, p. 9.

jurisdictions.<sup>190</sup> CAW, unlike some of the larger electric and gas utilities in California, has consistently used RSGM in the past to normalize changes in tax rates, so it will take time implement ARAM.<sup>191</sup>

In summary, there was an insufficient basis upon which CAW could have reasonably produced a credible forecast of its implementation expenses. Moreover, it is evident from tasks outlined by Mr. Wilde that it is quite intensive and would inevitably result in substantial costs. Accordingly, the CPUC should instead allow CAW to track its TCJA implementation expenses in a memorandum account.

## **X. PLANT**

### **A. The PD's denial of AMI ignores substantial evidence and is contrary to CPUC policy**

The PD incorrectly rejects CAW's proposal to implement a two-way AMI system in its San Diego, Ventura, Monterey, and Los Angeles County service districts.<sup>192</sup> In doing so, it hinders the ability of CAW to prioritize efficient water use and undercuts the CPUC's earlier support for AMI deployment. Furthermore, the PD's claim that "CAW's pilot AMI pilots are ongoing,"<sup>193</sup> is inaccurate since PD does not include any funding in rates for these programs. Without funding, these programs will cease, forcing CAW to mothball the AMI pilot program and its investments to date. Using water more wisely and eliminating water waste have been identified as state water objectives.<sup>194</sup> The CPUC has already found that AMI would assist in meeting these objectives<sup>195</sup> and that existing meters, such as those CAW currently has in place, "do not accomplish these objectives."<sup>196</sup> By rejecting CAW's AMI proposal, the PD would hinder CAW's ability to further the State goals of wiser water use and eliminating water waste

The PD claims that CAW did not provide sufficient information on the costs and benefits of AMI implementation. This is inaccurate both as to the standard that the PD adopts and in its characterization of CAW's showing in this proceeding. First, the PD echoes ORA's inaccurate claim that CAW was required to provide a detailed cost benefit analysis to justify its AMI proposal.<sup>197</sup> As CAW has previously explained, the CPUC previously rejected ORA's proposed cost benefit cost-benefit requirement in D.16-12-026.<sup>198</sup> Second, contrary to the PD's claims, CAW provided substantial and detailed information regarding its proposed AMI program and the benefits to customers. With its application, CAW served its AMI plan, which included the project description, schedule, cost estimate and AMI-related benefits<sup>199</sup> and was reviewed by and developed in cooperation with Black & Veatch.<sup>200</sup> Additionally, CAW provided extensive testimony regarding how AMI benefits customers, including use of AMI data to respond to leaks, encourage conservation, and provide more efficient and responsive service.<sup>201</sup> Finally, CAW

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<sup>190</sup> *Id.*

<sup>191</sup> *Id.*

<sup>192</sup> PD, p. 139; Application, p. 17.

<sup>193</sup> PD, p. 140.

<sup>194</sup> See Making Conservation a California Way of Life, Implementing Executive Order B-37-16, Final Report (April 2017).

<sup>195</sup> D.16-12-026, pp. 61-62.

<sup>196</sup> *Id.*, p. 62.

<sup>197</sup> PD, p. 135.

<sup>198</sup> CAW Reply Brief, p. 40.

<sup>199</sup> Exh. CAW-13, Svindland Direct – Confidential, Attachment 5.

<sup>200</sup> Exh. CAW-18, Bui Rebuttal, pp. 4-5.

<sup>201</sup> Exh. CAW-13, Svindland Direct – Confidential, pp. 41-63; Exh. CAW-30, Sabolsice Rebuttal, pp. 3-6; Exh. CAW-24, Hofer

also provided information on the lessons learned from its pilot programs, including experience with leak detection and the web and mobile applications necessary to provide information to customers.<sup>202</sup>

CAW's AMI plan represents an important tool to promote conservation efforts and reduce water loss.<sup>203</sup> The PD would needlessly delay implementation of this tested and beneficial technology. The CPUC should modify the PD to allow CAW to move forward with AMI implementation, giving it the tools to encourage and prioritize efficient water use now, allowing it to further State water policy objectives, and making CAW better equipped to respond to future droughts. In the alternative, the CPUC should, at a minimum, modify the PD to allow CAW to recover the costs that it has already expended related to AMI, which it has been tracking in a memorandum account.<sup>204</sup> Alternatively, the PD should eliminate the requirement to provide a detailed cost-benefit analysis in future AMI requests, which is not required by D.16-12-026, and which will severely hinder approval of future AMI requests by not only CAW, but by all water utilities.

#### **B. Rejection of recycled water projects ignores evidence and contradicts CPUC policy**

The PD rejects CAW's request for additional initial planning dollars for its proposed recycled water projects.<sup>205</sup> Specifically, CAW requested additional funding for consulting expenses necessary to complete the information and California Environmental Quality Act ("CEQA") requirements of the Tier 3 advice letter template minimum criteria found in D.14-08-058.

The PD asserts that "CAW improperly makes this request for the first time in its rebuttal testimony, which prejudices other parties and does not provide customers notice of the rate impacts associated with this request."<sup>206</sup> This characterization is misleading. In its original application, CAW proposed three recycled water projects as Tier 2 Advice Letter Projects in the Los Angeles, San Diego, and Sacramento districts.<sup>207</sup> However, after carefully taking account ORA's recommendations, CAW believed it was best to pare down its request to only the preliminary costs for meeting the Tier 3 advice letter requirements of D.14-08-058.<sup>208</sup> CAW is still seeking to ultimately construct substantially the same three proposed projects. The public notices circulated by CAW for this proceeding described impacts of the original full recycled projects. CAW's request is merely a modified version of those earlier requests.

The PD also erroneously stated that CAW fails to justify the reasonableness of the amounts requested.<sup>209</sup> For the original proposed projects, CAW provided detailed information, justification, and documentation about the three proposed projects not only in testimony, but also in the Capital Investment Project Work Papers for each individual project.<sup>210</sup> After the specific request regarding these projects was modified, CAW presented extensive

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Rebuttal, pp. 13-19.

<sup>202</sup> Exh. CAW-30, Sabolsice Rebuttal, pp. 3-6; Exh. CAW-24, Hofer Rebuttal, pp. 14-16.

<sup>203</sup> Exh. CAW-13, Svindland Direct – Confidential, Attachment 5.

<sup>204</sup> Exh. CAW-13, Svindland Direct – Confidential, p. 55.

<sup>205</sup> PD, p. 141.

<sup>206</sup> *Id.*

<sup>207</sup> Exh. CAW-5, Linam Direct, p. 34.

<sup>208</sup> Exh. CAW-25, Linam Rebuttal, p. 39.

<sup>209</sup> PD, p. 141.

<sup>210</sup> Exh. CAW-12, Schubert Direct, pp. 157, 164, 189 (For each of the three proposed projects, witness Mark Schubert

details regarding the status of CAW's planning for each of the projects and described the tasks necessary to meeting the Tier 3 advice letter requirements of D.14-08-058.<sup>211</sup> This evidence substantiates the amounts requested for preliminary work on the proposed recycled water projects.

Lastly, the PD states that "CAW is not precluded from pursuing the proposed recycled water projects and seeking recovery of costs associated with these projects either via an advice letter pursuant to D.14-08-058 or in its next GRC."<sup>212</sup> While this statement is technically true, it overlooks the fact that the preliminary steps of negotiations, planning, CEQA, Tier 3 filing and design process can take and estimated 2 to 3 years – without preliminary funding CAW would effectively be unable to move forward with these recycled water projects.<sup>213</sup> By rejecting CAW's request for the initial planning dollars to even prepare the necessary information for the Tier 3 Advice Letter, the PD is unreasonably expecting CAW to simply put substantial money at risk, with no assurances that it will be able to ultimately earn a return on its investment. Such a position is contrary to both CPUC and state policy, which have made clear the pressing need and demand for recycled water given the State's water conservation goals.<sup>214</sup> Therefore, the CPUC should grant CAW's request for funding for preliminary consulting expenses on its three proposed recycled water projects.

**C. The PD's removal of the Arden Intertie project from rate base ignores substantial evidence**

The PD erroneously removes \$2,557,725 in construction costs for the Arden Intertie carryover capital project (I15-600051) from rate base.<sup>215</sup> The PD does not dispute the prior approval of the project or its need, but finds that CAW did not provide sufficient information that the project is likely to be completed by the end of 2019.<sup>216</sup> However, based on a change in ownership in a key piece of property and a meeting with the Land Use Authority of Sacramento County, CAW has re-commenced work on this project by soliciting an engineering consultant to start design and permitting activities.<sup>217</sup> The Sacramento County Zoning Administrator recently approved the Arden Intertie project, completing the design and planning portions of the project.<sup>218</sup> Therefore, the CPUC should instead find that the Arden Intertie is likely to be completed by the end of 2019 and should remain in rate base.

**D. The PD's denial funds to purchase groundwater rights ignores substantial evidence**

The PD denies CAW's request to purchase groundwater rights in the Los Angeles District, claiming that it is speculative.<sup>219</sup> It is imperative for CAW to have funding available to make such purchases in order to reduce

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explained that "Additional information, justification, and documentation can be found in the Capital Investment Project Work Papers for this specific project.").

<sup>211</sup> Exh. CAW-21, Crooks Rebuttal, pp. 14-31.

<sup>212</sup> PD, pp. 141-142.

<sup>213</sup> See Exh. CAW-25, Linam Rebuttal, p. 43.

<sup>214</sup> See generally D.14-08-058, p. 37, Finding of Fact 1; State Water Resources Control Board, *Policy for Water Quality Control for Recycled Water (Recycled Water Policy)* (January 22, 2013), available at [https://www.waterboards.ca.gov/water\\_issues/programs/water\\_recycling\\_policy/docs/rwp\\_revto.pdf](https://www.waterboards.ca.gov/water_issues/programs/water_recycling_policy/docs/rwp_revto.pdf).

<sup>215</sup> PD, p. 165.

<sup>216</sup> *Id.*, p. 166.

<sup>217</sup> *Id.*; Exh. CAW-31, Schubert Rebuttal, p. 15.

<sup>218</sup> See Sacramento County Planning Administrator, November 21, 2018 Hearing Action Summary, Item 1, available at <http://www.per.saccounty.net/applicants/Zoning%20Administrator/ZA%20Action%20Summary%2011-21-2018.pdf>.

<sup>219</sup> *Id.*, p. 185.

reliance on imported supplies, which is a reasonable and prudent course of action for any water purveyor in Southern California wary of future restrictions to supply.<sup>220</sup> The PD denies CAW's requests based in part on the misplaced contention that it cannot evaluate the circumstances of a particular purchase at this time.<sup>221</sup> However, just as with the costs incurred in any other capital project, the CPUC would review CAW's purchase of groundwater rights to ensure that they are just and reasonable. For example, in Resolution W-5080, the CPUC addressed the ratemaking treatment of certain water rights that were purchased separately alongside CAW's acquisition of Adams Ranch Mutual Water Company using a similar plant item for that purpose. The Division of Water and Audits reviewed CAW's valuation study and found that the purchase price was reasonable.<sup>222</sup> Thus, the PD's worry that these funds will simply be a blank check is unfounded. Therefore, the CPUC should instead approve CAW's request or, alternatively, authorize CAW to pursue it as an advice letter project.

## **XI. DEPRECIATION EXPENSES**

### **A. The PD ignores substantial evidence supporting CAW's forecasted depreciation expenses**

The PD erroneously finds that CAW failed to substantiate the increase in annual depreciation expense and thereby rejects CAW's forecasted annual depreciation expense of \$23.9 million.<sup>223</sup> The PD fails to recognize the substantial evidence CAW provided, while simultaneously finding an inferior figure is reasonable. CAW retained Alliance Consulting Group to conduct a depreciation study in 2015.<sup>224</sup> This depreciation study analysis focused not only on historical data regarding depreciable property but also on the field experience noted by CAW's operations personnel through interviews.<sup>225</sup> Using that information and knowledge about CAW, the depreciation study uses the straight-line, Average Life Group remaining-life depreciation system to calculate annual and accrued depreciation.<sup>226</sup> This methodology is consistent with the CPUC's Standard Practice U-4-W.<sup>227</sup> While the County of Los Angeles proposed to phase in the depreciation expense changes over a period of time, no party disputed the findings and recommendations of the depreciation study or the depreciation rates proposed.<sup>228</sup>

Instead, the PD "find[s] reasonable and adopt[s] the current annual depreciation expense of \$21.6 million for 2018-2020."<sup>229</sup> However, CAW's current depreciation rates were set as part of a settlement agreement approved by the CPUC in CAW's Test Year 2012 GRC (A.10-07-007).<sup>230</sup> Those depreciation rates were based upon a

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<sup>220</sup> Exh. CAW-24, Hofer Rebuttal, p. 4; Exh. CAW-12, Schubert Direct, p. 101; Exh. CAW-31, Schubert Rebuttal, p. 21.

<sup>221</sup> *Id.*

<sup>222</sup> Resolution W-5080 (February 25, 2016), p. 7.

<sup>223</sup> PD, p. 198.

<sup>224</sup> Exh. CAW-12, Schubert Direct, pp. 200-206, Attachment 10.

<sup>225</sup> See *id.*, p. 202; see also *id.*, Attachment 10, p. 15 ("This depreciation study encompassed four distinct phases. The first phase involved data collection and field interviews. The second phase was where the initial data analysis occurred. The third phase was where the information and analysis was evaluated. Once the first three stages were complete, the fourth phase began. This phase involved the calculation of depreciation rates and the documenting the corresponding recommendations.").

<sup>226</sup> *Id.*, p. 201.

<sup>227</sup> See Standard Practice U-4-W, *Determination of Straight-Line Remaining Life Depreciation Accruals* (January 3, 1961), Chapter 8, Section 7.

<sup>228</sup> CAW Opening Brief, pp. 191-192; see Exh. ORA-7, Dawadi Testimony, p. 1-12 ("The differences between ORA's and Cal Am's forecast of depreciation reserve is the result of differences in forecasted Utility Plant in Service.").

<sup>229</sup> PD, p. 198.

<sup>230</sup> D.12-06-016, p. 87. The Test Year 2015 GRC (A.13-07-002) retained the same depreciation rates based upon the

depreciation study conducted in 2010 by the **same** consultant using the **same** methodology as the depreciation study in this proceeding.<sup>231</sup> As the PD finds that the current annual depreciation expense based on the 2010 depreciation study is “reasonable,” it unclear why CAW’s currently proposed annual depreciation expense based on a similar depreciation study is not also reasonable. Moreover, the earlier study relies upon now-outdated data from 2010 and therefore is inferior to the newer 2015 depreciation study that uses more up-to-date information. Pursuant to the mandated schedule, CAW’s next scheduled depreciation study of all of its accounts will be conducted in 2021, requiring the CPUC and CAW to rely on the outdated 2010 information well beyond what is reasonable.<sup>232</sup>

If the CPUC still has issues regarding the information presented in CAW’s current depreciation study or prior studies, CAW will endeavor to meet the CPUC’s specific desires for depreciation studies outlined in the PD the next time such a study is produced. In this instance, however, the CPUC should not rely on the earlier study based on obsolete data. Therefore, the CPUC should grant CAW’s requested increase to authorize an annual depreciation expense of \$23.9 million as substantiated by the 2015 Alliance Consulting Group depreciation study.

## **XII. MEMORANDUM AND BALANCING ACCOUNTS**

### **A. The PD incorrectly removes uncollectible costs for the San Clemente Dam**

The PD directs CAW to “remove the uncollectible costs in the calculation of the annual amortization of the San Clemente Dam costs” because they are counted elsewhere in the RO model.<sup>233</sup> This is the correct outcome for the collection going forward from January 1, 2018, once new rates become effective and those costs have been incorporated into base rates. However, from 2012 through 2017, CAW collected it **solely** through a surcharge. Consequently, the double-collection issue had not arisen yet because uncollectible costs were not being accounted in base rates under the Results of Operation model). The CPUC should clarify CAW is to remove double-counted uncollectible costs prospectively only once CAW begins to collect such costs in base rates.

## **XIII. SPECIAL REQUESTS**

### **A. The PD should seek to further minimize future WRAM/MCBA balances**

In this proceeding, CAW requested to keep the Water Revenue Adjustment Mechanism/Modified Cost Balancing Account (“WRAM/MCBA”) open and eliminate the current cap limiting total annual surcharges to 10% of the last authorized revenue requirement for each of CAW’s districts. Recognizing the opportunity the CPUC has with the tax law changes and the reduced rate of return authorized in D.18-03-035, the PD grants CAW’s request for the account to remain open<sup>234</sup> and increases the WRAM/MCBA cap to 15% for this rate cycle.<sup>235</sup> While this temporary increase in the cap does help to more quickly reduce the large WRAM/MCBA balances and is a step in

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depreciation study completed in the prior GRC.

<sup>231</sup> A.10-07-007, *Partial Settlement Agreement Between the Division Of Ratepayer Advocates, The Utility Reform Network and California-American Water Company on Revenue Requirement Issues* (July 28, 2011) (“A.10-07-007 Settlement”), p. 89.

<sup>232</sup> Standard Practice U-4-W, *Determination of Straight-Line Remaining Life Depreciation Accruals* (January 3, 1961), p. 37 (setting forth time periods between completing studies; see also A.10-07-007 Settlement, p. 384 (adopted settlement between Division of Ratepayer Advocates and CAW providing for depreciation studies to be completed on a 6-year cycle).

<sup>233</sup> PD, p. 202.

<sup>234</sup> *Id.*, p. 205.

<sup>235</sup> *Id.*, p. 234.

the right direction, the CPUC should seek to amortize the WRAM/MCBA balance as quickly as practical.<sup>236</sup> The PD cites the fact that it is ordering the refund of \$7.1 million in Unprotected Excess ADIT balances and amounts of Protected Excess ADIT balances as one of the reasons to increase the cap temporarily.<sup>237</sup> Accordingly, the reduction of the existing WRAM/MCBA balances should similarly be implemented over **the same** timeframe – the best way to accomplish that goal would be for the CPUC to use the refund of Unprotected Excess ADIT balances directly as a net reduction to the \$100+ million in WRAM/MCBA balances that CAW is seeking to recover.<sup>238</sup> The CPUC should also further increase the annual cap to 17% as part of the Monterey Settlement.<sup>239</sup>

#### **XIV. OTHER ISSUES**

##### **A. The PD's ordering paragraphs sets infeasible compliance deadlines**

The PD orders CAW to file several advice letters within 30 days of the issuance of the decision.<sup>240</sup> Many of these advice letters will be complicated, requiring careful drafting to implement the exact directive of the CPUC.<sup>241</sup> Still others could not be completed within 30 days even if they were the only items that CAW's rates department had to focus on.<sup>242</sup> Moreover, the calculations underlying several advice letters cannot be completed concurrently and instead require the results of one to complete the next.<sup>243</sup> CAW appreciates the need to expedite the implementation of these revised tariffs; however, the schedule and structure set forth in the PD is not feasible. The PD purported to adopt CAW's motion for transitional rate relief, which was prepared in consultation with the CPUC water division, but reduced the number of days requested for filing of advice letters. Therefore, CPUC should adjust the compliance deadlines in the PD for the filing of particular advice letters as CAW has proposed in its recommendations to the ordering paragraphs shown in **Appendix A**.

#### **XV. CONCLUSION**

CAW respectfully asks that the CPUC revise the PD as described above and as shown in **Appendix A**.

December 3, 2018

Respectfully submitted,

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<sup>236</sup> CAW Opening Brief, pp. 162-166 (describing the harm of large lingering balances); CAW Closing Brief, pp. 74-76 (same).

<sup>237</sup> PD, p. 233.

<sup>238</sup> *Id.*, pp. 231-232.

<sup>239</sup> Monterey Settlement, p. 11.

<sup>240</sup> See PD, Ordering Paragraphs 12, 16, 17, 18, 21, 22, 23, 24, 28, 40.

<sup>241</sup> See, e.g., *id.*, pp. 318, Ordering Paragraph 21 (directing CAW to file an advice letter to "provide all the accounting entries for the Seaside Ground Water Basin Balancing Account from January 1, 2015 through December 31, 2017 and to request to transfer the outstanding balance," along with "explanations for any discrepancies or variances"). Of the memorandum and balancing accounts that can feasibly be done in 30 days, it nonetheless does not make sense to implement these in a piecemeal fashion given that others are more reasonably completed in 60 days – the CPUC should minimize the number of filings necessary in keeping with the practice for CAW's prior multi-district cases.

<sup>242</sup> See, e.g., PD, pp. 317-318, Ordering Paragraph 17-18 (directing CAW to file advice letters to refund the 2018-2020 excess protected and unprotected ADIT balances, including extensive provide calculations and supporting documentations).

<sup>243</sup> For example, the advice letters to implement 2018 test year base rates, increases caused by surcharges, and 2019 escalation step rates must be completed in that order and cannot be done concurrently.