

February 1, 2011

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Via E-Mail and USPS

Chairman Mary Freeman
c/o Ms. Sharla Dillon
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

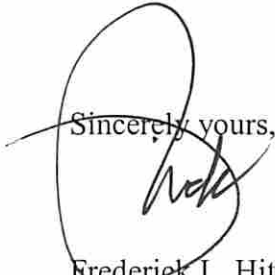
**Re: Petition of Tennessee American Water Company
Docket No. 10-00189**

Dear Chairman Freeman:

Enclosed please find an original and five (5) copies of the City of Chattanooga's First Supplemental Responses to TAWC's Second Discovery Requests. I would appreciate you stamping the extra copy of the document as "filed," and returning it to me in the enclosed, self-addressed, stamped envelope.

With best regards, I am

Sincerely yours,


Frederick L. Hitchcock

FLH:pgh
Enclosures

Chairman Mary Freeman
c/o Ms. Sharla Dillon
February 1, 2011
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cc: Mr. J. Richard Collier (w/encl.)
Mr. R. Dale Grimes (w/encl.)
Mr. Vance L. Broemel (w/encl.)
Mr. Ryan L. McGehee
Ms. Mary L. White
Mr. David C. Higney (w/encl.)
Mr. Henry M. Walker (w/encl.)
Mr. Michael A. McMahan (w/enc.)
Ms. Valerie L. Malueg
Mr. Mark Brooks (w/encl.)
Mr. Scott H. Strauss (w/encl.)
Ms. Katharine M. Mapes
Mr. Donald L. Scholes (w/encl.)
Ms. Kelly Cashman-Grams (via email)
Ms. Monica Smith-Ashford (via email)
Ms. Shilina Chatterjee Brown (via email)

**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

IN RE:

**PETITION OF TENNESSEE AMERICAN
WATER COMPANY TO CHANGE AND
INCREASE CERTAIN RATES AND
CHARGES.**

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Docket No. 10-00189

**CITY OF CHATTANOOGA'S FIRST SUPPLEMENTAL RESPONSES AND
OBJECTIONS TO TENNESSEE AMERICAN WATER COMPANY'S SECOND
DISCOVERY REQUEST**

The City of Chattanooga ("the City"), by and through counsel, hereby serves its First Supplemental Responses to certain of the Second Discovery Requests propounded by Tennessee-American Water Company ("TAWC").

The City incorporates by reference and restates its General Objections and Reservation of Right set forth in its Responses to the Second Discovery Requests.

DISCOVERY REQUEST NO. 1:

List each consulting assignment Ms. Dismukes has performed directly for a regulated utility or a utility service company and for each such assignment please provide: (a) the name of the utility; (b) the name, position, and title of her client contact; (c) the project description; and (d) the project duration (including start and completion dates).

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections

or the General Objections, *see* Attachment 1 to the testimony of Ms. Kim Dismukes. *See* also TAWC-02-01, listing client contact information.

DISCOVERY REQUEST NO. 2:

Please state all facts that support Ms. Dismukes' qualifications to testify as an expert witness with respect to management fees and provide a detailed listing in the tabular format below for each docket or case in which Ms. Dismukes has testified specifically to the prudence or imprudence of management fees charged by the service company of an investor-owned, multijurisdictional utility.

State of Jurisdiction	Year	Docket (case)#	Name of Parent Co.	Name of Subsidiary	Summary Of MJM position	Was MJM position upheld by Commission

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, *see* Attachment 1 to Kim Dismukes' testimony and *see* response to Request No. 9 and 30.

DISCOVERY REQUEST NO. 3:

Please state all facts that support Ms. Dismukes' qualifications to testify as an expert witness with respect to utility-affiliate transactions and provide a detailed listing in the tabular format below for each docket or case in which Ms. Dismukes has testified specifically

regarding utility-affiliate transactions for investor-owned, multi-jurisdictional utility.

State of Jurisdiction	Year	Docket (case)#	Name of Parent Co.	Name of Subsidiary	Summary Of MJM position	Was MJM position upheld by Commission

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, *see* Attachment 1 to Kim Dismukes' testimony and *see* response to Request Nos. 9 and 30.

DISCOVERY REQUEST NO. 4:

Please identify, and to the extent not previously produced, provide all information reviewed by Ms. Dismukes and any analysis performed by Ms. Dismukes prior to the filing of her testimony in this docket that addresses how organization changes at AWW, AWWSC, or TAWC have impacted or caused the changes in management fees for 2000 through present, including but not limited to: the creation of the national customer service facility, the creation of the centralized shared service transactional accounting facility, the creation of the centralized national procurement group, or any other organization change that has occurred at AWW, AWWSC, or TAWC.

RESPONSE:

See the City's Third Supplemental Response to the First Discovery Requests of

Tennessee American Water Company ("Third Supplemental Response").

FIRST SUPPLEMENTAL RESPONSE:

As part of her analysis of the issues in this proceeding, Ms. Dismukes reviewed numerous documents that are part of the record in the instant proceeding (discovery responses, testimony of the Company, and testimony of other parties). As part of her normal background examination in any rate proceeding, she also reviewed documents that are publically available, like AWW Annual Reports, 10-Ks, Orders, Related Testimony, News Releases, etc. that may not be cited in her testimony. If she relied upon specific aspects of any of these, they are cited in her testimony. Ms. Dismukes specifically reviewed no additional documents not cited in her testimony and preformed no specific analyses on how the organization changes at AWW, AWWSC, or TAWC may have impacted or caused the changes in management fees for 2000 through present, including but not limited to: the creation of the national customer service facility, the creation of the centralized shared service transactional accounting facility, the creation of the centralized national procurement group, or any other organization change that has occurred at AWW, AWWSC, or TAWC.

DISCOVERY REQUEST NO. 5:

Please provide all information reviewed by Ms. Dismukes (or analysis performed by Ms. Dismukes) prior to the filing of her pre-filed testimony in this docket that addresses the impact that changes in ERISA pension expense and OPEB expenses have had on management fees charged to TAWC on an annual basis from 2000 to 2011.

RESPONSE:

See Third Supplemental Response.

FIRST SUPPLEMENTAL RESPONSE:

As part of her analysis of the issues in this proceeding, Ms. Dismukes reviewed numerous documents that are part of the record in the instant proceeding (discovery responses, testimony of the Company, and testimony of other parties). As part of her normal background examination in any rate proceeding, she also reviewed documents that are publically available, like AWW Annual Reports, 10-Ks, Orders, Related Testimony, News Releases, etc. that may not be cited in her testimony. If she relied upon specific aspects of any of these, they are cited in her testimony. Ms. Dismukes specifically reviewed no additional documents not cited in her testimony and preformed no specific analyses on how the organization changes at AWW, AWWSC, or TAWC may have impacted or caused the changes in management fees for 2000 through present, including but not limited to: the creation of the national customer service facility, the creation of the centralized shared service transactional accounting facility, the creation of the centralized national procurement group, or any other organization change that has occurred at AWW, AWWSC, or TAWC.

DISCOVERY REQUEST NO. 6:

Please provide a list of all sources and individuals that Ms. Dismukes consulted with in developing her testimony in this proceeding.

RESPONSE:

All sources on which Ms. Dismukes relied in reference to her testimony were cited therein or are disclosed in the material accompanying the City of Chattanooga's Third Supplemental Responses.

DISCOVERY REQUEST NO. 7:

Produce all source documents that Ms. Dismukes referred to or relied on to substantiate

her statement that electric utilities have a higher skilled workforce than water utilities.

RESPONSE:

The differences between the complexity of the operations of a municipal water system and an electric utility are obvious to anyone who has observed both. For example, electric utilities do not have unaccounted for electricity of 24% or more, and water utility customers are not electrocuted by touching a puddle of water produced by a broken main. Ms. Dismukes' observations are based on the numerous documents and testimony that she has examined in both electric and water rate proceedings during her experience of more than 30 years of work with both electric and water utilities. This experience generally is reflected in her background information contained in Attachment 1 to her pretrial testimony.

DISCOVERY REQUEST NO. 8:

Identify, and to the extent not previously produced, provide all work papers or spreadsheets in native form (e.g., excel, word) with formulas intact, annual reports and all other source documents referred to, relied upon or used by Ms. Dismukes to create the schedules attached to her testimony.

RESPONSE:

See Third Supplemental Response.

DISCOVERY REQUEST NO. 9:

For every management audit conducted or performed by Ms. Dismukes, provide a copy of the audit report and for each audit report that was filed with any commission identify the state, docket number, year, company name and parent company name for which the management audit was conducted, and any related RFPs or contracts.

RESPONSE:

TAWC-2-09 contains a copy of the public versions of Ms. Dismukes' report.

DISCOVERY REQUEST NO. 10:

Identify "all Class A water and combination water/waste water utilities operating in the South," referred to by Ms. Dismukes on page 40, line 6 of her direct testimony.

RESPONSE:

See TAWC-2-10, which contains a listing of the requested information.

DISCOVERY REQUEST NO. 11:

State the criteria used to "determine which reports contained the data necessary to conduct the analysis," as testified to by Ms. Dismukes on page 40, line 14 of her direct testimony.

RESPONSE:

The reports that were used for the analysis were those that contained accounting details sufficient to derive information comparable to that set forth in the TAWC annual report.

DISCOVERY REQUEST NO. 12:

Provide any analysis regarding Ms. Dismukes' comparison of the "salaries and wages, pensions and benefits, materials and supplies, all contractual services, rental of buildings, and miscellaneous expenses" of TAWC to expenses in the same accounts of each comparative Class A water and combination water/wastewater company, as described on pages 40, line 22 through page 41, line 8 of Ms. Dismukes' direct testimony.

RESPONSE:

See KHD-15 and KMD-16, appended to the pre-trial testimony of Ms. Dismukes.

DISCOVERY REQUEST NO. 13:

Please identify all increases in City of Chattanooga rates for electricity, wastewater/sewer and property taxes since 2008 or projected for the attrition year and for each increase identify all facts that were relied upon to justify each increase.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence.

DISCOVERY REQUEST NO. 14:

Produce a copy of the current uniform system of accounts, as published by the regulatory commissions of Arkansas, Florida, Kentucky, Missouri, South Carolina and Virginia.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, that the request seeks information equally available to TAWC, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence.

FIRST SUPPLEMENTAL RESPONSE:

Please see the attached information for the States of Arkansas, Florida, and South Carolina provided in Supplemental Attachment TAWC-2-14.

DISCOVERY REQUEST NO. 15:

With respect to Ms. Dismukes' testimony at page 41 lines 9-10, please state why Ms. Dismukes chose to include the referenced accounts and provide any supporting documentation for this decision.

RESPONSE:

In general, the referenced accounts were chosen because they were the accounts AWWSC management fees would have been charged to had they not been charged to the contractual services account by TAWC. In addition, for the companies that do not have management fees or service companies, the functions generally performed by the management company would be performed by company personnel, whose costs would be charged to these accounts.

DISCOVERY REQUEST NO. 16:

Please state each and every basis for Ms. Dismukes' statement on page 44, lines 14-17 that "the length of calls, on average, for an electric company would be longer than a water company," and provide any documents referred to or relied upon by Ms. Dismukes in support of this statement.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, In general, the basis is stated in the testimony. The observation is

based upon Ms. Dismukes' extensive experience with both water and electric utilities and the greater complexity and risks involved with electric utilities. TAWC-2-16 contains documents that show that the average handling time for an electric company are longer than for a water company.

DISCOVERY REQUEST NO. 17:

With respect to page 47, lines 5 to 9 of Ms. Dismukes' direct testimony, provide the percent discount that Ms. Dismukes believes a third party provider of management and professional services would provide to TAWC for outsourcing services it receives from AWWSC and provide any documents referred to or relied upon by Ms. Dismukes in support of this statement.

RESPONSE:

Discounts reflect a number of factors, including whether they are negotiated in an arms-length transaction between unrelated parties. In general, discounts are the result of negotiations and are not subject to general rules of estimation.

DISCOVERY REQUEST NO. 18:

With respect to page 7, lines 8 through 12 of Ms. Dismukes' direct testimony, please provide all evidence, studies, or any other information in the possession of Ms Dismukes that supports her assertion that American Water or American Water Works Service Company may be incentivized "to misallocate or shift costs to regulated companies so that the non-regulated companies can reap the benefits" and reference any portion of the independent Schumaker Management Audit performed for the TRA that found evidence of misallocation or shifts of costs to the regulated companies.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, because companies maximize profit and public utility profits are typically limited by regulation, there is an inherent incentive to shift costs to the regulated operations to maximize the profits of a company that has both regulated and nonregulated companies or operations.

DISCOVERY REQUEST NO. 19:

With respect to page 13, line 26 to page 14, line 1 of Ms. Dismukes' direct testimony, please state whether, based on the information presented in the American Water 10-K provided to Ms. Dismukes, the non-regulated segment of American Water produces more net income than the regulated segment.

RESPONSE:

Not according to American Water Work's 10K.

DISCOVERY REQUEST NO. 20:

With respect to page 18, line 22 to page 19, line 5; page 24, lines 4 - 23; and page 55, lines 18 to 21 of Ms. Dismukes' direct testimony, does Ms. Dismukes advocate a benefit based system of cost allocation? If so, provide all studies, analyses, publications, testimony, briefs, orders or any other documents or information referred to or relied upon to support this position.

RESPONSE:

Ms. Dismukes has not made a recommendation concerning an adoption of a benefit based system of cost allocation in this case. She has endorsed such an approach in other cases.

DISCOVERY REQUEST NO. 21:

With respect to page 18, line 22 to page 19, line 5; page 24, lines 4 - 23; and page 55, lines 18 to 21 of Ms. Dismukes' direct testimony, does Ms. Dismukes believe that the metrics used for Tier 1 allocations are inappropriate? If so, provide all studies, analyses, publications, testimony, briefs, orders or any other information referred to or relied upon to support this position.

RESPONSE:

The City objects to the request, as it mischaracterizes the testimony.

FIRST SUPPLEMENTAL RESPONSE:

Ms. Dismukes does not support the use of largely size-based allocation factors for allocating costs between regulated and non-regulated companies or operations, because they fail to reflect the significant benefits received by the smaller non-regulated companies from the services provided. The Tier I allocation factors used by AWWSC are largely size-based and are similar to the Massachusetts Formula, which Ms. Dismukes in the past has rejected in other proceedings. Ms. Dismukes, if she were making a recommendation on this subject, would develop a methodology which better reflects the benefits received by the smaller non-regulated companies/operations. Attached as Supplemental Attachment TAWC-2-21 are orders that support Ms. Dismukes' position.

DISCOVERY REQUEST NO. 22:

Please provide any studies, reports, correspondence, City Council minutes, committee minutes,

ordinances, resolutions, or other documents of any kind created from January 1, 2008 to the present that reflect discussions with or requests to TAWC related to planning, proposing, or making capital improvements for reasons including, but not limited to: fire protection, downtown revitalization, service problems, economic development, or transportation improvements.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, the City does not have any role in TAWC's capital expenditure decisions. TAWC-2-22 contains copies of documents that might be responsive to a broad reading of the request. The City will supplement as needed.

DISCOVERY REQUEST NO. 23:

With respect to page 27, line 20 to page 30, line 7 of Ms. Dismukes' direct testimony, please provide a list of all water utilities used by Ms. Dismukes for comparison in schedules KHD-1 5 and KHD-16, and for each utility identified, state whether the water is produced or purchased, and if produced, the source of the water. If there is more than one type of source of water, list annual amounts from each source and provide the type of treatment system utilized to produce finished drinking water.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of

information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, the utilities are identified in the materials provided in the City's Third Supplemental Responses. TAWC-2-23 contains available information responsive to the request.

DISCOVERY REQUEST NO. 24:

With respect to page 27, line 20 to page 30, line 7 of Ms. Dismukes' direct testimony, list all affiliates for each water company listed by Ms. Dismukes in schedules KHD-15 and KHD-16, and identify the states in which they operate. For each affiliate, indicate: (a) whether the affiliate is regulated or non-regulated; (b) whether tariff rates are metered rates, flat rate, or some combination; and (c) list the number of residential, commercial, industrial, governmental, public authority, fire service and other classes of customer for each affiliate.

RESPONSE:

The City objects to the request as it mischaracterizes the testimony, and it is, therefore, impossible to respond to the request. The City further objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence.

FIRST SUPPLEMENTAL RESPONSE:

Below is a table that reflects for each company contained on Revised Schedules KHD-1 and KHD-2, whether or not the company has one or more affiliates and if the affiliate(s) is

regulated or non-regulated.

Utility	Affiliates (Yes/No)	Regulated/Nonregulated
United Water Arkansas	Yes	Regulated & Nonregulated
Aqua Utilities of Florida	Yes	Regulated & Nonregulated
Indiantown Company, Inc.	Yes	Nonregulated
Lake Utility Services	Yes	Regulated & Nonregulated
Mad Hatter Utility, Inc.	Yes	Regulated
Marion Utilities, Inc.	No	
Ni Florida, LLC	Yes	Regulated & Nonregulated
North Beach Utilities, Inc.	Yes	Nonregulated
North Fort Myers Utility, Inc.	Yes	Regulated & Nonregulated
North Sumter Utility Company	Yes	Nonregulated
O&S Water Company, Inc.	No	
Peoples Water Service Co.	Yes	Regulated & Nonregulated
Rainbow Springs Utilities	Yes	Nonregulated
Royal Utility Company	No	
Sanlando Utilities Corporation	Yes	Regulated & Nonregulated
Southlake Utilities Inc.	No	
Utilities, Inc. of Florida	Yes	Regulated & Nonregulated
Water Management Services	Yes	Nonregulated
Wedgefield Utilities, Inc.	Yes	Regulated & Nonregulated
Water Service Corp. of KY	Yes	Regulated & Nonregulated
The Empire District Electric Co.	Yes	Regulated
Carolina Water Services	Yes	Regulated & Nonregulated
Kiawah Island Utility	No	
Utilities Services of South Carolina	Yes	Regulated & Nonregulated
Aqua Virginia, Inc.	Yes	Regulated & Nonregulated
Massanutten Public Service Corp.	Yes	Regulated & Nonregulated

DISCOVERY REQUEST NO. 25:

With respect to page 30, lines 8-11 of Ms. Dismukes' direct testimony, please provide all studies, analyses, publications, testimony, briefs, orders or any other information referred to, or relied upon by Ms. Dismukes to support her contention that there are minimal seasonal differences in demand for water utilities, and provide all comparative studies performed by Ms. Dismukes of the relative demand differentials of electric and/or gas utilities and water utilities.

RESPONSE:

The City objects to the request as it mischaracterizes the testimony, and it is, therefore,

impossible to respond to the request. The City further objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence.

FIRST SUPPLEMENTAL RESPONSE:

Ms. Dismukes has not prepared any comparative studies of the seasonal demand differentials of electric and/or gas utilities compared to water utilities. However, she has been involved in many water and wastewater and electric and gas proceedings where the subject of seasonal demand was addressed.

DISCOVERY REQUEST NO. 26:

With respect to page 44, lines 3-8 of Ms. Dismukes' direct testimony, please provide all studies, analyses, publications, or other information referred to or relied upon by Ms. Dismukes to support her statement that "Underground facilities cause fewer safety concerns and therefore fewer calls to water call centers than to electric company call centers."

RESPONSE:

The observation is based upon Ms. Dismukes' 30 years of experience working with electric and water utilities and upon logic and common sense. It is generally understood in the electric industry that underground facilities are safer and cause fewer outages during storms and inclement weather than overhead lines. The same is true for water companies, however, most if not all of their water is transported underground and not in overhead or aboveground lines. A similar conclusion obviously was reached by Mr. Baryenbruch as he adjusted the electric company data to recognize that water companies have fewer calls per customer than electric

companies.

DISCOVERY REQUEST NO. 27:

With respect to page 44, lines 3-8 of Ms. Dismukes' direct testimony, please provide all studies, analyses, publications, or other information referred to or relied upon by Ms. Dismukes to support her statement that " . . . due to their more complicated operations and seriousness of outages, the length of calls, on average, for an electric company, would be longer than a water company."

RESPONSE:

In general, the basis is stated in the testimony. The observation is based upon Ms. Dismukes' extensive experience with both water and electric utilities. See response to Request No. 26.

DISCOVERY REQUEST NO. 28:

With respect to page 48, lines 19 and 20 of Ms. Dismukes' direct testimony, please state whether Ms. Dismukes contends that AWWSC provides public utility water service to customers of Tennessee American or any other state utility subsidiary of American Water. If not, please state whether Ms. Dismukes contends that water service is provided by the comparative water utilities shown on KHD-16 at a lower cost than the cost of water service provided by Tennessee American to its customers.

RESPONSE:

The City objects to the request as it mischaracterizes Ms. Dismukes' testimony. The City further objects to this request on the grounds that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, see Ms. Dismukes' testimony at the referenced page

and lines. The comparative utilities referenced in KHD-16 provide management and administrative services at a lower cost than TAWC.

FIRST SUPPLEMENTAL RESPONSE:

Ms. Dismukes has not prepared a study that compared the overall rates of the comparative group to TAWC.

DISCOVERY REQUEST NO. 29:

With respect to page 6, lines 10-13 of Ms. Dismukes' direct testimony, identify by page and line number in Ms. Dismukes' testimony each alleged problem and flaw identified with respect to the Baryenbruch report that is "equally applicable" to the Schumaker audit and leads her to the conclusion that the TRA should reject the Schumaker audit.

RESPONSE:

The City objects to this request on the grounds that the request mischaracterizes the testimony, that the request seeks information that is overly broad, that the request is unduly burdensome, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, the problems with the Baryenbruch report identified on page 27, line 13 through page 33, line 9 equally apply to the Schumaker report and those identified on page 34, line 1 through page 39, line 17 apply to the Schumaker report, but the accounts are different.

DISCOVERY REQUEST NO. 30:

In Appendix 1 to Ms. Dismukes' testimony Ms. Dismukes lists 29 water or water/wastewater cases in which she appeared as a witness. With respect to those cases, identify each case that involved a utility which is part of a multi-state utility holding company organization structure and for each of the utilities listed, (a) identify each case in which Ms.

Dismukes provided testimony regarding affiliate agreements between a multi-state service company affiliate and the regulated utility in that case; (b) provide copies of the testimony (with exhibits) given by Ms. Dismukes in each case; and (c) provide copies of all studies, reports and exhibits referred to or relied upon to support Ms. Dismukes' position in each case.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome and is duplicative of other requests, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, see responses to Request Nos. 2, 3, and 9. Additional responsive documents are contained in TAWC-2-30.

DISCOVERY REQUEST NO. 31:

Does the City contend that the Schumaker Management Audit ordered by the TRA fails to provide the "thorough examination of the affiliate arrangement between TAWC and AWR" as recommended by Ms. Dismukes on page 3, lines 7-8? If yes, please state each fact or basis for the City's position.

RESPONSE:

Yes. See, generally, Ms. Dismukes' testimony concerning the Shumaker Management Audit. The request is premature in that it seeks information concerning matters about which discovery and analysis are ongoing and may not be completed the time of the hearing. The City notes that TAWC has withheld extensive documents that may be relevant to this request, and that the City has requested that the deposition of Ms. Shumaker be scheduled in Chattanooga. The

City reserves the right to supplement this response.

DISCOVERY REQUEST NO. 32:

With respect to page 3, lines 17 through 19 of Ms. Dismukes' direct testimony, please state whether Ms. Dismukes agrees that the use of customers to allocate costs is acceptable in this case, or whether she proposes an alternative approach. If an alternative approach, please describe in detail the proposed alternative approach.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, Ms. Dismukes did not make a recommendation on the subject. However, she pointed out the shortcomings of the customer allocation methodology.

DISCOVERY REQUEST NO. 33:

Please identify each service included in AWWSC's A&G costs that are not essential to maintain adequate service, meet accounting standards, meet water quality standards, process regulatory filings, obtain low cost capital, prepare budgets, communicate with customers, and obtain and retain qualified employees. If the Company is not able to obtain the lower costs Ms. Dismukes proposes please explain in detail how setting rates at the cost of service Ms. Dismukes proposes will result in just and reasonable rates.

RESPONSE: The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of

information that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information or analysis that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, Ms. Dismukes did not complete an item-by-item analysis of each of the thousands of charges made to TAWC. Instead, she undertook a comparison of the overall administrative and management customer account expenses incurred by comparable water utilities. If TAWC is well-managed, there is no reason that it can not obtain needed levels of necessary management services at cost comparable to those paid by other water utilities in the south. The TRA should not permit TAWC to charge its customers for expenses that are excessive when compared to comparable companies.

DISCOVERY REQUEST NO. 34:

Provide any studies which Ms. Dismukes refers to or relies upon to support: (1) the statement on page 5 of her testimony that business development costs should be eliminated and/or (2) that growth in revenue from regulated customer acquisition or regulated services does not benefit the customer.

RESPONSE:

The City objects to the mischaracterization of Ms. Dismukes' testimony. Without waiving this objection or the general objections, please refer to pages 49 through 55 of Ms. Dismukes' testimony.

FIRST SUPPLEMENTAL RESPONSE:

Ms. Dismukes has not completed any analysis other than that referred to at pages 49 through 55 of her testimony concerning business development costs charged to TAWC.

DISCOVERY REQUEST NO. 35:

Please state whether the City contends that the allocations of time and expenses made during the service company accounting process should be made at the account level or the transaction level and explain your understanding of how overhead transactions are allocated in the service company accounting process.

RESPONSE:

The City objects to the request, as it uses terms that are not defined. The City further objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence.

FIRST SUPPLEMENTAL RESPONSE:

Ms. Dismukes is not making a recommendation as to the method (transaction or account level) by which the service company expenses should be allocated. It is Ms. Dismukes' understanding that the allocation of costs from the service company to the AWWC subsidiaries is made at the transaction level.

DISCOVERY REQUEST NO. 36:

With respect to page 3, lines 18-19 of Ms. Dismukes' testimony, please identify all approaches that "are superior" to the use of customers for allocating costs between the regulated companies. For each approach identified: (a) explain why the listed approach is superior; (b) explain how the allocation methodology "considers usage and/or volume in the allocation formula;" and (c) referencing page 19, lines 6-7, explain how the approach listed

"recognizes the benefits received by each affiliate" in the allocation formula and provide all studies, reports, etc. that support the superiority of each approach.

RESPONSE:

The City objects to the request as it mischaracterizes Ms. Dismukes' testimony. The City further objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving this objection or the general objections, Ms. Dismukes has not identified all the approaches that are superior to the use of customers for allocating costs. However, she does describe some deficiencies in the present allocation method in her testimony.

DISCOVERY REQUEST NO. 37:

Please state whether Ms. Dismukes has performed any studies that show there is a relationship between the type of customer (e.g., residential, commercial, industrial, other) served by a regulated water/wastewater utility and the level of support services required from an affiliate service provider to serve the specific type of customer. If so, please provide a copy of all such studies.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor

likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, studies of the type indicated were not required for the preparation of Ms. Dismukes' testimony.

DISCOVERY REQUEST NO. 38:

With respect to page 19, line 9 of Ms. Dismukes' testimony, please define the term "relatively new acquisitions" and state whether Ms. Dismukes performed any studies that show that "relatively new acquisitions" may benefit disproportionately from the corporate functions that are provided by AWWSC. If so, please provide all such studies.

RESPONSE:

The City objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, in general, Ms. Dismukes used the phrase "relatively new acquisitions" to refer to companies and startup or development that have not yet achieved planned numbers of customer levels, revenue, levels of assets, and/or levels of employees.

FIRST SUPPLEMENTAL RESPONSE:

Ms. Dismukes has not prepared, nor does she have, any such study. Refer to Supplemental Attachment TAWC-2-21 for orders that support Ms. Dismukes' position.

DISCOVERY REQUEST NO. 39:

With respect to Appendix 1 — Dismukes Qualifications page 4, line 28, Ms. Dismukes refers to "the Massachusetts Formula for cost allocations" in her qualifications. Please identify

the allocation factors contained in the Massachusetts Formula and for each allocation factor identified in the Massachusetts Formula, explain whether Ms. Dismukes believes that the allocation factor is largely "size based" and explain how the factor recognizes the benefits received by each affiliate in the allocation formula.

RESPONSE:

The City objects to the request as it mischaracterizes Ms. Dismukes' testimony and/or uses terms that are not defined. The City further objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, allocation factors used in the "Massachusetts Formula" generally includes operating expenses, net assets, and number of employees. The formula generally does not recognize or allocate the full benefits provided by a service company to a new unregulated enterprise.

DISCOVERY REQUEST NO. 40:

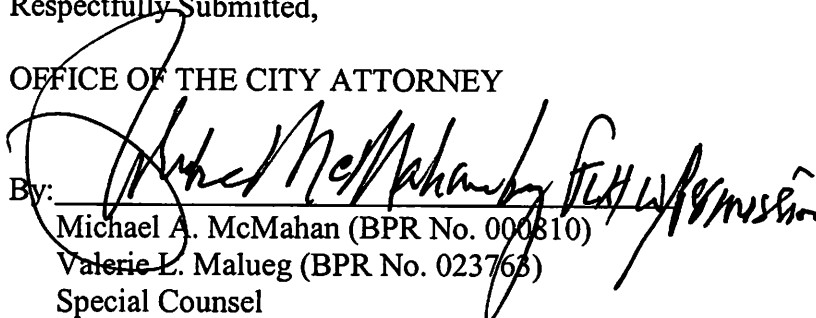
Please state whether the Massachusetts Formula and the Modified Massachusetts Formula have been used and accepted to allocate costs between regulated and non regulated affiliates by various regulatory authorities and whether Ms. Dismukes has ever recommended use of Massachusetts formula or used the formula in any analysis of the appropriateness of allocations. If so, please provide the name of the regulatory commission, state, rate case number and a copy of all relevant testimony, exhibits and orders related to its use.

RESPONSE:

The City objects to the request as it mischaracterizes Ms. Dismukes' testimony or requests that express opinions as to matters not included within the scope of her testimony. The City further objects to this request on the grounds that the request seeks information that is overly broad, that the request is unduly burdensome, that the request seeks the creation of information or analysis that is not in existence and seeks its presentation in a form that may be incomplete or inaccurate, and that the request seeks information that is neither relevant nor likely to lead to the discovery of admissible evidence. Without waiving these objections or the General Objections, Ms. Dismukes has not recommended or used the "Massachusetts Formula."

Respectfully Submitted,

OFFICE OF THE CITY ATTORNEY

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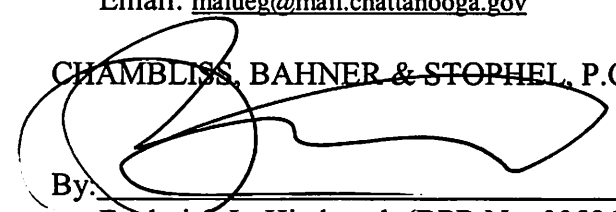
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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing pleading was emailed and was served upon the following person(s) via ☐ hand delivery or ☒ United States first class mail with proper postage applied thereon to ensure prompt delivery:

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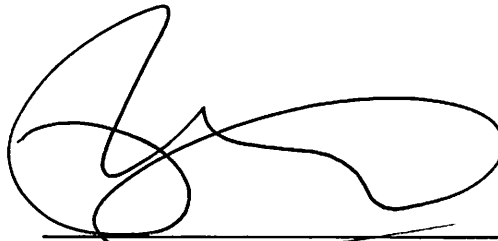
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This 1st day of February, 2011.



Frederick L. Hitchcock

Supplemental TAWC-2-21



65 of 99 DOCUMENTS

Commonwealth Edison Company: Petition pursuant to Sections 7-101, 7-102 and 7-204A(b) of the Illinois Public Utilities Act for an order approving an agreement for the provision of facilities and services and the transfer of assets between Commonwealth Edison Company and Unicom Corporation and its subsidiaries

95-0615

ILLINOIS COMMERCE COMMISSION

1997 Ill. PUC LEXIS 134

March 12, 1997

OPINION: [*1]

ORDER

By the Commission:

On December 7, 1995, Commonwealth Edison Company ("ComEd" or the "Company") filed with the Illinois Commerce Commission ("Commission") a verified petition pursuant to Sections 7-101, 7-102 and 7-204A(b) of the Public Utilities Act (the "Act") for an order approving an Affiliated Interests Agreement between ComEd and its holding company, Unicom Corporation ("Unicom"), and Unicom's other subsidiaries: Unicom Resources Inc., Unicom Technology Development Inc., Unicom Enterprises Inc., (formerly CECO Enterprises Inc.) and Unicom Thermal Technologies Inc., (formerly Northwind, Inc.). Unicom and its subsidiaries are hereinafter referred to as "Unicom entities."

During the pendency of this proceeding, appearances were entered or Petitions to Intervene were filed by: the Staff of the Commission ("Staff"); the City of Chicago ("City"); the Illinois Attorney General on behalf of the People of the State of Illinois ("AG"); the State's Attorney of Cook County on behalf of the People of Cook County ("Cook County") and the Citizens Utility Board ("CUB"). The Hearing Examiner granted all Petitions to Intervene.

Pursuant to notice given in accordance with the law and [*2] the rules and regulations of the Commission, this matter came on for hearing, before a duly authorized Hearing Examiner of the Commission at its offices in Chicago, Illinois on April 17-19, 1996. ComEd appeared by counsel and presented the testimony of Mr. John Bukovski, Vice President and Chief Financial Officer; Mr. Charles L. Jakubowski, Manager of Financial Reporting; Mr. Richard P. Rolling, Assistant Comptroller; Mr. James E. Farmer, Partner, Arthur Andersen LLP; and Dr. Morten I. Kamien, Professor at the Kellogg Graduate School of Management, Northwestern University. Staff appeared by counsel and presented the testimony of Dan Jenkins, Audit Supervisor, Accounting Department of the Public Utilities Division. The City, Cook County, and AG appeared by counsel and conducted cross-examination, but did not sponsor any witnesses of their own. At the conclusion of the hearings on April 19, 1996, the record was marked "Heard and Taken."

ComEd, Staff, Cook County, the City and AG filed simultaneous initial briefs and reply briefs. The AG requested oral argument on the face of its briefs.

A Hearing Examiner's Proposed Order ("Proposed Order") was served on all the parties. Briefs on exceptions [*3] and replies thereto were filed by ComEd, Staff, AG, and the City/Cook County jointly. The foregoing exceptions and replies have been considered by the Commission. In large part, the exceptions to the determinations reached in the Proposed Order reiterate the arguments presented by the parties in their initial briefs and reply briefs. Additionally, the exceptions corrected clerical errors, recommended clarifications and proffered additional analysis. In those instances where the Proposed Order has been changed to correct clerical errors and to include clarifications and additional analy-

sis which do not affect the determinations reached in the Proposed Order, the Proposed Order is corrected, clarified and analysis added without further discussion. The only determination reached in the Proposed Order which has been modified or changed as a result of the exceptions and replies is the formula for allocation of common costs. The Post Exceptions Proposed Order adopts Staff's two-factor formula.

I. DESCRIPTION OF THE AFFILIATED INTERESTS AGREEMENT

The Affiliated Interests Agreement ("AIA" or "Agreement"), admitted into evidence as ComEd Exhibit 3a, establishes policies and procedures [*4] for intercompany charges for transactions involving ComEd and the Unicom entities. The AIA covers an extensive range of transactions, among them the use of facilities (including office space, warehouse and storage space, real property, manufacturing and production facilities, vehicles, and computers, communications, and other types of equipment); the provision of services (including not only administrative/management and personnel services, but also purchasing services and operational services such as engineering, design, construction, and testing); joint purchasing; centralized cash management; tax sharing; asset sales (real, personal, and tangible); and sales of Unicom common stock for employee and director compensation purposes. The Agreement is "two-way" in that it provides for the provision of facilities and services and the transfer of assets both from ComEd to the Unicom entities and from the Unicom entities to ComEd.

The core provisions of the Agreement are its policies and procedures for intercompany charges and accounting. Specifically, with respect to asset transfers, the Agreement provides that sales or transfers are to be made at fair market value, whenever that value [*5] is determinable. The Agreement establishes that fair market value may be determined by looking at the price that the selling entity charges for the same or similar assets to third parties, the price charged by unaffiliated vendors for the same or similar assets, or the value ascribed to the asset by an independent appraisal or valuation. If no such fair market value exists, the asset sales or transfers shall be made at the historical cost to the selling party, less all applicable valuation reserves.

As for facilities and services, those provided by ComEd to the Unicom entities will be charged at the prevailing price to the public (i.e., a tariffed price where such a price exists) or, where such does not exist, at ComEd's fully distributed cost. Facilities and services provided by the Unicom entities to ComEd will be charged at the prevailing price to non-affiliates, or, if there is no such prevailing price, at an amount not to exceed the Unicom entity's fully distributed cost. The Agreement further provides that Unicom costs that jointly benefit all other parties to the Agreement, such as shareholder services, financial and accounting information systems, legal services, and procurement [*6] services, will be charged to a "Consolidated Pool" and apportioned to all parties using a three-factor methodology that weighs equally the parties' gross payrolls, operating revenues, and capital assets.

The AIA also provides for asset transfers among ComEd and the Unicom entities. ComEd seeks blanket approval for real estate transfers of \$ 1,000,000 or less, and for tangible personal property transfers of \$ 300,000 or less. Transfers above those amounts, and all transfers of intangible assets, would require case-by-case approval by the Commission.

The Agreement also provides for the sharing of taxes or credits resulting from the Unicom entities' filing of consolidated federal income tax returns. Under certain circumstances, consolidated or combined state income tax returns also are required. To ensure that each party to the Agreement bears its fair share of such taxes, the AIA includes, as Exhibit C to the Agreement, the Income Tax Allocation Agreement ("the Tax Agreement"), which allocates consolidated income taxes to each member participating in a return in a manner commensurate with the portion of the tax liability caused or avoided by that member for the tax year.

Upon ICC approval, [*7] the AIA would govern future transactions between ComEd and each of the current Unicom entities. The AIA also provides that any other entity which may become an affiliate of Unicom or any of the other parties to the AIA, may become a party to the AIA by executing an agreement adopting all of its terms and conditions. Additionally, the AIA would replace previous agreements between ComEd and the Unicom entities.

Detailed policies and procedures implementing the principles of the Agreement are contained in a user's manual referred to as a Cost Allocation Manual ("Manual"). The Manual will provide guidelines and specifications necessary to ensure that the provisions of the Agreement are well-understood and properly applied by employees. It is described by the Company as a user's manual that by its very nature will be a constantly evolving document. A preliminary draft of the Manual was admitted into evidence as AG Cross Exhibit 8.

II. SUMMARY OF PARTIES' POSITIONS

A. ComEd

ComEd contends that it has amassed overwhelming and largely uncontradicted record evidence that its Agreement is in the public interest and should be approved. It alleges that the record shows that diversification [*8] has enormous benefits for ComEd, its ratepayers, and the general public, that a comprehensive two-way agreement is necessary for these benefits to be fully realized, and that the Agreement is more than adequate to prevent cross-subsidization and other ills against which this Commission must guard. ComEd notes that the Commission has on several occasions in the past considered and approved affiliated interest agreements similar to that before it here, citing Northern Illinois Gas Co., Docket 60256 (Feb. 11, 1976); Peoples Gas Light & Coke Co. & North Shore Gas Co., Docket 55071-Supp. (Nov. 13, 1974); People Gas Light & Coke Co. & North Shore Gas Co., Docket 55071 (Sept. 10, 1969).

B. Staff

Staff recommends approval of the AIA subject to certain conditions which allow Staff to perform its duties as required by the Act, and to assist the Commission in safeguarding the public interest by preventing subsidization of non-utility affiliates by ComEd ratepayers. Certain of the conditions have been agreed to by ComEd and Staff and are unopposed by Intervenor. The following agreed-to conditions are found at page 3 of Staff's Reply Brief:

- Record transactions in separate [*9] subaccounts;
- Record costs and reimbursements reciprocally "above the line";
- Charge market price or fully loaded/allocated cost;
- Develop and maintain written guidelines;
- Subject affiliate transactions to internal auditing procedures;
- Enact ratemaking for consolidated taxes in ComEd's rate cases;
- Require approval to transfer intangible assets.

In addition, Staff and ComEd have agreed to certain procedures for adding new affiliates to the AIA. These are found at pages 12 and 13 of Staff's Initial Brief. Intervenor. oppose these procedures as contrary to the Act. Staff also recommends that the Agreement be conditioned by language establishing that the guidelines contained in the approved contracts will not necessarily be determinative for ratemaking purposes. Finally, Staff recommends two other conditions which are opposed by ComEd: that Staff be provided access to books, accounts and records of the AIA signatories and that a two-factor formula be used consisting of total assets and gross payroll factors to allocate the Consolidated Pool costs.

C. City

The City recommends that the Commission reject the Agreement as not in the public interest. The City [*10] asserts that the record shows that it is ComEd's affiliates, and not ComEd, that will benefit most from the terms of the Agreement; that several of the specific provisions of the Agreement are unlawful since they contravene the plain language of the Act; that other provisions would permit ComEd to provide substantial services and facilities to its affiliates without receiving compensation that reflects the value of those services and facilities to the affiliates; and that the Agreement contains a methodology that assures that virtually all of the common costs under the Agreement will be allocated to ComEd. In the alternative, the City recommends that the Commission should modify the Agreement substantially.

D. Cook County

Cook County recommends denial of the Agreement in its present form. It maintains that approval would violate the provisions of the Act regarding the supervision of public utilities, specifically Sections 4-101, 7-101(2), 7-102, 7-204A(b) and 7-205. Additionally, Cook County maintains that ComEd's Manual must be reviewed along with the AIA to determine that both of these agreements are in the public interest and are just and reasonable.

E. AG

The AG [*11] recommends denial of the Agreement for the following reasons. First, ComEd has failed to demonstrate approval of the proposed AIA is in the public interest and will convenience the public, as required by Sections 7-101, 7-102 and 7-204A(b). According to the AG, approval of the Agreement would permit the diversion from ComEd of any of its resources that Unicom wants for its other subsidiaries. Additionally, this would facilitate the moving of corporate opportunities belonging to ComEd to other Unicom affiliates. Further, certain provisions of the Agreement, the addition of new parties without Commission approval and exempting certain real estate transactions from Commission review, are illegal. Other provisions permit cross-subsidies to flow to ComEd's affiliates; specifically, the allocation of Consolidated Pool costs using a three-factor formula and permitting use of ComEd's skilled employees without adequate compensation. The AG further maintains that certain of the provisions are so onerous that their approval would thwart the goals of the Act, creating a virtually open-ended obligation for ComEd to provide to its affiliates the resources they request and one-sided termination [*12] provisions. Finally, the AG contends that the Manual is a key element to implementing the provisions of the Agreement and should be submitted to the Commission for its review and approval as required by the Act in order to safeguard the public interest.

Alternatively, the AG recommends that if the Commission approves the Agreement, such approval must be conditioned as follows: The illegal provisions of the Agreement must be stricken; those provisions that permit cross-subsidies must be modified; the onerous provisions must be modified or stricken; and the Manual must be submitted for Commission approval. Additionally, the AG lists six conditions on pages 22-24 of its initial brief which it urges the Commission should place on approval of the Agreement.

III. LEGAL STANDARD FOR APPROVAL OF THE AGREEMENT

A. ComEd's Position

ComEd contends that under Sections 7-101 and 7-102 the Commission must approve the AIA if it finds that it will not harm the interests of ComEd's ratepayers. In support of its position ComEd cites Illinois Power Co., Docket 93-0039, May 19, 1993, and Illinois Power Co., Docket 92-0404, November 9, 1993. ComEd argues that the record in this proceeding [*13] compels a finding that the AIA safeguards the public interest by preventing cross-subsidization and other harms against which the Commission is duty-bound to protect. Moreover, ComEd maintains that the record establishes that the Agreement affirmatively benefits ratepayers and the public in several respects, most importantly by requiring ComEd's affiliates to pay a portion of its fixed costs that ratepayers otherwise would be required to bear.

ComEd argues that the evidence supports its position that the Agreement will prevent cross-subsidization. It maintains that the Agreement establishes comprehensive policies and procedures for allocating costs related to transactions between ComEd and its Unicom affiliates, thereby ensuring that costs are tracked and properly accounted for. In particular, it argues that cross-subsidization is precluded by the Agreement's requirements that ComEd be paid fair market value or prevailing price, if available, or historical cost less applicable valuation reserves, for any assets transferred, and the prevailing price or fully distributed cost for any services or facilities provided to Unicom entities. The Agreement prevents cross-subsidization where [*14] the Unicom entities are providing facilities and services to ComEd by ensuring that ComEd will pay prevailing price if available or no more than fully distributed cost.

In support of its position that the Agreement affirmatively benefits ratepayers and the public, ComEd references the testimony of Dr. Kamien, Mr. Farmer and Mr. Bukovski and maintains that the record establishes that the Agreement benefits ratepayers by requiring ComEd's affiliates to pay a portion of its fixed costs that ratepayers otherwise would bear; by ensuring that ComEd always is able to purchase goods and services from affiliates at the same prices available to others in the market; by allowing ComEd the means to achieve cost savings and other efficiencies by having certain services centrally provided to ComEd and other Unicom entities; and by making possible a level playing field between ComEd and Unicom and other utility holding company systems, such as the Peoples Gas and NI-Gas systems.

B. Intervenor's Position

The City and AG argue that ComEd's interpretation of the legal standard applicable to this proceeding is too narrow and should be rejected. They argue that a fair reading of the two Illinois [*15] Power cases cited by ComEd reveals that ComEd has not fairly presented the Commission's decision on the applicable legal standard.

They assert that rather than ComEd's unduly narrow interpretation of the "public interest" standard, these cases instead provide that the Commission has broad discretion to decide whether a proposed transaction should be approved or not pursuant to this Section and that discretion is not limited to merely examining whether ratepayers will be adversely impacted by the transaction. They cite *Illinois Power v. Illinois Commerce Commission*, 111 Ill. 2d. 505, 490 N.E. 2d

1255 (1986), in support of their position. Moreover, they maintain that there is no support in the case law or the Commission decisions for ComEd's contention that the Commission must approve a transaction unless it finds ratepayers will be adversely affected.

The City and AG further argue that even if the Commission were to adopt Edison's unduly narrow interpretation of the "public interest" standard, the Agreement still should be rejected or substantially modified since the record and briefs filed by the AG, City and Cook County show that the Agreement in its present form will result [*16] in significant harm to ratepayers. Among those arguments are the following: the Agreement is not in the public interest because it does not compensate ComEd for the value to its affiliates of their access to ComEd's employees and facilities; it is not in the public interest because it does not compensate ComEd for the costs incurred in training, or for the costs it might incur in replacing, employees who transfer to an affiliate; and ComEd's three-factor formula for allocating common costs is not in the public interest because it assures that virtually all of the common costs will be allocated to ComEd and likely will result in cross-subsidization. Each of these arguments is discussed later in this Order.

C. Commission Conclusion

The Commission has reviewed Section 7-102, the case law relating thereto, our decisions cited by the parties, and the positions of the parties relating to the standard to be applied under Section 7-102. Section 7-102 provides that "... if the Commission is satisfied that such petition should reasonably be granted, and that the public will be inconvenienced thereby, the Commission shall make such order in the premises as it may deem proper and as the [*17] circumstances may require, attaching such conditions as it may deem proper" We agree with Intervenor that we have broad discretion to decide whether a proposed transaction should be approved under the public convenience standard. The legislature, apparently recognizing that it would be impractical to attempt to provide precise criteria to be considered in every transaction regulated under this Section, gave the Commission such broad discretion. *Illinois Power Co. v. Illinois Commerce Commission*, 111 Ill. 2d 505, 512, 514, 96 Ill. Dec. 50, 490 N.E. 2d 1255 (1986).

For purposes of this proceeding, the Commission believes that if the evidence indicates the benefits to ratepayers are reasonably likely to exceed the costs or harms to ratepayers, then approval of the Agreement would be appropriate.

Applying this standard to the record before us, we find that the Agreement, as modified herein, is in the public interest because it has affirmative benefits. The record establishes that the Agreement safeguards the public interest by preventing cross-subsidization to the maximum extent practicable under Illinois law. The record also establishes that the Agreement benefits ratepayers [*18] by requiring ComEd's affiliates to pay a portion of its fixed costs that ratepayers otherwise would bear; and by allowing ComEd the means to achieve cost savings and other efficiencies by having certain services centrally provided to ComEd and other Unicom entities.

The Commission further finds, and as will be further discussed with particularity herein, that the arguments presented by Intervenor in opposition to the approval of the Agreement are based on speculation and lack evidentiary support. Accordingly, the Commission concludes that subject to the conditions, restrictions and modifications found appropriate herein, the Agreement should be approved.

IV. ADDITION OF NEW AFFILIATES TO THE AGREEMENT

The Agreement provides that any other entity which is or may become an affiliate of Unicom or any other party to the Agreement may become a party by executing an agreement adopting all of its terms and conditions. (Agreement, ComEd Ex. 3A at Section 9.2). This provision would permit new affiliates to proceed under the Agreement without additional Commission approval.

A. Staff/ComEd Stipulation

ComEd and Staff entered into a stipulation which amends ComEd's initial [*19] proposal ("the Stipulation"). (Staff/ComEd Joint Ex. 1). The amended procedure provides Staff with the information it desires regarding new affiliates and creates a public record, while still providing ComEd and its affiliates the flexibility needed to take advantage of business opportunities and to compete with other energy service providers.

Under the Stipulation, 30 days before a new affiliate will become a party to the Agreement, ComEd will provide Staff with information about the proposed new affiliate and the projected type and frequency of transactions with that affiliate. During the 30-day review period, Staff may investigate whether the provision of facilities and services to the new affiliate is in the public interest within the meaning of Section 7-101.

If Staff notifies ComEd at any time during the review period that it believes that the provision of facilities and services to the new affiliate is not in the public interest within the meaning of Section 7-101, ComEd will file a petition at the Commission seeking resolution of the issues raised by Staff within 30 days after Staff's notice.

At the end of the 30-day review period, regardless of whether ComEd is required to [*20] file a petition with the Commission, the new affiliate may become a party to the Agreement and engage in transactions with ComEd unless and until ordered otherwise by the Commission after a hearing on ComEd's petition. However, if at the end of the review period Staff has not required ComEd to file a petition, ComEd will instead file a document, similar to that entered as ComEd Exhibit 3.B, as a Supplemental Report which will provide information regarding the new affiliate and the projected type and frequency of transactions the new affiliate is expected to have with ComEd. ComEd will serve the Supplemental Report on the parties to this docket.

Finally, at the end of the first 12-month period after a new affiliate has been added to the Agreement, ComEd will file a second Supplemental Report with the Commission. This Report will show the actual type and frequency of transactions between ComEd and that affiliate over the previous 12 months, including a listing of any asset transfers and ComEd's monthly billings to the affiliate. ComEd also will serve this second Supplemental Report on the parties to this docket.

Staff points out in its Brief on Exceptions that the Commission's recent [*21] Order in Docket 95-0353 for MidAmerican Energy Company supports and is consistent with the terms and provisions included in the Stipulation.

B. Intervenor's Position

The City, Cook County and AG argue that the Stipulation providing that future affiliates can be added to the Agreement without Commission approval is contrary to the Act and therefore must be rejected.

First, Intervenor's argue that the Stipulation violates the straightforward requirements of Section 7-101(3). That Section requires that "no management, construction, engineering, supply, financial or similar contract and no contract or arrangement for the purchase, sale, lease or exchange of any property or for the furnishing of any service, property or thing, hereafter made with any affiliated interests . . . shall be effective unless it has been filed with and consented to by the Commission." 220 ILCS 5/7-101(3) (emphasis supplied). The stipulation would allow contracts with the new affiliates to be effective unless the Commission affirmatively refuses to consent. This would contravene the plain meaning of the Act, frustrate the General Assembly's clear intent, and render that portion of the Act a nullity. [*22]

They further argue that Section 7-101(3) does not contain any waiver provisions, nor does it provide for prospective approval to allow new affiliates to bypass Commission approval. The only waivers available to Section 7-101(3) requirements are detailed in Section 7-101(4) but this listing does not expressly include the addition of new affiliates to a contract or arrangement. Finally, Intervenor's argue that in enacting Sections 7-105 and 7-106, the General Assembly clearly specified that Sections 7-101 and 7-102 applied. Moreover, Section 7-106 clearly states that contracts and arrangements must be filed. 220 ILCS 5/7-106(h).

C. ComEd Position

ComEd maintains that the stipulation meets the Act's requirements. As an initial matter, because the Agreement itself provides that new affiliates may be added from time to time, the Commission's approval of the original Agreement is the only approval required by Sections 7-101 and 7-102. Moreover, the Commission's approval of the original Agreement's cost allocation policies and procedures constitutes a Commission finding that these policies and procedures are adequate to guard against cross-subsidization and thus are in the public [*23] interest. Thus, argues ComEd, there is no need under the Act for the Commission to engage in the empty exercise of re-approving these cost allocation guidelines each time a new affiliate agrees to be bound by them.

ComEd further argues that if this procedure were deemed illegal under the Act, then the Commission's orders approving affiliated interest agreements for ComEd competitors such as NI-Gas, Peoples and North Shore also would be illegal. ComEd cites the Commission's Order in NI-Gas, Docket 60256 at 7 (Feb. 11, 1976), wherein it approved an operating agreement that provided "that any entity which is or may become an affiliate . . . may become a party to the Operating Agreement by adopting all the terms of the Operating Agreement." Likewise, in People Gas Co. and North Shore Gas Co., Docket 55071 (Sept. 10, 1969) and People Gas Co. and North Shore Gas Co., Docket 55071-Supp. (Nov. 13, 1974), the Commission held that Peoples and North Shore could add "any other corporation which may become an affiliate" to their respective intercompany service agreement merely by executing a copy of the service agreement.

ComEd further argues that NI-Gas, Peoples and North Shore are [*24] not required to file anything with the Commission in order to add a new affiliate to their respective affiliated interests agreements, nor is there a requirement that these utilities even notify Staff of the addition of new affiliates. Nor are NI-Gas, Peoples Gas or North Shore required to file any supplemental reports regarding the expected type and frequency of transactions between the utility and the new affiliate under the respective agreements. Also, NI-Gas, Peoples Gas or North Shore are not required to notify other interested parties of the addition of new affiliates to their affiliated interest agreements.

In short, ComEd maintains that the procedures agreed to by ComEd and Staff plainly comply with the requirements of the Act. Moreover, they require ComEd to provide considerably more information to the Commission and to intervening parties than NI-Gas, Peoples Gas or North Shore are required to provide under their Commission-approved agreements.

In response to Intervenor's arguments, ComEd argues that the plain language of the Agreement, which makes clear that the addition of new affiliates will not involve "new" contracts with ComEd, flatly contradicts Intervenor's argument [*25] that the Agreement as implemented in the stipulation violates Sections 7-101 and 7-102. ComEd maintains that if the Commission ultimately approves the AIA, it will approve Section 9.2 of the Agreement, which provides that "any other entity which is or may become an affiliate of Unicom or any of the other parties to this agreement may become a party to this Agreement by executing an agreement adopting all of the terms and conditions of this Agreement." Because the AIA by its own terms permits the addition of new affiliates, the Commission's approval of the Agreement will constitute the approval required by Sections 7-101 and 102. So long as the new affiliate adheres to precisely the same policies and procedures the Commission has determined to be adequate to protect against cross-subsidization and other harms, the new affiliate is not entering into a "new" agreement; rather, it is becoming an additional party to an existing approved agreement pursuant to the express terms of that existing agreement.

D. Commission Conclusion

The Commission has reviewed Sections 7-101 and 7-102 and the arguments of the parties. Based on its review, the Commission concludes that the addition of [*26] new affiliates to the AIA will not involve "new" contracts with ComEd, but rather is the addition of a new party to an existing agreement adopting all the terms and conditions of the agreement. The Commission finds that by filing and receiving Commission approval of the AIA, ComEd has satisfied the requirements of Sections 7-101 and 7-102. Since the addition of new affiliates is provided for in the Agreement and the new affiliates will be subject to the same terms and conditions provided in the ASA, the Commission finds it unnecessary to reapprove the AIA for the addition of each new subsidiary to the Agreement. Moreover, the Commission finds that the Stipulation sets forth requirements which further satisfy the public interest, and that the Stipulation's provisions are consistent with the requirements that we recently adopted in our Order in Docket 95-0353. Accordingly, the Commission determines that it is not necessary for ComEd to seek individualized approval for the addition of each new affiliate to the Agreement.

V. PRE-APPROVAL OF ASSET TRANSFERS BELOW A SPECIFIED DOLLAR AMOUNT

The Agreement provides that ComEd and its affiliates may transfer real property having a [*27] value of \$ 1,000,000 or less, and tangible personal property having a value of \$ 300,000 or less, without approval of the specific transfer agreement by the Commission. (Agreement, ComEd Ex. 3A at Sections 3.1 and 3.2).

A. Intervenor's Position

The City, Cook County and AG argue that ComEd's request for pre-approval for real property transfers below \$ 1,000,000 violates Section 7-102. They explain that the purpose of this Section is to ensure both that the public is adequately served, and that the utility receives an appropriate amount when entering into real estate contracts with affiliated interests. They maintain that Section 7-102 specifically sets forth what is required for Commission approval of inter-corporate real estate transactions with affiliated interests: ComEd must file a petition setting forth the terms and conditions of any contract with an affiliated interest. According to Intervenor, without such a filing, the Commission will be unable to determine if the public is being inconvenienced.

Intervenor further argue that ComEd's reliance on Section 13-601 of the Telecommunications Act as support for approval of real estate transfers below \$ 1,000,000 is misplaced. [*28] They explain that the General Assembly expressly granted telecommunication carriers the authority to transfer real estate of up to \$ 1,000,000 without Commission approval, but has not granted the same authority to electric utilities. Since the Act does not directly grant Edison the power to transfer real property of up to \$ 1,000,000, and the Act does not authorize the Commission to permit such

transfers, the Commission cannot give ComEd that privilege. Further, filing requirements under Section 7-101 and 7-102 apply unless the Commission grants a waiver. The Commission has no authority to grant a waiver for sales of property for more than \$ 300,000. They note that the General Assembly did not modify these requirements in Sections 7-105 and 7-106.

In response to ComEd's contention that the Commission has pre-approved similar transactions for Peoples and North Shore in Docket 60270, Intervenor maintain that the fact that the Commission purported to grant such relief to another utility is meaningless where the Commission does not have the authority to give ComEd the relief it seeks.

B. ComEd Position

ComEd asserts that it does not seek exemptions for such transactions under [*29] the Act; rather, it seeks to have the Commission pre-approve real estate and tangible personal property transfers up to the specified amounts, so long as the transactions are priced according to the AIA.

ComEd explained that it looked to Section 7-102 to set the \$ 300,000 level beyond which asset transfers would require individual approval. Similarly, for real estate transfers, ComEd based its \$ 1,000,000 figure on the fact that telecommunications carriers need no Commission approval for real estate transfers below that same amount. See 220 ILCS 5/13-601.

ComEd argues that the Commission has the authority to pre-approve transactions. It maintains that pre-approval is particularly appropriate in this case because, as Mr. Bukovski explained, "real estate and tangible personal property transfers at prices below the specified amounts encompass routine, non-controversial transactions", where the real issue concerns setting a price for the assets. (Id. at 10). According to ComEd, if the Commission were to determine, after reviewing the pricing methodologies and cost allocation principles set forth in the Agreement, that the manner in which ComEd intends to value real estate and [*30] personal property is reasonable, then such transfers would not need case-by-case approval. See, e.g., 83 Ill. Admin. Code 310.40. ComEd further argues that the Commission has pre-approved similar transactions for other Illinois utilities, finding not only that pre-approval would "contribute to the efficient and economic operation" of the utility, but also that pre-approval would "eliminate the present need for costly and time consuming proceedings concerning the approval of certain personal property transfers." Order, Peoples Gas Light and Coke Co. and North Shore Gas Co., Docket 60270 at 3 (Mar. 24, 1976).

In reply to Intervenor's arguments, ComEd argues that "pre-approval" is precisely what is required by the Act. Pursuant to Section 7-102, a public utility is generally prohibited from transferring real property unless and until it first obtains approval, i.e., pre-approval, from the Commission. 220 ILCS 5/7-102. The Commission has long recognized its authority to pre-approve transactions with values in excess of the statutory limit. See, e.g., Order, Docket 22569 (June 2, 1953) (approving transactions up to \$ 15,000 where statutory exemption was \$ 500).

Moreover, [*31] ComEd argues that it is not asking for permission to transfer real property on undefined terms and conditions. To the contrary, it is seeking approval to transfer real property pursuant to the specific terms and conditions set forth in the Agreement. (See Agreement, ComEd Ex. 3A at 6). Approval of the relevant Section (3.1) of the Agreement, therefore, is entirely consistent with the Act.

In its Brief on Exceptions, ComEd requests that if the Commission does not approve the transfer of real property of less than \$ 1,000,000 pursuant to Section 3.1 of the Agreement, that the Commission expressly make clear that parties may amend Section 3.1 of the Agreement so that it permits what is plainly implicit in the Proposed Order, the transfer of real property involving consideration of not more than \$ 300,000 without Commission approval.

C. Commission Conclusion

Pursuant to our review of Sections 7-102, 7-105 and 7-106, we conclude that Section 7-102 expressly limits the Commission's authority to waive the filing and approval of real estate sales only up to \$ 300,000. The General Assembly has not authorized the Commission under the Act to permit transfers over that amount. ComEd's [*32] reliance on Section 13-601 of the Telecommunications Act as support for approval of real estate transfers below \$ 1,000,000 is applicable only to telecommunications carriers. Accordingly, Section 3.1 of the Agreement pertaining to real estate transfers below \$ 1,000,000 cannot be approved. Implicit in this finding is permission to transfer real property without Commission approval involving consideration of not more than \$ 300,000. Section 3.1 should be amended so that it is consistent with this conclusion.

VI. ACCESS TO BOOKS, ACCOUNTS AND RECORDS OF THE AIA SIGNATORIES

Staff proposes that one condition for approving the AIA should be that the Staff shall have access to all books, accounts and records (collectively, "Records") of each current and future party to the AIA to the extent that ComEd may obtain possession or control of such books, accounts and records, to allow the Staff to determine whether there has been any transaction with or any impact on ComEd related to its non-utility affiliates and the contracts in this docket. The AG supports Staff's proposal.

A. Staff Position

Staff argues that under Section 7-101(2), the Commission has "access to **all** [*33] accounts and records of such affiliated interests" having transactions with ComEd. The Random House College Dictionary (Random House, Inc., 1975) Revised Edition defines transaction as "something that is transacted esp. a business agreement." Staff submits that the AIA is a business agreement, and deduces that the AIA itself is a "transaction." Staff maintains that as soon as the Unicom affiliates become signatories to the AIA, they became "affiliated interests having transactions . . . with public utilities under the jurisdiction of the Commission." Accordingly, Staff argues that the Commission shall have access to "all" accounts and records of such "affiliated interests."

Staff further argues that Section 7-101(3) provides that when a utility seeks approval for contracts with an affiliated interest, "the Commission may condition such approval in such manner as it may deem necessary to safeguard the public interest." According to Staff, this is a broad grant of authority to the Commission to impose conditions to the approval of the AIA, particularly where Staff testifies that it needs the access in order to perform its oversight duties.

Staff points out that [*34] the Commission previously required this exact same condition of Illinois Power in Docket 94-0005 (May 11, 1994). Staff contends that this condition will assist Staff in its duty to remain informed of the use of the Company's resources and will help the Commission to protect against subsidization of non-utility activities, and is consistent with Sections 7-101(2) and 7-101(3), 7-205 and 4-101.

Staff maintains that the limited access that ComEd proposes is not adequate for Staff to monitor transactions under the AIA. Staff refers to an admission by Mr. Farmer that it is possible that ComEd could provide services or assets to affiliates and not record the transaction at all, resulting in no record of the activity on ComEd's books. However, under Staff's proposal, unrecorded labor services, for example, may be discovered by examining the memos, letters, meeting minutes, reports, notes or other documents of the affiliate. Likewise, Mr. Farmer stated that asset sales under the AIA are made at fair market value whenever possible, and that fair market value may be evidenced by examining the prices that the affiliate charges for sale of the same or similar assets to third parties. ComEd's [*35] proposal for limited access would not allow Staff to examine such third party transactions, whereas Staff's proposed access would. Mr. Farmer also stated that, for Staff to determine whether ComEd's proposed three-factor formula allocates the correct amount of Unicom costs, Staff will need access to the payroll, asset and revenue data of each Unicom subsidiary even for subsidiaries that do not otherwise engage in transactions with ComEd. ComEd's proposed limited access would not allow this.

Staff points out in its Brief on Exceptions that the Commission's recent Order in Docket 95-0353 for MidAmerican Energy Company adopted precisely the same access to nonutility books, accounts and records that Staff has proposed for ComEd in this case.

B. ComEd Position

ComEd maintains that Staff's proposal is contrary to Section 7-101. Section 7-101(2) provides that:

The Commission shall have jurisdiction over the affiliated interests having transactions, . . . with public utilities under the jurisdiction of the Commission, to the extent of access to all accounts and records of such affiliated interests relating to such transactions, including access to accounts and records of [*36] joint or general expenses, any portion of which may be applicable to such transactions[.]

ComEd contends that when read in its entirety, including the underlined phrases--which Staff neglects to mention when it argues that its proposal is "consistent" with Section 7-101, it is clear that the General Assembly intended the Commission to have precisely the access that ComEd has proposed, i.e., access to all accounts and records related to transactions between ComEd and its affiliates under the Agreement. Any attempt to enlarge the authority specifically granted to the Commission would result in exceeding its jurisdiction.

According to ComEd, the record makes clear as a factual matter that Staff does not need broad access to all unregulated affiliate records to monitor affiliate transactions. ComEd asserts that the testimony of Mr. Farmer and Mr. Ja-

kubowski establishes that ComEd's books and records alone are sufficient to identify any transaction provided by ComEd to its affiliates because the unique function numbers that will be used to record affiliate transactions will readily identify all such transactions. Thus, to track a service or asset provided by ComEd to an affiliate, [*37] the Commission need only review the ComEd books to ensure that the transferred asset or provided service was accounted for properly and that either market price or fully allocated cost was received.

Similarly, to track a service or good provided by an affiliate to ComEd, the Commission need only look to the specific accounting data on ComEd's books and the books of the unregulated affiliate regarding that particular transaction to match the amount paid by ComEd to the accounting data of the affiliate. For such transactions valued at no greater than fully distributed cost, what is required is access to the relevant general ledger cost accounts and support that is used to compute the fully distributed cost of the products or services. Finally, for asset transfers based on fair market value, Staff will need to review the studies or other documentation which support the valuation.

ComEd proposed that in order to ensure consistency with Section 7-101, the Commission should essentially incorporate the precise terms of Section 7-101 in its order and provide that:

ComEd will give the Commission and its Staff access to all accounts and records of Unicom and Unicom's other subsidiaries [*38] related to transactions between ComEd and Unicom and Unicom's other subsidiaries under the AIA, including access to accounts and records of joint or general expenses, any portion of which may be applicable to such transactions.

In response to Staff's argument that the Unicom entities as parties to the Agreement are involved in an on-going transaction with ComEd, ComEd contends that this position has no support in logic or in law and would make the statutory restriction of Section 7-101 meaningless.

ComEd responds to Staff's contention that it needs access to all books and records in order to discover evidence of transactions that might not be recorded at all on ComEd's books by referring to Mr. Farmer's testimony that "this could only occur as a result of a breakdown in ComEd's system of internal accounting control", and "ComEd's internal control system is adequate to ensure that affiliate transactions are recognized and properly recorded." Furthermore, Mr. Farmer pointed out the unrecorded affiliate transactions are recognized by neither party. Thus, access to the books and records of affiliates to search for transactions provided by ComEd would not address this issue.

In response [*39] to Staff's suggestion that if an affiliate sold an asset to ComEd at fair market value, Staff would not be provided with access to third party sales transactions of the affiliate to validate the prevailing price, ComEd refers to Mr. Farmer's testimony wherein he stated that in those transactions based on prevailing prices, the relevant books and records would include the general ledger revenue accounts, supporting journals and underlying source transactions. He testified that these records would enable Staff to verify that the prices charged by Unicom affiliates to ComEd are the same as those charged to unaffiliated third-party customers for like products or services.

ComEd contends that there is no real issue with respect to Staff's access to records in connection with the three-factor formula. Mr. Jakubowski and Mr. Farmer both indicated that in order to determine that the three-factor formula allocates the correct amount of the Unicom Consolidated Pool to ComEd, Staff will need access to the three-factor formula values even for affiliates that do not otherwise engage in transactions with ComEd.

Finally, ComEd points out that the provision for access to records in the Illinois [*40] Power order cited by Staff as identical to that proposed by Staff here, was part of a settlement agreed to by IP; the Commission did not order IP to include such a provision.

C. Commission Conclusion

Section 7-101(2) gives the Commission jurisdiction over affiliated interests having transactions with public utilities. It further provides for Commission "access to all accounts and records of such affiliated interests relating to such transactions," including access to accounts and records of joint or general expenses "any portion of which may be applicable to such transaction." ComEd is not seeking approval here for a singular transaction but for a comprehensive agreement that concerns several affiliated interests with ongoing transactions for a ten-year period. Thus, the construction to be given Section 7-101(2) must be broad enough to accommodate these circumstances. Furthermore, Section 7-101(3) authorizes the Commission to condition the approval of the Agreement in such manner as we may deem necessary to safeguard the public interest. The Commission concludes that under the circumstances presented here, Staff's proposed access to all records of the AIA signatories is [*41] a necessary condition that will enable Staff to ascertain whether

there has been any unjustified subsidization of non-utility activities and to determine whether costs are fairly and reasonably allocated between utility and non-utility activities. As we recently stated in our Order in Docket 95-0353, the Commission believes that Staff's proposed access is in compliance with the Act and is both reasonable and necessary to protect the public interest. We agree with Intervenor's that we have broad discretion

VII. ALLOCATION OF COMMON COSTS

The Agreement assigns to each affiliate the costs that are directly attributable to that affiliate. (Agreement, ComEd Ex. 3A at Section 5.2). To the extent that costs cannot be attributed directly to any particular affiliate, they will be placed in a "Consolidated Pool" and then apportioned using a three-factor formula. Staff and the Intervenor's are opposed to this formula. Staff proposed a two-factor formula while the AG, Cook County and the City recommend the adoption of the FCC's one-factor formula.

A representative list of the types of services for which costs shall be charged to the Consolidated Pool includes: corporate services, financial [*42] and accounting services, information systems, investor relations, legal services, procurement services, regulatory services, risk management services, shareholder services and secretary's office services. The three-factor formula that would be used to allocate the unattributable common costs of Unicom consists of three measures of the relative size of the Unicom affiliates: gross payroll, operating revenues, and capital assets. Each party is allocated and billed costs from the Consolidated Pool based on that party's relative average of each of these three items compared to the corresponding averages for the other parties to the Agreement. Capital assets include the net book value of property, plant and equipment and nuclear fuel, coal and material and supplies inventory, as applicable.

A. ComEd Position

According to ComEd, the common costs in the "Consolidated Pool" by definition have no cost causation component. These costs, which are limited to costs of corporate governance and investor relations and compliance, are largely fixed in nature and primarily cover costs that were incurred wholly by ComEd prior to the formulation of Unicom. Thus, any allocation of Pool costs to [*43] affiliates other than ComEd likely will benefit ratepayers by causing the affiliates to share in their recovery.

ComEd argues that its three-factor formula is the most appropriate methodology for allocating common costs because (1) it is a balanced measure of three commonly accepted indicators of relative size that cut across any type of business that one can imagine; (2) each of the factors is easy and objective to measure; and (3) it has been widely accepted by regulators, including FERC and this Commission, as well as by the federal government for use in government contracts.

ComEd further argues that the costs in question are by definition common costs which means they are incurred on ComEd's behalf as well as on behalf of its affiliates. And by any measure of relative size, it is reasonable to expect that, in the near term, ComEd will be and should be allocated a predominant share of these common Pool costs.

With respect to Mr. Jenkins' recommendation that the Commission use a two-factor formula ComEd argues that the Commission already has approved a three-factor formula on the grounds that it is a "widely accepted means for allocating" common costs. Order, Northern Illinois [*44] Gas Co., Docket 95-0219 at 33 (April 3, 1996). Indeed, in so holding, the Commission rejected Mr. Jenkins' identical recommendation for a two-factor formula. Rather, the Commission held that a three-factor formula including a revenue component should be used to allocate general expenses. Order, Northern Illinois Gas Co., at 33.

ComEd also disagrees with Mr. Jenkins' arguments that total assets rather than capital assets should be used in an allocation formula. ComEd acknowledges that the three-factor formula approved by the Commission in the NI-Gas proceeding used total assets rather than capital assets. ComEd contends, however, that there is no evidence that in the NI-Gas proceeding the Commission had before it a proposal to use capital assets rather than total assets in the three-factor formula. By contrast, in this proceeding Mr. Farmer explained why use of capital assets is preferable to use of total assets.

First, Mr. Farmer explained that use of total assets would create difficulties in applying the three-factor formula. Unlike capital assets, total assets include "a number of intangible or 'soft' assets such as goodwill." Thus, issues as to how to measure the value of [*45] these intangible assets arise when using total assets as a component--issues that do not arise with capital assets because such assets are usually tangible and can be valued.

Second, Mr. Farmer testified that use of total assets within the context of a three-factor formula that uses a revenue component would skew the allocation of Pool costs. Total assets includes accounts receivable--the end result of revenue recognition--which would mean that the revenue measure of size would be double-weighted and thus would not provide a balanced allocation formula. For this reason, Mr. Farmer testified that he is unaware of any proceeding that has adopted a two-factor formula using total assets and operating revenues.

Third, Mr. Farmer explained that the three-factor formula is made up of three components, only one of which is capital assets. The other two factors--gross payroll and operating revenues--give equal recognition to businesses with a large emphasis on labor or customer sales volume. Accordingly, the three-factor formula was designed to provide the most balanced method of allocating Pool costs. It was formulated without a specific result in mind and was devised to be the most fair [*46] means to allocate costs that have no cost causation component.

Finally, Mr. Farmer explained that Mr. Jenkins' recommendation does little to resolve Mr. Jenkins' concerns about the undue weight given to capital intensive businesses like ComEd. Because most of ComEd's total assets are capital assets, even if total assets were used in the three-factor formula, ComEd would receive a "high proportion of the allocation" of Pool costs in any case.

ComEd further argues that no witness supports the one-factor formula advocated by the AG and the City. Thus, there is no evidence on the record that would show whether that formula is appropriate to an electric utility and to ComEd in particular, or what its impact would be (although like every other size-based formula, it would likely allocate most Pool costs to ComEd since it has by far the most expenses). Moreover, the assertion by the AG that "the use of the FCC one-factor formula would establish a cost causative basis for the assignment of these costs since the direct costs assigned to the Parties under the Agreement would become the basis for allocating the Consolidated Pool costs" is wrong and has no record support whatever. Indeed, as shown, [*47] the record establishes that there is no true cost causative basis for the assignment of the Consolidated Pool costs.

B. Staff Position

Staff recommends two revisions to the method used to allocate Unicom costs to ComEd and its other subsidiaries. Staff recommends (1) that total assets should be used rather than capital assets and (2) that operating revenues should not be used at all. Thus Staff recommends use of a two-factor formula consisting of total assets and gross payroll. First, Staff argues that using capital assets as a factor to allocate general costs is obviously biased against a capital-intensive industry, and utilities are widely recognized as one of the most capital-intensive industries of all. According to Staff, use of capital assets as a factor would overallocate costs to ComEd and result in subsidization of Unicom's non-utility subsidiaries. Mr. Jenkins testified that most other utility holding companies examined use a total asset factor to allocate pool costs. Second, Staff argues that there is insufficient evidence to show that the revenue factor formula is appropriate for the circumstances within ComEd/Unicom or that the revenue factor is based [*48] on cost causation. Also, revenue-based allocations lead to the conclusion that an increase in ComEd's utility rates would simultaneously and directly cause an additional, iterative increase in ComEd's cost of service due to a higher allocation of Pool costs as a result of the relative increase in utility revenues. This is clearly illogical and demonstrates that the revenue-based allocation is not cost-based. Further, many of the non-utility ComEd affiliates are start-up or new ventures that are in the development phase whereby revenue will understate the actual management activities and focus occurring at those affiliates. Revenues would over-allocate costs to an established, mature business like ComEd and subsidize Unicom's start-up and developing ventures such as Unicom Resources, Unicom Thermal Technologies, Inc., and Unicom Technology Development, Inc.

Staff maintains that its proposal to use the gross payroll and total assets factors is directly related to cost causation at ComEd and Unicom and that the Commission should reiterate the costcausation principles advocated in the Order in Illinois Power, Docket 91-0147 (Feb. 11, 1992) by adopting Staff's proposal. Mr. Jenkins [*49] explained that asset and payroll-based factors satisfy the principles of cost causation because these factors either cause, are controlled by, or receive benefits from the items being allocated in the Consolidated Pool. For example, the assets of Unicom and ComEd must be financed by investors and this causes the cost for investor relations, SEC fees, stockholder reports, etc. that are included in the Consolidated Pool. Likewise, Mr. Jenkins testified that ComEd's and Unicom's employees, and the related payroll costs, are managed, directed and controlled by Unicom's executives, board and chairman. Sales, on the other hand, are not caused, controlled or benefitted by the functions included in the management fee. Thus, the asset and payroll factors do relate to the principles of cost causation, but revenues do not.

Staff further contends that its proposed rejection of the revenue factor is supported by an authoritative accounting text, *Cost Accounting: A Managerial Emphasis*, (Prentice Hall, Inc., 1977) by Charles T. Horngren. Staff also stated

that ComEd in this proceeding and NI-Gas in Docket 95-0219 could only cite to one 1964 case to support ComEd's contention that the three-factor [*50] formula is "widely accepted." Staff also notes that Mr. Farmer acknowledged that he knew of no utility that used capital assets as an allocation factor.

In its Brief on Exceptions, Staff reports that the Commission's recent Order in Docket 95-0353 for MidAmerican Energy Company adopted precisely the same allocation method that Staff has proposed for ComEd in this case. The Commission's Order specifically found that the revenue factor "does not reflect principles of cost causation."

C. Intervenor's Position

The AG, City and Cook County reference Staff's testimony concerning the inadequacies of the three-factor formula and argue that Mr. Jenkins' testimony demonstrates that the use of the three-factor formula would result in cross-subsidies. They contend that while Mr. Jenkins' two-factor formula is clearly superior to ComEd's proposed three-factor formula, it fails to account adequately for the fact that at least three of the parties to the agreement have no employees, no gross payroll, and necessarily have limited assets. Even with use of this formula, it appears that predominantly all of the Pool costs will be allocated to ComEd.

Intervenors recommend the adoption of the [*51] FCC's one-factor formula which uses the ratio of operating expenses of affiliated companies to allocate Pools of costs among the companies. Intervenors argue that the use of the FCC formula would establish a cost-causative basis for the assignment of these costs since the direct costs assigned to the parties under the Agreement would become the basis for allocating the Pool costs. They maintain that, given the characteristics of ComEd's affiliates, the one-factor formula is fairer than ComEd's three-factor formula. They argue that the record shows that for the foreseeable future, ComEd's affiliates will incur the majority of direct costs under the Agreement because they will be acquiring facilities and services from ComEd. Accordingly, the FCC's formula would allocate most of the common costs to ComEd's affiliates. This is fair because, as the evidence shows, it is the affiliates, and not ComEd and its ratepayers, that stand to realize the most benefits from the Agreement.

Further, Intervenors maintain that ComEd's citation to the Commission's recent order in Docket 95-0219, Northern Illinois Gas Company, for use of a three-factor formula should be given little weight. They argue [*52] that ComEd has failed to demonstrate that NI-Gas' transactions are with affiliates that are start-up companies with no revenue, no employees and little or no capital assets, as is the case here. A proper formula for allocating common costs is dependent on the circumstances and facts of the particular case and here the evidence demonstrates that use of either the three-factor formula or the two-factor formula, proposed by ComEd and Staff respectively, will result in cross-subsidies.

D. Commission Conclusion

The Commission finds that Staff's two-factor formula, consisting of gross payroll and total assets, is the fairest means for allocating common costs in the Consolidated Pool. Unlike ComEd's three-factor formula consisting of gross payroll, operating revenues and capital assets, Staff's proposal is directly related to cost causation at ComEd and Unicom. The Commission recently reiterated cost causation principles and adopted the same allocation method as is proposed by Staff here in Docket 95-0353 for MidAmerican Energy Company. The Commission agrees with Staff that operating revenues should not be a factor used to allocate common costs since this factor could understate [*53] the managements resources and attention devoted to new affiliates. Moreover, as we found in Docket 95-0353, it does not reflect principles of cost causation. The Commission also agrees with Staff that total assets rather than capital assets should be used since a capital asset factor is biased against the utility and could result in subsidization of Unicom's non-utility businesses. No witness supported the Intervenors' one-factor formula. Thus, there is no evidence on record that would show whether that formula, used at the FCC, is appropriate to an electric utility and to ComEd in particular or what its impact would be.

VIII. FILING AND APPROVAL OF THE COST ALLOCATION MANUAL

The AIA provides that the parties to the Agreement intend to develop and implement a set of guidelines to address specific applications of the general principles contained in the AIA. These guidelines will become the so-called "Cost Allocation Manual." The current draft of the Manual was admitted into the record as AG Cross Exhibit 8, by stipulation of the AG and ComEd. The Manual describes how the AIA cost allocation guidelines would be implemented.

A. Intervenor's Position

The AG and Cook County [*54] contend that in order to find that the AIA is in the public interest, and to fulfill its supervisory role, the Commission must examine the Cost Allocation Manual. They maintain that the AIA should not be approved by the Commission unless the Manual is similarly approved as part of the AIA or on a stand alone basis.

They argue that, pursuant to Section 4-101, the Commission is empowered with general supervisory power over all public utilities and is required to keep itself informed as to the manner and method in which business is conducted. They further argue that, according to Section 7-101(2), the Manual must be filed with the Commission because it is a report or record detailing transactions and expenses applicable to transactions with affiliated interests. Additionally, Section 7-101(3) requires ComEd to seek Commission approval before any "contract or arrangement" is made with any affiliated interest. Under these statutory provisions, Intervenor argue that the Commission must be provided access to all reports and records potentially related to transactions between a public utility and its affiliates. Moreover, no contract or arrangement between a public utility and an affiliated [*55] interest is valid unless it has been filed and approved by the Commission. According to Intervenor, within the confines of the instant proceeding, where the Commission has been requested to approve the AIA, the Manual that ostensibly details the implementation of that Agreement, should have been submitted for the Commission's review. They maintain that the Manual is in the nature of a "contract or arrangement" between the parties that unless "consented to or excepted by the Commission" is void. 220 ILCS 5/7-101(3).

Intervenor contend that the record shows that the Manual is an essential component of the AIA. In support of their contention, they cite the testimony of Mr. Jakubowski who indicated that the principal measures ComEd will institute to comply with Section 4.2 of the Agreement (Accounting) consist of the Manual, ongoing monitoring and annual internal audits. (ComEd Ex. 3 at 4). He indicated that the Manual being developed will include among other things, the business practices to be observed in the relationships between ComEd and Unicom and its other subsidiaries, detailed information regarding the nature and frequency of corporate support services that will be provided [*56] by ComEd to these entities and how these services will be accounted and budgeted for, a detailed explanation of the loading factors and how these will be applied, and other detailed procedures and instructions. (Id at 4-5).

Intervenor also cite the testimony of Mr. Farmer and Mr. Jenkins as support for their argument. Mr. Farmer testified that ComEd and its Unicom affiliates will maintain detailed methods and procedures that document how the AIA will be implemented and applied. (ComEd Ex. 2 at 15) According to Mr. Farmer, these guidelines provide the "how to" specifications necessary to ensure that the provisions of the Agreement are consistently understood and applied. (Id). Notably, Mr. Farmer recognized the Manual to be an important element and necessary for the Staff's oversight responsibilities to determine whether ComEd has, in fact, complied with the Agreement. (Tr. 353). In Mr. Farmer's words, it "explains to ComEd employees, and other interested parties, ultimately how the AIA's cost apportionment methodology will, in fact, be applied day to day." (Tr. 351). (Emphasis supplied).

Mr. Jenkins proposed that ComEd develop and maintain written guidelines for conducting, [*57] charging and allocating transactions between the utility and its non-utility affiliated companies. (Staff Ex. 1.0 at 11-12) (Emphasis in original). He testified that ComEd should inform all departments or individuals which may be involved in transactions with affiliated subsidiaries of such guidelines. (Id. at 12). To the extent that the testimony showed that ComEd has established policies and internal control and has prepared a Manual, he indicated that these practices should be continued and kept up-to-date. (Id. at 12). Staff needs to understand the procedures ComEd and its affiliated interests used to assign and allocate costs on books and records in order to determine if their actions were appropriate and reasonable. (Tr. 40).

Finally, Intervenor argue that with the absence of the incorporation of the Manual into the Agreement, it requires separate approval as an affiliated interest agreement if the AIA is approved. In support of this argument, they maintain that the instant Agreement is a two-way contract intended to govern transactions between ComEd and Unicom and its other subsidiaries. Since the AIA is a two-way arrangement, the Manual also must be a two-way arrangement [*58] requiring assent of all parties.

In order for the Manual to be established as the definitive implementation plan for all the parties to the AIA, Intervenor argue that it is necessary that the parties agree to the specifics contained therein and evidence their agreement to "observe and comply" with the details and procedures. This is not possible under the provisions of the Agreement as presently written. Thus, to give legally binding effect to the Manual, the parties will need to supplement their agreement by a written instrument signed by an authorized representative of each of the parties. And that supplement must be "consented to or excepted" by the Commission pursuant to Section 7-101(3).

B. ComEd's Position

ComEd maintains that the Manual is not properly a part of the Agreement and not before the Commission for approval. It asserts that (1) this Commission has never required the production and approval of an implementing cost allocation manual as a condition of approving an affiliated interest agreement; (2) the Agreement already is much more detailed than similar affiliated interest agreements of other Illinois utilities approved by the Commission; (3) although the [*59] FCC has required telecommunications carriers to file and seek approval of what it terms a "cost allocation manual", such a manual is the equivalent of, and contains even less detail with respect to affiliated transactions than ComEd's Agreement; and (4) the telecommunications carriers that file the so-called cost allocation manuals with the FCC keep more detailed implementation manuals that are equivalent to ComEd's Manual, and these are not filed with and approved by the FCC.

ComEd also asserts that it would be impractical and a mistake to be required to file its Manual for approval. By its very nature, it will be a constantly evolving document. Mr. Farmer testified that its more detailed methods and procedures will contain references to data sources and systems that change frequently, and if this additional detail were included in the Agreement, it would be necessary to amend the Agreement regularly as these references change, resulting in an unwarranted administrative burden on the Commission. (Farmer, ComEd Ex. 2 at 15; See also Jakubowski, Tr. 108 (the Manual is "almost like a living document that changes")).

ComEd contends that there is no record support whatever for [*60] Intervenor's position that the Cost Allocation Manual is an essential part of the Agreement and must be approved by the Commission. The Company argues that the testimony of every witness who addressed the issue--Mr. Jenkins of Staff and Messrs. Jakubowski and Farmer for ComEd--is to the contrary. (See, e.g., Jenkins, Tr. 43; Jakubowski, Tr. 107-08; Farmer, ComEd Ex. 2 at 15-16; Tr. 352-54). Nor can the AG explain how the Manual is an "essential" part of the Agreement and "must" be approved when this Commission has never required such approval for other utilities and when the record shows that no Commission--including the FCC--requires approval of this type of user's implementation manual.

Moreover, ComEd argues that the record shows that there are numerous "good reasons" for not incorporating the Manual into the AIA. The record shows that the Manual is currently incomplete, in draft form, and not approved by ComEd management. (AG/ComEd Stipulation 1 at 2; Jakubowski, Tr. 101). Mr. Farmer explained that the methods and procedures described in the Manual will contain references to data sources and systems that change frequently, some day to day. (Tr. 352). It is not realistic [*61] to think that such a Manual could ever work if even Staff, much less this Commission, had to approve such changes every time they were made.

ComEd further argues that this does not mean, as the AG contends, that the Commission will be unable to determine whether the Manual can, in reality, accomplish what the Agreement intends. Quite the contrary, what Intervenor ignores is the role the Staff can and will play as part of its oversight responsibilities with respect to the Manual. Mr. Farmer testified that "there is no question that the Staff as part of its ongoing oversight responsibilities would have a natural interest in the Manual to determine that ComEd has, in fact, complied with the affiliated interest agreement." (Tr. 353).

Moreover, Staff would have available in addition to whatever reviews it wishes to undertake, the periodic compliance audits of the cost allocation system that will be performed by ComEd's internal auditing group. (See Jakubowski, ComEd Ex. 3 at 5). Staff has specifically requested that the internal audits include written reports that ComEd would retain and make available for Staff's review. (Jenkins, Staff Ex. 1.0 at 12-13). Mr. Jakubowski has made [*62] clear that ComEd agrees with Mr. Jenkins' proposed condition. (Jakubowski, ComEd Ex. 8 at 2-3).

ComEd also contends that Intervenor is unable to provide any reason why Staff's exercise of its oversight responsibilities, and access to written reports of internal audits, are not fully adequate to ensure the compatibility of the Manual with the Agreement. ComEd contends that the Intervenor's argument that the Commission should separately review and approve the Manual because it is "necessary" that each of the Parties to the Agreement agree to the specifics in the Manual and evidence through a separate written instrument their agreement to "observe and comply" with these specifics, is without merit. ComEd asserts that this supposed necessity for a separate written instrument has been contrived by Intervenor in a transparent attempt to create an agreement among ComEd and the Unicom affiliates in addition to the AIA that the Commission would have to approve under Section 7-101(3). The Parties to the Agreement have agreed that they will develop and implement guidelines to address applications of the principles of the Agreement, but it does not follow that each affiliate must develop and [*63] implement the same guidelines and procedures. Indeed, there is no reason to believe, for example, that Unicom Thermal's books and records and employee procedures are the same or should be the same as ComEd's. Consistent with these facts, the Manual does not address how Unicom or ComEd's other affiliates will set up their own books and records. (Id.; AG/ComEd Stipulation at 1).

C. Commission Conclusion

Following a review of the evidence contained in the record and the arguments presented by the respective parties, we find that the Cost Allocation Manual is properly not a part of the agreement and not before the Commission for approval. This Commission has never required the production and approval of an implementing cost allocation manual as a condition of approving an affiliated interest agreement and the Agreement already is more detailed than similar affiliated interest agreements of other Illinois utilities. Intervenor's argument that the Manual is an essential component of the Agreement requiring separate Commission approval is without record or legal support and cannot be accepted.

IX. AIA's PRICING PROVISIONS

A. Intervenor's Position

The AG, [*64] City and Cook County argue that the Agreement fails to compensate ComEd for the value to the affiliates of their access to ComEd's skilled employees. They assert that all the parties to the Agreement are start-up companies. Three of the five affiliates have no employees. Moreover, although this Agreement has been presented as a two-way Agreement, only ComEd has substantial resources and for the foreseeable future all resources will flow in one direction - from ComEd to an affiliate.

Intervenor's note that ComEd has acknowledged that under the Agreement its affiliates will gain access to its skilled employees. They maintain that this access has value to the affiliates and will reduce their risk. Yet, there is no provision in the Agreement for the affiliates to compensate ComEd for this value. According to Intervenor's, by failing to negotiate for itself a payment for this value, ComEd has effectively transferred this value to its affiliates. Such a transfer is unfair to ComEd and its ratepayers since it constitutes a cross-subsidy flowing to the affiliates. It is also unfair to potential competitors of ComEd's affiliates that do not enjoy a similar subsidy in the provision of competitive [*65] services.

The City also contends that Mr. Bukovski acknowledged similar valuable benefits with respect to access to office space and other physical facilities. ComEd's affiliated start-up companies can avoid the need for full-time office space and other facilities by using only small units of space that are more desirable than those available on the open market. Edison Exh. 6 at 11-12. Without "as-needed" access to ComEd's office space and other physical facilities, the affiliates would have to obtain facilities elsewhere on more conventional terms--that is, discrete (not interspersed) space and without the volume discounts available to tenants as large as ComEd. Tr. 211. Additionally, the City also argues that the Agreement does not compensate ComEd for the costs that it has incurred in training, and may incur in replacing, employees who transfer to an affiliate.

Accordingly, the City recommends that ComEd should receive the greater of its fully allocated costs or the fair market value of its facilities and services, where the fair market value recognizes, at a minimum, the value to ComEd's affiliates of: its employees' experience; these employees' unique technical expertise; "as-needed" [*66] access to ComEd's personnel and facilities; avoidance of the risk associated with hiring new employees; and avoidance of the risk associated with guessing about the full range of facilities needed. The AG and Cook County propose that any Commission approval of the Agreement should be conditioned on requiring ComEd to negotiate for itself a payment for the value to its affiliates for providing them access to its skilled employees.

B. ComEd's Position

In response to Intervenor's arguments that the Agreement fails to compensate ComEd for the value to the affiliates of access to its skilled employees and for "intangible" benefits received by affiliates as a consequence of the Agreement, ComEd argues that there is no basis on this record or otherwise to require it to pay some additional compensation, above and beyond the fair market value of its services and facilities, for these evanescent "benefits" to the affiliates. ComEd notes that the Commission recently considered and rejected precisely the claim Intervenor's advance here. See Order, Illinois Power Co., Docket 92-0404 at 102 (Nov. 9, 1993). There the Commission found no basis for requiring IP's affiliate to compensate [*67] IP for the sorts of intangible benefits Intervenor's claim here, noting that the affiliate "will pay to IP the fully loaded costs of services provided under the Services and Facilities Agreement, and there is no evidence of record indicating that the method of compensation set forth in this Agreement is unreasonable." Id.; See also Southern California Edison Co., CPUC Dec. No. 88-01-063, 1988 Cal. PUC LEXIS 2, *55-57 (Jan. 28, 1988) (case cited by AG rejecting position that affiliates should be required to pay utility for intangible benefits).

ComEd maintains that every witness in this proceeding agreed that the Agreement's measure of compensation to ComEd already fully reimburses it for any intangible benefits it provides to its affiliates through the Agreement. For

instance, Professor Kamien testified without contradiction that the Agreement's cost allocation guidelines "properly attempt to replicate the workings of a competitive market to the greatest extent possible" because "ComEd never is required to sell its assets or services at a price less than what it would receive from other third parties in an arms-length transaction." (Kamien, ComEd Ex. 4 at 10-11). Mr. [*68] Bukovski testified without contradiction that "fair market value" as used in the Agreement included the "value" to affiliates from intangible benefits of the sort cited by Intervenor. (Tr. 208). And Mr. Farmer testified at length without contradiction that the Agreement's provisions guaranteeing ComEd payment of fair market value or fully distributed cost fully compensate ComEd for its facilities and services and thus prevent cross-subsidization. (Farmer, ComEd Ex. 2 at 9-12).

In response to the City's argument that ComEd should be provided "recruitment fees" for employees that transfer to an affiliate, ComEd contends that this theory is inconsistent with this and other Commissions' past decisions, contrary to accepted business practices in Illinois and elsewhere, and in any case unsupported by any record evidence. First, this Commission recently rejected precisely the claim advanced here. See Order, Illinois Power Co., Docket. 92-0404 at 19-20 (rejecting proposal of CUB witness that an affiliate should pay the utility for "training costs for employees and their accumulated experience" when an employee transfers from the utility to the affiliate). California came to precisely [*69] the same conclusion in Southern California Edison Co., CPUC Dec. No. 88-01-063.

Second, the City's theory is inconsistent with well-accepted business practices. As Mr. Farmer testified, "it's just not an accepted business practice" for a company to pay a recruitment fee when it takes on an employee from some other company. (Tr. 466). He explained that "the reason is because it's a normal part of business that employees will transfer from one entity to another" or that employees will "leave the company altogether." (Id.) Moreover, when an employee leaves ComEd for an unaffiliated company, the unaffiliated company does not pay a recruiting fee or any other form of compensation to ComEd. (Tr. 467) For these reasons, a business such as ComEd inherently factors into its labor costs the probability that some employees will leave before the business has "recouped" the full benefit of its training expenditures. (See Jakubowski, Tr. 93). And Mr. Jakubowski testified that ComEd does precisely that, through the labor load-factor. (Id.)

Finally, and dispositively, no record evidence supports the City's arguments. As discussed above, the only two witnesses to address this [*70] issue--Messrs. Farmer and Jakubowski--each testified that there was no basis to require affiliates to pay recruitment fees. (Farmer, Tr. 46-67; Jakubowski, Tr. 93).

C. Commission Conclusion

The Commission finds that there is no basis for modifying the Agreement on the grounds that it fails to compensate ComEd for intangible benefits provided to its affiliates. Uncontradicted evidence established that the AIA cost allocation methodology already compensates ComEd for the various types of intangible benefits to the affiliates cited by Intervenor. Likewise, the Commission rejects the City's argument with regard to recruitment fees for employees that transfer to an affiliate because it is without record support, is inconsistent with this Commission's past decisions and contrary to accepted business practices.

X. PUBLIC INTEREST CONCERNS

A. AG Position

In addition to the public interest arguments presented heretofore by the AG, City and Cook County addressing specific issues related to specific provisions of the Agreement, the AG and City also address public interest concerns based on the Agreement as a whole.

The AG contends that the AIA raises public interest [*71] concerns not encompassed within the four corners of the Agreement. The AG points out that there is virtually a complete overlap among ComEd's officers and directors and/or the officers and directors of each of the Unicom entities. See AG Cross Ex. 4. The AG argues that such a complete sharing of officers and directors between ComEd and the Unicom entities mandates even greater scrutiny on the part of Commission for this Agreement. Not only did the same person sign the Agreement on behalf of each party to the Agreement, all parties were represented by the same counsel. (Tr. 294). The City also shares these concerns.

Given these circumstances, the AG provides a review of applicable corporate law principles, particularly the fiduciary duties that are owed by ComEd's officers and directors. The AG maintains that these principles establish that each of ComEd's officers and directors owe ComEd their undivided loyalty in all of their dealings with ComEd and other corporations. Moreover, under the corporate opportunity doctrine, ComEd's officers are not permitted to deprive ComEd of business opportunities that it would be able to take advantage of or that are in its line of business. [*72]

The AG asserts that potential abuses of the business judgment rule and the corporate opportunity doctrine are supported by the record. Under the business judgment rule, the AG argues the following: (1) that issues concerning the three-factor formula for consolidated pool costs demonstrate that this methodology would not result in a fair apportionment of these costs and would not protect against cross-subsidies; (2) that issues concerning the draft Manual including the fact that Mr. Bukowski is responsible for the development of the AIA, is responsible for signing off on the final Manual to implement the Agreement, and also is responsible for conducting internal audits to determine whether the Manual is being followed do not lead to an audit the Commission can rely on for protecting ratepayers from affiliated interest abuses; and (3) that the Agreement's failure to include a "value" payment for the use of ComEd's skilled employees in addition to a payment for their direct and indirect costs results in a transfer of this value to affiliates.

With respect to the corporate opportunity doctrine, the AG maintains that under the AIA, ComEd's affiliates would be able to use ComEd's skilled [*73] employees, facilities, services, and real, personal and intangible property to develop business opportunities that become available. The probability exists that the affiliates would develop business opportunities that ComEd itself could pursue since they will be heavily reliant on ComEd's resources. These opportunities will be developed with ComEd's resources. Such business opportunities would be included within the doctrine.

Another area the AG suggests the Commission should consider is the potential that ComEd may develop intangible assets using its own R&D and then sell these assets to affiliates to turn into commercial products. The record shows ComEd has developed an energy storage system using a flywheel technology. (AG Cross Ex. 6). Mr. Bukovski testified the use of this technology for which ComEd conducted the R&D could be beneficial to ComEd. (Tr. 278).

According to the AG, the diversion of business opportunities from ComEd to its affiliates raises at least two issues regarding stranded costs. First, such a diversion appears to run directly counter to ComEd using all measures to mitigate potentially strandable costs. Second, if stranded costs are defined as revenues less [*74] costs, the level of calculated strandable costs will be higher than they would be as a result of revenue-producing opportunities being diverted to ComEd's affiliates. The AG argues that, in the absence of restructuring, abusive affiliated interest transactions have the potential to lead to higher rates and a degradation of service. With the potential restructuring of the industry Edison has the incentive to use the economies of scale and scope of its utility system, developed pursuant to its state-granted monopoly, to pursue business opportunities through its unregulated affiliates for the benefit of its shareholders while saddling its ratepayers with the maximum level of stranded costs.

The AG maintains that the potential harm to ratepayers that may result from Commission approval of the proposed Agreement is so great that the Commission is urged to consider outright rejection of the Agreement. However, should the Commission approve the Agreement, the AG recommends that the Agreement be conditioned so that it:

- (1) Ensures that ComEd will not be deprived of corporate opportunities that rightfully belong to the Company;
- (2) Demonstrates how any transactions under the Agreement [*75] will not frustrate the mitigation of "strandable" costs;
- (3) Provides to Commission Staff complete access to the books and records of Unicom and all of the other affiliates that are parties to the Agreement;
- (4) Provides for the filing of annual reports with the Commission detailing each transaction that is completed under the Agreement, including all information about that transaction required to demonstrate how it conforms with the Agreement's provisions, the Cost Allocation Manual, and the limitations set out in the Commission's order; and
- (5) Accepts as a condition of approval that the Commission can use the information gained from ComEd and its affiliates' books and records, from the annual reports, or from any other source, to modify or void any of the transactions completed under the Agreement when necessary in the public interest.

In addition, in order to ensure that in future proceedings this Commission can take all measures needed to protect ComEd's ratepayers from any adverse consequences arising from its approval of the Agreement, the AG urges the Commission to adopt another condition requiring that ComEd:

(6) Agree that any reapportionment of benefits or expenses, [*76] using those terms in their broadest sense, will not constitute a violation of the rule against retroactive ratemaking.

B. City's Position

The City also urges the Commission to scrutinize the Agreement carefully, contending that there is considerable doubt that the Agreement is in the public interest.

The City maintains that the record in this case makes clear that the parties that stand to gain most from approval of the Agreement are ComEd's affiliates and not ComEd or its ratepayers. The City quotes Mr. Bukovski's testimony wherein he explained the primary purpose of the Agreement was "to make effective use of the holding company system." According to the City, certain provisions of the Agreement specifically were designed to benefit Unicom. For example, Mr. Bukovski testified that the provision of the Agreement that would allow new parties to be added to the Agreement without Commission approval is necessary to permit "Unicom the flexibility to pursue business opportunities in an unregulated environment."

The City asserts that the record also shows that, despite the fact that the Agreement is a two-way arrangement, the overwhelming majority of services and assets that [*77] would be transferred would go in one direction - from ComEd to its affiliates, and in terms that may not return the full value to ComEd and its ratepayers. The City references Mr. Bukovski's testimony wherein he testified that ComEd's current and future affiliates will receive considerable, valuable benefits by having access to its employees and technical support and to its office space and other physical facilities.

The City also maintains that the areas of the Agreement that would allow the parties to pool resources to obtain more favorable commercial terms - joint purchasing and cash management - obviously benefit the other parties far more than ComEd. It argues that the other parties stand to benefit greatly by pooling their relatively meager resources with ComEd's billions of dollars in assets and revenues.

C. ComEd's Position

In response to the AG's arguments concerning violation of the business judgment rule and the corporate opportunity doctrine, ComEd contends that they are unsupported by anything but speculation, and they are based on a misunderstanding of the applicable law.

ComEd argues that, contrary to the AG's apparent belief, "the business judgment rule is. [*78] . . . a tool of judicial review rather than a standard of conduct." Block, Barton and Radin, *The Business Judgment Rule: Fiduciary Duties of Corporate Directors*, 3-4 (4th ed. 1993). The rule simply protects certain business decisions--those made by disinterested and independent directors on an informed basis in the good faith belief that the corporation will benefit from the decision--from being second-guessed by a court. According to ComEd, because the rule is not a standard of conduct, it simply is not possible for ComEd's directors to "violate" it; the rule applies to guide the courts' actions, not those of corporate directors.

In referring to the business judgment rule, the AG apparently means to rely on the various fiduciary duties owed by officers and directors to the corporation and its shareholders, primarily the duty of loyalty. Notably, the AG is unable to identify any breach of the duty of loyalty which is likely to occur, however, and merely speculates regarding the theoretical possibility that approval of the Agreement will give the directors an opportunity to breach their duties. Moreover, ComEd maintains that the AG improperly attempts to equate regulatory policies [*79] with fiduciary duties, which are owed only to the corporation and its shareholders, not to ratepayers. Thus, while regulatory policy may require ComEd to protect against cross-subsidization, ComEd's officers and directors have no fiduciary duty to do so.

ComEd further argues that the AG's discussion of the law of fiduciary duties, and the manner in which these duties might apply here, is misleading in other ways as well. The thrust of the AG's argument appears to be that because many of ComEd's officers and directors are also officers and/or directors of the Unicom entities, the ComEd officers and directors cannot be loyal to ComEd. The AG's apparent notion is that the duty of loyalty cannot be satisfied where one is a director of two affiliated companies. This is not the law. It is very common for parents and subsidiaries to have common officers and directors. Indeed, in providing a mechanism in Section 7-101 for reviewing agreements among entities with common officers and directors, the General Assembly obviously assumed that such relationships would occur.

Thus, the fact that certain of the ComEd officers and directors have fiduciary duties to the Unicom entities does not [*80] by itself create any breach or potential breach of fiduciary duty. Absent some evidence that they are preferring one entity over the other, the AG's fiduciary duty concerns are of no moment. There is no such evidence here, and the AG tellingly fails to cite any.

Moreover, ComEd asserts that the uncontradicted evidence in the record is that the common directors and officers have been mindful of their obligations to all parties. Mr. Bukovski testified that he took heed of the interests of all of the parties in discussions regarding the Agreement and that he directed the people involved to do what was fair for all the parties.

The AG cites nothing in the record to contradict Mr. Bukovski's testimony, but instead cites three "examples" of how cross-subsidization and supposedly a consequent breach of fiduciary duty may result from the Agreement. These examples include: (1) that the three-factor formula proposed in the Agreement will result in cross-subsidization of the unregulated businesses, (2) that Mr. Bukovski is somehow biased as a result of his involvement in developing the Agreement and the Manual and his responsibility for the internal audit function, and (3) that the absence of [*81] a "value" payment for the use of ComEd's skilled employees will result in cross-subsidization. ComEd maintains that these examples consist of nothing but speculation unsupported by any record evidence. Moreover, the bases for the AG's speculation in this regard have, for the most part, already been rejected by the Commission as previously discussed herein.

In response to the AG's suggestions of violation of the corporate opportunity doctrine, ComEd maintains that there is nothing in the record that would support a claim that any corporate opportunity belonging to ComEd has in fact been diverted, nor is there any basis for speculating that one will be diverted. "The corporate opportunity doctrine prohibits a corporation's fiduciary from misappropriating corporate property and from taking advantage of business opportunities belonging to the corporation." *Dremco, Inc. v. South Chapel Hill Gardens*, 654 N.E.2d 501, 504-05 (Ill. App. 1995). Accordingly, the doctrine applies when the "proposed activity is reasonably incident to the corporation's present or prospective business and is one in which the corporation has the capacity to engage." *Id.* at 505. ComEd argues that its business [*82] is to provide electricity, and Mr. Bukovski testified that the Unicom entities will be providing services other than the provision of electricity. As a result, the business opportunities in which the Unicom entities will be engaging are not "corporate opportunities" belonging to ComEd.

ComEd notes that the only specific item identified by the AG as a potential ComEd business opportunity which allegedly may be improperly diverted to a Unicom entity is a technology developed by ComEd and discussed largely during in camera proceedings. Not only has there been to date no transfer of this technology, but also the record is devoid of any evidence of whether the technology could in fact be developed into a commercial product by ComEd or whether the most likely commercial product to be developed from the technology would be for the utility market at all. These and other issues would have to be explored before there could be any claim under the corporate opportunity doctrine. Moreover, should ComEd propose such a transfer, the Commission and other interested parties would have ample opportunity to review the terms of such proposed transfer for consistency with the AIA and any other valid [*83] concerns under the Act.

Finally, in response to the issue of "strandable costs," ComEd argues that this issue has no bearing on the instant proceeding, which relates to ComEd's request for approval of the AIA. The issue of strandable costs is an issue which is being dealt with elsewhere by the Commission. It also has been the subject of legislative initiatives.

In response to the six conditions which the AG argues the Commission should place on approval of the Agreement, ComEd contends that they have no support in the record, are entirely unwarranted, and would place unfair conditions on ComEd that have not been imposed on any other Illinois public utility as a condition of approval of an affiliated interest agreement. Specifically, ComEd argues the following:

First, there is no support for the AG's speculative contention that approval of the Agreement could "deprive" ComEd of business opportunities. Therefore, the AG's suggestion that the Commission "ensure" that the Agreement will not result in such deprivation should be rejected.

Second, the issue of "strandable costs" is irrelevant to this proceeding and is more appropriately addressed in different proceedings and/or forums. In [*84] any event, the AG has failed to identify even a scintilla of evidence to support the claim that approval of the Agreement could, in any way, impact "strandable costs." Thus, the "demonstration" that the AG seeks is unnecessary and inappropriate.

Third, the AG has provided no explanation of the suggestion that Staff have complete access to the books and records of all affiliates that are parties to the Agreement. ComEd agrees that, pursuant to the Act, approval of the Agreement will obligate it to provide the Commission and its Staff with complete access to books and records of its affiliates that relate to transactions under the Agreement. ComEd is fully prepared to provide that access. However, if the AG intends something more than what the language of Section 7-101(2) provides, the Commission would exceed its authority by imposing such a requirement.

Fourth, there is no need for the annual reporting requirement suggested by the AG. Staff has not indicated that it needs annual reports in order to carry out its duties and obligations. Further, Staff and ComEd have entered into a stipulation which would require ComEd to submit a detailed report of all transactions with an affiliate [*85] one year after that affiliate becomes a party to the Agreement. In addition, Staff will have access to all of the books and records of ComEd's affiliates that relate to transactions under the Agreement.

Fifth, the AG's suggestion that transactions under the Agreement be subject to retroactive modification or voidness is utterly unjustified. The AG has provided no evidence whatsoever to support the need for such a condition. Further, such a condition would effectively render approval of the Agreement all but meaningless. Neither ComEd nor its affiliates could make decisions regarding a transaction with any certainty about the terms and conditions of the transaction.

Sixth, the AG's proposal regarding retroactive ratemaking is nonsensical in the context of this proceeding. The rule against retroactive ratemaking prohibits the Commission from adjusting rates prospectively to compensate for past deficiencies or excesses. It is, by its very nature, relevant only to proceedings that include the establishment of rates.

ComEd contends that the City's argument that affiliates will benefit more from the Agreement than ComEd is based on patent mischaracterizations of the record evidence. ComEd [*86] maintains that every witness said ComEd and its ratepayers would benefit from the Agreement because affiliates would be required to make contributions to ComEd's fixed costs that ratepayers otherwise would bear.

ComEd argues that the City's quotes of Mr. Bukovski's testimony that the Agreement will benefit the holding company system as a whole, do not remotely prove that the Agreement is "biased" against ComEd, for ComEd obviously is part of Unicom, and will benefit from being part of Unicom through contributions to its fixed costs.

Likewise, ComEd asserts that the City's contention that the majority of services and facilities will "go in one direction--from ComEd to its affiliates, makes no sense. ComEd argues that it could equally well be said that "the majority of the money will go in one direction - from the affiliates to ComEd." Because the evidence is overwhelming that ComEd will be fairly compensated for its provision of facilities and services, the City's statement says nothing about whether the Agreement is one-sided.

D. Commission Conclusion

The Commission finds that the public interest concerns expressed by Intervenors are speculative and are not supported by evidence [*87] in the record. The AG's arguments regarding the potential for a breach of loyalty by ComEd's officers and directors and potential abuses of the business judgment rule and the corporate opportunity doctrine are based on conjecture not evidence. Likewise, the City's argument that for the foreseeable future, the majority of services and facilities will go in one direction, from ComEd to its affiliates, and that makes the Agreement unfair to ComEd, is without merit. The record establishes that ComEd will be fairly compensated for those services. Accordingly, we conclude that the Agreement should be approved subject to the conditions, restrictions and modifications found appropriate herein.

XI. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having considered the entire record, and being fully advised in the premises, is of the opinion and finds that:

(1) Commonwealth Edison Company is an Illinois corporation engaged in the generation, transmission, sale and distribution of electricity to the public in Illinois, and is a public utility within the meaning of Section 3-105 of the Public Utilities Act;

(2) ComEd seeks approval of an Affiliated Interests Agreement between [*88] ComEd and its holding company, Unicom Corporation and Unicom's other subsidiaries: Unicom Resources Inc., Unicom Tech-

nology Development Inc., Unicom Enterprises Inc. and Unicom Thermal Technologies Inc., which establishes comprehensive policies and procedures for charges between ComEd and the Unicom entities for central management of certain services, the two-way provision of services, the sharing of certain facilities, the transfer of certain property and for other transactions;

(3) all of the companies listed in Finding (2) above are "affiliated interests" of ComEd within the meaning of Section 7-101 of the Act;

(4) the Commission has jurisdiction over the parties and over the subject matter of this proceeding;

(5) the findings of fact and law and conclusions thereon stated in the prefatory portions of this Order are supported by the evidence of record and are incorporated herein by reference;

(6) the conditions, restrictions and modifications found appropriate herein, including: the limitation on real estate transactions; access by Staff to all books and records of the AIA signatories; the Staff/ComEd stipulation for addition of new affiliates to the Agreement; and the adoption [*89] of Staff's two-factor formula for allocation of common costs are supported by the record;

(7) in accordance with Section 7-101(3) of the Act, nothing in this Order shall be construed to adopt, for ratemaking purposes, ComEd's methods for allocation of costs between ComEd and the Unicom entities or to remove ComEd's burden of proving in subsequent rate cases, as required by the Act and the Commission's Rules, the propriety of its allocation of costs between ComEd and the Unicom entities;

(8) the Agreement, appended to the Petition as Attachment A, is reasonable, is in the public interest and convenience, and should be approved subject to the conditions, restrictions and modifications found appropriate herein;

(9) all motions or objections which have not been ruled upon should be deemed disposed of in a manner consistent with the ultimate conclusions in this Order.

IT IS THEREFORE ORDERED that Commonwealth Edison Company is hereby authorized by the Commission to enter into the Affiliated Interests Agreement, appended to the Petition as Attachment A, subject to the conditions, restrictions and modifications found appropriate herein.

IT IS FURTHER ORDERED that ComEd shall modify [*90] the Agreement attached to the Petition as Attachment A as set forth herein and shall provide a copy of the amended Agreement to the Commission.

IT IS FURTHER ORDERED that nothing in this Order shall be construed to adopt, for ratemaking purposes, ComEd's methods for allocation of costs between ComEd and the Unicom entities or to remove ComEd's burden of proving in subsequent rate cases, as required by the Act and the Commission's Rules, the propriety of its allocation of costs between ComEd and the Unicom entities.

IT IS FURTHER ORDERED that any motions or objections not yet ruled upon are hereby deemed disposed of in a manner consistent with the ultimate conclusions reached herein.

IT IS FURTHER ORDERED that subject to the provisions of 83 Ill. Adm. Code 200.880, this Order is final; it is not subject to the provisions of the Illinois Administrative Review Law.

10/1

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Application)
of Utah Power & Light Company)
for (1) and Order Disclaiming)
Jurisdiction, or (2) in the)
Alternative for an Order Author-)
izing it to Form and Finance a)
Wholly Owned Subsidiary.)

CASE NO. 84-035-02

ORDER

ISSUED: October 1, 1985

Appearances:

S.G. Baucom
Ralph L. Jerman

For Utah Power & Light Company

Craig R. Rich
Assistant Attorney General

" Division of Public Utilities
Department of Business
Regulation, State of Utah

Brian Burnett
Assistant Attorney General

" Committee of Consumer
Services

Fred W. Finlinson

" UCIPP, Intervenors

By the Commission:

On June 26, 1984, the Public Service Commission entered its Order in the above matter authorizing the formation and financing of a subsidiary corporation under the laws of the State of Utah to be wholly owned by Utah Power & Light Company (UP&L). In that order, the Commission set for hearing the subjects of the proper relationship between the utility and its subsidiary, and the means to be employed to assure the continued operation of the utility in the public interest. Thereafter, the parties conducted discovery and prefiled testimony, and at the stipulation of the parties, the hearing date was continued until January 10-11, 1985.

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Hearings were held January 10 and 11, 1985, at which the Commission received testimony of Witnesses Colby and Bryner of UP&L, Huntsman of the Division of Public Utilities (Division), and Wilson for the Committee of Consumer Services (Committee).

In its written statements and in testimony presented before the Commission, UP&L indicated its position as follows:

First, while the parent is subject to the regulation of the Commission, the subsidiary, primarily engaging in qualifying projects as defined by PURPA and FERC regulations, should be generally free from regulatory burdens, so that it can effectively compete with other cogenerators and small power producers who are generally exempted from Commission regulation except when they enter into a power sales agreement with UP&L or seek wheeling.

Second, that the subsidiary was formed to take advantage of tax incentives not available to the parent as a public utility. The legislative history of PURPA as well as the administrative fact finding of FERC in making regulations strongly encourages the formation of subsidiaries by public utilities to engage in cogeneration, small power production and geothermal power production.

Third, the Commission does not have a specific statutory grant of jurisdiction to regulate the formation of a non-utility subsidiary, and since PURPA exempts state regulation of qualifying facilities, the Commission's regulatory authority extends only to the parent's involvement with the subsidiary.

Fourth, the Company does recognize that the Commission has legitimate concerns that the subsidiary not have a detrimental impact on the Company's regulated utility operation. In that respect, affiliated transactions will be subject to Commission review. However, the activities involving qualifying facilities are specifically exempted from Commission regulation to encourage the policy of developing alternative energy resources. Access to subsidiary records and personnel should be limited by the Commission to legitimate concerns about the economic well being of the regulated parent. By and large, if the subsidiary projects are successful, there would not be reason for regulatory interference with the subsidiary. That is not to say that the Company is not sensitive to appearances of fairness. However, as a practical matter, the subsidiary must compete with private enterprise, and any unnecessary burdens will limit its ability to compete.

Fifth, the framework of PURPA and the regulations are clear that the incentive benefits flow to shareholders of the utility in return for the risks associated with development of alternative energy. The Company has taken all prudent steps to insulate the ratepayers from detrimental aspects of alternative energy development by the subsidiary, including separate offices, and employees, and while filing a consolidated tax return, the calculations of taxes are on a stand alone basis, and dealings with the parent are on an arms length basis. Any incidental services performed by UP&L for the subsidiary will be billed to the subsidiary at a full recovery of cost price.

Sixth, the subsidiary will generally be involved primarily in alternative energy development either not available to, or not otherwise economical for the parent, but in a related venture area in which the parent has experience and is knowledgeable about the risks. Accordingly, the five percent upper limit for diversification recommended by the NARUC for non-utility investments does not necessarily fit in the UP&L subsidiary facts, and that this figure not be fixed at this time. There are benefits to the Utah ratepayers in having cogeneration or small power production projects with an ability to perform and to provide alternative resources that cannot be economically developed by UP&L, which in the case of hydro are environmentally sound and are very reliable.

Seventh, where the Commission appropriately sets the avoided costs in the Utah jurisdiction, the ratepayers should be indifferent to who generates electricity from qualifying facilities, and the Commission should not be concerned that, because of the subsidiary's involvement, the UP&L shareholders earn a higher rate of return on the subsidiary's investment in PURPA qualifying facilities for which they take a higher risk. Nevertheless, UP&L will continue to examine each generating opportunity of whatever form and make its own determinations on whether to pursue new construction or to purchase existing generating facilities depending upon the need and economic benefit to UP&L and the ratepayers.

Eighth, the financing of investment capital for the non-utility investment of the parent in the subsidiary will not impact UP&L's capital structure, and there is no capital structure effect for ratemaking purposes. Losses incurred as a result of participation in the subsidiary will be borne solely by the shareholders, not the ratepayers.

Ninth, while the subsidiary will be interested in the avoided cost rates set by the Commission, neither the subsidiary nor UP&L will seek any adjustments in the avoided cost determinations or in the terms and conditions of standard form contracts approved by the Commission because of that interest. Contracts between UP&L and the qualifying facility in which the subsidiary is involved as an investor will be on the same basis as other cogeneration and small power production agreements. Line losses will be credited on a case by case basis determined by computer simulation, and line extensions will be made on a contribution-in-aid of construction basis. The subsidiary's involvement in a qualifying facility will not change the method of determining such credit or costs. Wheeling will be considered on a case-by-case basis for any cogenerator or small power producer, and no advantage will be given to projects in which the subsidiary is involved.

Tenth, if a project has been studied by UP&L and is transferred to the subsidiary, all of the related or associated costs incurred by UP&L will be billed to the subsidiary. If a

major project by UP&L is determined to be more economically advantageous for the subsidiary to develop because of risk factors, tax benefits, or capacity questions, UP&L would be willing to advise the Commission prior to transferring the future development to the subsidiary for a determination on allocation of costs and to meet any of the Commission's concerns.

The Committee presented testimony by Dr. John W. Wilson who generally agreed with the Division's fifteen recommendations regarding the guidelines the Public Service Commission should adopt when allowing UP&L to diversify through the activities of their subsidiary, Energy National, Inc. (ENI). Dr. Wilson testified regarding general areas of concern he had with diversified activities of any utility. The Division's proposals presented by Wesley D. Huntsman satisfy many of the concerns Dr. Wilson had regarding accountability and proper access to information so that the activities of the subsidiary will not have an adverse impact on the ratepayers of Utah.

Dr. Wilson also had certain specific concerns that were not addressed by the Division's recommendations. These are as follows:

1. That the Committee should have access to the reports and documents provided to the Public Service Commission and the Division pursuant to the Division's guidelines so that the Committee can ascertain the impact the subsidiary is having on the ratepayers.

2. That the profits of ENI be limited to the current authorized rate of return for UP&L and the profits over and above that authorized rate be returned to UP&L and the ratepayers of Utah. This policy recognizes the risk that the UP&L ratepayers have if the project fails and the impact such a failure would have on the rates. This policy also recognizes that there will be some trading of information between UP&L and ENI regarding potential projects. Dr. Wilson felt that there would be no actual or true "arms length" competition for potential projects because of the conflicts which exist for officers and employees of UP&L sitting on the board of directors for ENI. These people have knowledge regarding projects both companies would be competing for and cannot make impartial decisions about the development of the projects. The projects UP&L could develop itself, will be developed instead by ENI who has certain tax advantages and the ratepayers of Utah will not be able to benefit from the profits unless the profit sharing approach is implemented.

3. That UP&L be properly compensated by ENI for services and technology that were transferred and will be transferred from UP&L to ENI. The \$120,000 figure listed by UP&L for all setup costs for ENI was too low and ENI received far greater benefits than the \$120,000 listed. The services provided by UP&L were priced well below market price and market prices need to be charged in the future for any service or information UP&L transfers to ENI. Also, UP&L was not properly compensated for

information transferred to ENI regarding 43 projects that were investigated by UP&L.

The Division's Witness Wesley D. Huntsman made the following recommendations:

(1) "The investment in the unregulated portion of the consolidated enterprise should not exceed five percent of the total Applicant's assets." This recommendation is based upon the NARUC Ad Hoc Committee on Utility Diversification recommendation that the non-utility investment not become large enough to place significant risk on ratepayers.

(2) "Employees, officials, directors or agents of the subsidiary should be available to testify before the Commission as required." This recommendation is also based upon the NARUC study, where the regulator's may have a need to investigate potential financial questions which involve utility operations.

(3) "The subsidiary books, records, and other relevant documents should be available for Public Service Commission and Division access when requested, subject to protective order if necessary." This recommendation is similar to item (2) above.

(4) "Commission approvals of contracts with 'qualifying facilities' will be conditioned upon adequate access to relevant books, records and officials of the partnership with which the subsidiary is affiliated." This recommendation is similar to item (2) above.

(5) "The subsidiary should be required to maintain a complete set of transactions and financial records in Utah." This recommendation indicates a concern that out of state projects may have financial impacts on UP&L and records should be maintained in Utah where it will be easier to access for regulatory review purposes.

(6) "The Applicant should be required to file quarterly and annual financial statements of the subsidiary." This recommendation is based upon the NARUC study which reports that accounting methods are not entirely adequate to provide adequate information about the regulated utility and non-regulated activities, so that a continual monitoring system should be required.

(7) "The Applicant should be required to allocate any costs incurred for which a benefit accrues to the subsidiary, and utilize generally accepted cost accounting standards." This recommendation is based upon the NARUC report, and necessitates the use of timekeeping and project management systems adequate to support cost allocations for review in utility rate cases.

(8) "The Applicant should be required to implement timekeeping and project management systems adequate to support the allocation of costs." This recommendation is similar to item (7) above.

(9) "The Utility should be required to obtain Commission approval before lending any funds to the subsidiary,

and interest rates should exceed the utility's current cost of debt or authorized return on equity, whichever is higher."

(10) "The Applicant should be required to account for the diversified activities in accordance with procedures outlined in the FERC system of accounts, until and unless those procedures are modified by the Commission."

(11) "The Applicant should be required to fund the subsidiary entirely from investor supplied capital and authorize income taxes to be computed on a 'stand-alone' basis."

(12) "The Applicant should be required to account for the investment in the subsidiary in Account Number 123.1, 'Investment in Subsidiary Companies', and account for any dividends declared by the subsidiary through the same account."

(13) "The Commission should reserve the right to hear and resolve complaints of conflicts between subsidiary activities and the public interest." This recommendation is based upon the Division's concerns of possible conflicts between the interests of the ratepayers and those of the utility shareholders where a generating facility could conceivably be constructed by either the parent or the subsidiary, where wheeling is requested by competing small power producers and capacity is restricted, or if there were market dominance by the parent.

(14) "The Commission should retain the flexibility to change strategies or rulings regarding the Applicant's diversification if circumstances dictate." This recommendation is based upon the relative lack of experience of Utah regulators in dealing with diversification by utilities and concern about preserving the ability of regulators to protect the public interest.

(15) "The Commission should require periodic review of the operation of the subsidiary by an independent entity or the Division to determine if any of the circumstances relevant to approval of the diversification have changed."

During the course of the proceeding, the Division clarified and modified its recommended guidelines as follows:

(a) The Division clarified its position regarding recommendation No. 5 by stating that the requirement to keep a complete set of records and transactions in Utah would not include such things as a complete set of transactions of projects outside Utah.

(b) The Division modified recommendation No. 6 to the extent that if consolidated financial statements are filed monthly, and if the consolidating worksheets are available for examination, the filing of quarterly and annual financial statements would not be necessary.

(c) Recommendation No. 12 was modified to consider the possibility that the Uniform System of Accounts may be modified in the future. The requirement is intended to follow any changes in the Uniform System of Accounts.

The Commission having been fully advised in the premises, now makes this Report containing the following Findings of Fact and Conclusions of Law, together with the Order based thereon.

FINDINGS OF FACT

1. UP&L has organized a subsidiary, Energy National Inc., in accordance with the Commission's prior order in this matter, and has billed the same for direct costs incurred, which costs should not be recovered from utility ratepayers.

2. There is no evidence that indicates that there is an immediate, quantifiable effect on the rates of UP&L or on its ability to provide adequate service as a result of forming the subsidiary. The Division did not know what the long-term impact would be, but asserted that the public interest will be served by UP&L's participation in alternative energy development through a PURPA subsidiary and the Commission would have the regulatory authority in the future to protect the ratepayers' interests.

3. While the formation of the subsidiary will not have an immediate impact on rates or service, it does pose additional complications for regulators. It has been the Commission's experience that additional difficulties can arise in the regulation of public utilities when affiliated with non-utility operations. Because the Commission must retain its ability, both jurisdictionally and practically, to regulate public utilities effectively and in the public interest, it is appropriate to consider and to act to minimize any such difficulties that may

result from diversified activities, such as the creation of the subsidiary.

4. Substantial involvement in non-utility activities changes the risk characteristics of the corporate entity. Unsuccessful non-utility ventures could affect the parent and ultimately the financial condition and cost of capital for the utility corporation. Additional complexities are created in the obtaining of sufficient information to ensure adequate and informed regulation. Potential conflicts of interest exists between affiliated entities, particularly when the activities of a non-utility affiliate are the same as or similar to activities of the utility. Transactions and allocations between affiliates create numerous opportunities for unfair treatment and must be adequately reviewed by regulators. The Commission finds it necessary and convenient to address these general concerns and to ensure that information access be adequate to enable the Commission to regulate the utility parent.

5. The Commission finds that the general guidelines proposed by the Division and modified herein are a good "first step" in meeting our concerns about diversification through the subsidiary operations. We find that such guidelines are of assistance in protecting the financial integrity of the utility parent, ensuring fair dealings between affiliates and assisting in the Commission's practical ability to regulate the utility corporation. We find that the Division's recommendations, as modified, are an appropriate starting point.

6. The Commission has previously determined that the investment in the subsidiary will not adversely affect ratepayers, at least in the near term. However, the long-term effect on ratepayers is not ascertainable and for this reason, as well as those above stated, the Commission will require UP&L to meet the minimum standards set forth herein.

7. The Commission finds the primary purposes of these minimum standards is to avoid cross subsidization of the subsidiary by the present and to maintain the Commission's ability to assess the impact of the subsidiary operator on the financial ability of UP&L to continue to serve the public interest as a regulated electric public utility. In order to assess impacts, we must retain the ability to hold hearings and assess evidence, and we must retain the ability to require action which will protect the ratepayers and the public interest.

8. The Commission finds that the Committee should have access to all reports and documents provided to the Public Service Commission and the Division as specified in the Division's proposed guidelines.

9. The Commission finds inadequate evidence on the record in this case to support the position of the Committee that UP&L was not properly compensated by ENI for the information transferred to ENI regarding 43 projects that were investigated by UP&L.

CONCLUSIONS OF LAW

1. The role of utility regulation is to ensure that

management decisions do not impair the ability of the utility to fulfill its statutory duties. These may be summarized as the duty to provide reliable, safe and adequate utility service at just and reasonable rates. To the extent that decisions of a regulated public utility company's management may impair the efficient discharge of its statutory duties, such decisions may be deemed adverse to the public interest and corrective actions are appropriate and within the powers of this Commission. The Commission's role with respect thereto is limited, but important. For this reason, the jurisdictional authority of the Commission is set forth below.

2. The Utah Supreme Court has commented on the duty to protect the public interest in cases of diversification. See Utah Department of Administrative Service Commission, ("Wexpro II"), 658 P2d 601 (Utah 1983) and Committee of Consumer Services v. Public Service Commission, ("Wexpro I"), 595 P.2d 871 (Utah 1979). In Wexpro I, the Court stated:

[I]t is the duty of the public utility corporation to operate in such a manner as to give to the consumers the most favorable rate reasonably possible. This duty stems from the fact the State has conferred on the utility the exclusive right to sell and distribute gas. As a consequence, the utility bears a trust relationship to its customers and must conduct its operations on that basis and not as though it were engaged in a private enterprise with no restrictions as to its income.

595 P.2d at 874. In clarification of this trust relationship, Justice Oaks stated in Wexpro II:

This Court's references to MFS's "trust relationship to its customers," 595 P2d at 874 and 876, have been productive of

considerable confusion. The single judicial authority cited for this reference unquestionably used those words not in the technical sense of property owned in trust for another That statement is simply an expression of the utility's legal responsibilities to make "just and reasonable" charges for its services and to assure that those services are "in all respects adequate, efficient, just and reasonable" (Citation omitted)

This clarification is not intended to minimize the extent of MFS's duties to its customers. Those duties are extensive, and they are enforceable. The Commission is empowered to "supervise and regulate every public utility in this state, and to supervise all of the business of every such public utility." §54-4-1, including the fixing of rates. U.C.A., 1953, §54-4-4. We have often said that the Commission is responsible to exercise its statutory powers over utilities to assure "that the public receives the most efficient and economical service possible." (Citation omitted). The fixing of rate presupposes "efficient and economical management." (Citation omitted). Although the Commission is normally forbidden from intruding into the management of a utility, we have suggested that it can do so where "the policy and consequent expenditure is actuated by bad faith, or involves dishonesty, wastefulness, or gross inefficiency." (Citation omitted). These powers are surely sufficient for the Commission to ascertain and correct wasteful or grossly inefficient business practices by utilities in order to enforce what Wexpro I referred to as "the duty of a public utility corporation to operate in such a manner as to give to the consumers the most favorable rate reasonably possible."

658 P.2d at 618.

Moreover, on remand from Wexpro I, the Commission recognized the issues involved in utility diversification and consequent company reorganization and formulated its respective policy:

[T]he Commission recognizes the advantages and disadvantages which may follow utility investment in non-utility ventures. Some of the problems which concern us are noted in the 1972 Report of the Ad Hoc Committee on Non-Utility Investments - Diversification by Utility Companies, of the National Association of Regulatory Utility Commissioners.

The crucial question is whether diversification by public utilities poses a threat to the basic investment-revenue cycle. For now, only the most obvious aspects need to be noted. If utility resources are devoted to non-utility operations, no major problem is presented if either: (1) The non-utility enterprise is as profitable as the utility enterprises; or (2) the non-utility enterprise is of insignificant scale in comparison with the utility enterprise. In either event, utility revenues will support new utility investments, in a continuing cycle. The utility's investors may gain some extra profits in the first instance, and may sustain some losses in the second instance, but the interest of the public is not adversely affected in serious degree in either case. On the other hand, if the non-utility investment is both substantial and unprofitable, there is risk of disruption of the investment-revenue cycle. An enterprise with a substantial and unprofitable non-utility operation has only two options: (1) it can increase revenues of the utility business sufficient to cover the losses on the non-utility business and thereby maintain the flow of needed capital; or (2) it can refuse to support the unprofitable non-utility operation by such a subsidy from the utility operation which would mean that the enterprise as a whole would be unprofitable and unable to attract capital on reasonable (or perhaps any) terms.

The end result is precisely the same as in those situations in which utility investments were diverted to promoters' pockets or utility revenues were diverted to affiliated interest.

It should be noted that even if non-utility operations are profitable, there may

be political difficulties in retaining an effective investment-revenue cycle. Confronted with an enterprise with good overall profitability (resulting from its non-utility ventures), the public may be unusually resistant to permitting rate increases, even if they clearly are warranted by the investment and revenue requirements of the utility operation. An analogy is the apparent expectation of consumers of some AT&T operating subsidiaries that the parent, through its nationwide operations, should support losing operations of the subsidiaries.

The Commission believes the utility business of MFS is the cornerstone of its operations; other activities must enhance and not jeopardize that cornerstone. It is for these reasons that the Commission is vitally interested in company restructuring, which is in effect diversification or functional separation. We believe Utah statutes authorize Commission review of such proposals, and the setting aside or modification of same, if after a hearing, the scheme itself, or its logical or intended consequences, are found to be detrimental to the utility cornerstone or injurious to the public interest.

In Wexpro II at 617, the Supreme Court expressly upheld the Commission's reasoning on jurisdiction as set forth above:

We find no error in the Commission's conclusions on these important jurisdictional matters. (Citation omitted).

We therefore conclude that the Commission possesses requisite jurisdiction to approve, modify or prevent corporate reorganizations which are found by the Commission to be detrimental to the public utility or injurious to the public interest. In addition, the ability to protect the public interest is not lost by approval of a reorganization. We also conclude that even after approval of the creation of the subsidiary, if subsequent operations are found by the Commission to be detrimental to the

utility or injurious to the public interest, the Commission possesses authority to take appropriate action to protect the public interest and the utility operations of the corporate entity. Changes in corporate organization do not defeat the jurisdictional grant of authority to the Commission to regulate utilities in the public interest.

3. Based upon the evidence presented, there being no immediate impact upon rates or the quality of service, we conclude that the present and proposed operation of the subsidiary is consistent with the public interest.

4. In order to ensure that the subsequent activities in connection with the subsidiary remain in the public interest, it is necessary to the exercise of our jurisdiction over public utilities to establish guidelines intended to govern the relationship between the utility corporation parent and its subsidiary affiliate. The Commission therefore concludes that guidelines suggested by the Division in general are appropriate to assist in protecting the public interest and should govern the relationship between UP&L and Energy National, Inc. Such guidelines, as modified, are not unduly burdensome and will assist in defining and determining reasonable intercorporate dealings.

5. The Commission concludes that its power to obtain information necessary for the effective regulation of public utilities is not affected by the proposed accounting treatment of the subsidiary or its separate incorporation. The Commission's powers to obtain information are set forth in Section 54-7-4.5,

U.C.A. (1983 Amend.), and the Commission may thereunder require production by any company of any documents or information relevant to any matter before the Commission, whether said documents or information are in the possession of UP&L or the subsidiary, or any other company.

6. The Commission concludes that the existence of the subsidiary has no effect on the ability of regulators to review allocation of common costs between the utility and its subsidiary or to review the capital structure of the utility to ensure that the components of capital remain at reasonable levels.

7. The Commission concludes that limiting the rate of return of ENI to the currently authorized rate of return for UP&L would not be consistent with existing case law or the intent of PURPA. ENI has been set up to attempt to develop PURPA projects and as such would be receiving its return on investment by way of avoided cost rates determined by this Commission or another State Commission. The so called "no profits to affiliates" rule or the "California approach" are not applicable to the operations of ENI on PURPA projects.

ORDER

NOW, THEREFORE, IT IS HEREBY ORDERED that:

1. The approval previously granted for the formation and financing of the subsidiary is conditional, as indicated in the prior order, on the Commission's ongoing ability to regulate the public utility operations. At a minimum, and subject to future modification, Commission approval of the formation and

operation of Energy National, Inc. is conditioned on adherence to the following guidelines:

- o (1) The investment in the unregulated portion of the consolidated enterprise will not exceed five percent of the total assets of the Applicant without prior Commission approval.
- o (2) Employees, officials, directors or agents of the subsidiary will be available to testify before the Commission as required.
- o (3) The subsidiary books, records, and other relevant documents will be available for PSC and Division access when requested, subject to protective order if necessary.
- o (4) Commission approvals of contracts with "qualifying facilities" will be conditioned upon adequate access to relevant books, records and officials of the partnership with which the subsidiary is affiliated.
- o (5) The subsidiary will be required to maintain a complete set of financial records in Utah.
- o (6) The Applicant will be required to file monthly consolidated financial statements, and shall make available to the Commission and the Division, when requested, consolidating worksheets.
- o (7) The Applicant is required to allocate any costs incurred for which a benefit accrues to the subsidiary, and utilize generally accepted cost accounting standards.

- o (8) The Applicant is required to implement timekeeping and project management systems adequate to support the allocation of costs.
- o (9) The utility is required to obtain Commission approval before lending any funds to the subsidiary, and interest rates should exceed the utility's current cost of debt or authorized return on equity, whichever is higher.
- o (10) The Applicant is required to account for the diversified activities in accordance with procedures outlined in the FERC system of accounts, until and unless those procedures are modified by the Commission.
- o (11) The Applicant is required to fund the subsidiary entirely from investor supplied capital and authorize income taxes to be computed on a "stand-alone" basis.
- o (12) The Applicant is required to account for the investment in the subsidiary in Account Number 123.1 "Investment in Subsidiary Companies," and account for any dividends declared by the subsidiary through the same account. In the event the Uniform System of Accounts is modified, this requirement will follow the modified system of accounts, unless there is an order to the contrary by the Commission.
- o (13) The Commission reserves the right to hear and resolve any complaints of conflicts between subsidiary activities and the public interest.

- o (14) The Commission will retain the flexibility to change strategies or rulings regarding the Applicant's diversification if circumstances dictate.
- o (15) The Commission will require periodic review of the operations of the subsidiary by an independent entity or the Division to determine if any of the circumstances relevant to approval of the diversification have changed.
- o (16) The Applicant will notify the Commission prior to transferring any project or project information to ENI and will provide a description of the project as well as all of the related or associated costs incurred by UP&L to be billed to the subsidiary.

2. The reports and documents provided to the Commission and the Division pursuant to the Division's guidelines will also be provided to the Committee of Consumer Services.

DATED at Salt Lake City, Utah, this 1st day of October, 1985.

/s/ Brent H. Cameron, Chairman

/s/ James M. Byrne, Commissioner

(SEAL)

/s/ Brian T. Stewart, Commissioner

Attest:

/s/ Georgia B. Peterson
Executive Secretary



14 of 99 DOCUMENTS

In the Matter of the Revised Tariff Schedules for Electric Service in Oregon filed by
PORTLAND GENERAL ELECTRIC COMPANY.

ORDER NO. 95-322; UE 88

Oregon Public Utility Commission

1995 Ore. PUC LEXIS 45

March 29, 1995, Entered

PANEL: [*1] Ron Eachus, Commissioner; Roger Hamilton, Commissioner; Chairman Smith concurs in part and dissents

OPINION: ORDER

SUMMARY

This order approves new rate schedules for Portland General Electric Company (PGE). Under the new schedules, PGE's rates increase approximately 5.8 percent overall. PGE's original filing, which included a proposal to accelerate the Boardman gain amortization, sought an increase in revenues of \$ 58,974,927 for 1995, and \$ 60,783,781 for 1996. PGE subsequently withdrew its Boardman proposal, which increased the company's revenue need to \$ 92,275,240 in 1995 and \$ 95,105,468 in 1996. In this order, the Commission grants PGE an increase in revenues of \$ 50,970,243 for 1995 and \$ 51,812,359 for 1996.

Undepreciated Trojan Investment. The dominant issue in this docket is the allocation of undepreciated investment and other costs resulting from the premature closure of the Trojan Nuclear Power Plant (Trojan).

In January 1993, PGE retired the 1200 megawatt (MW) plant, which was licensed to operate until 2011. Degradation of the plant's steam generator tubes led PGE to retire the plant 19 years before the expiration of its 35-year license life. As of January 1, 1995, [*2] PGE's net undepreciated investment in Trojan totaled approximately \$ 288 million. In this proceeding, PGE seeks full recovery of and return on that undepreciated investment, plus other costs related to service.

We reject PGE's request for full recovery of Trojan costs. We conclude that the allocation of the Trojan costs is properly determined by a "net benefits" analysis. A net benefits analysis compares the costs of a plant's continued operation with the costs associated with retiring the plant plus the expected long-term costs of replacing the plant's output. The purpose of a net benefits test is to identify the point at which ratepayers are indifferent between the options of continued operation of Trojan and shutdown and construction or acquisition of replacement resources.

Full recovery of undepreciated Trojan costs is not guaranteed to PGE, nor is it required of the Commission. Granting full recovery in rates where there is not a net benefit to ratepayers would insulate the utility from risk no matter what its actions. On the other hand, granting no recovery of undepreciated investment would not encourage PGE to engage in prudent management and responsible least-cost planning, [*3] goals the Commission wishes to promote. The net benefits analysis is a tool to determine where ratepayers are held harmless for imprudent operation or management of Trojan, and to share costs between ratepayers and shareholders on that basis.

The Commission staff (staff) conducted a net benefits analysis, using PGE's least-cost plan (LCP) as a starting point. The final result of PGE's least-cost planning process indicated that immediately closing Trojan was the least-cost op-

tion. The LCP, however, considered the plant as it actually existed and projected those costs forward to 2011. To determine whether there was a net benefit to ratepayers from closing Trojan, staff sought to determine whether the costs on which PGE's least-cost planning process was based would have been allowed in rates. If PGE's LCP projections were based on costs that had been driven up by management problems, for instance, the net benefits analysis would disallow the costs if they were imprudently incurred.

Staff hired an independent consulting firm, Theodore Barry and Associates (TBA), to evaluate whether the costs of operating Trojan were prudently incurred. TBA assessed the reasonableness of PGE's operation [*4] and management of Trojan from the plant's initial commercial operation in 1976 through its current delicensing and decommissioning activities. TBA explored Trojan's comparative performance, reviewed management issues, and analyzed the steam generator issue. Its examination focused on whether PGE's actions, based on all the information PGE knew or should have known at the time, were reasonable and prudent in light of all the circumstances. TBA did not base conclusions on hindsight or knowledge acquired after the fact, and recognized that one or more courses of action may be reasonable in a given set of circumstances.

TBA also quantified the effects of PGE's management and operation deficiencies, and staff projected TBA's figures out over the period from 1995 to 2011, a period beginning with the first test year in this rate case and running through Trojan's originally scheduled closure. Staff compared these imputed costs with the cost of replacement resources to determine whether there was a net benefit from closing Trojan.

After an examination of the net benefits analysis, we conclude that the premature closure of Trojan resulted in a negative net benefit of approximately \$ 20.4 [*5] million. We find that continued operation of Trojan would have cost less than immediate shutdown but for steam generator defects and management problems at Trojan. Management problems resulted in avoidable costs that should be borne by shareholders, not ratepayers.

We adopt TBA's finding that PGE behaved prudently with respect to the steam generator degradation. However, we disallow the steam generator costs incurred since 1991 and exclude the cost of replacing the steam generators from the imputed costs of running Trojan in the net benefits analysis. Although PGE's behavior was not faulty, PGE and the ratepayers are the only two parties to whom we can assign or impute steam-generator costs. As between those two parties, PGE is better situated to recover its costs from the manufacturer of the steam generators. Moreover, it is fair that shareholders bear some of the consequences of management investment decisions.

To hold PGE's ratepayers harmless for the effects of steam generator defects and management failures, we are disallowing recovery in rates of \$ 20.4 million of the company's remaining investment in Trojan.

Post-1991 Capital Expenditures. We also disallow PGE's post-1991 [*6] capital expenditures to repair Trojan's steam generators and costs for the purchase of a spare nuclear reactor coolant pump. Although we find that PGE acted prudently with regard to its maintenance and operation of the steam generators, PGE is better situated to pursue remedies for any manufacturing defects against Westinghouse, the steam generator manufacturer, than are the ratepayers. PGE's purchase of the spare reactor coolant pump was not prudent and will not be allowed in rates. These disallowances total an additional \$ 17.1 million, for a total Trojan-related disallowance of \$ 37.5 million.

These conclusions result in a disallowance of 13.0 percent of the remaining Trojan costs, which will be borne by shareholders, not ratepayers. That result approximates a scenario in which Trojan was reasonably operated and managed. In the main, the disallowances correct for avoidable costs.

Decommissioning and Transition Costs. In this order, we also approve funds to decommission Trojan and to pay for the transition to shutdown. Decommissioning costs are the costs of physically dismantling the plant and packaging and storing the radioactive components and spent fuel. Transition costs [*7] are the operations and maintenance (O&M) and administrative and general (A&G) costs associated with plant closure.

PGE would incur decommissioning and transition costs regardless of when the plant was taken out of service, and the company has already been paying into a decommissioning fund. Because Trojan was shut down before the end of its license life, however, payments into the fund will have to increase for a time. Even with the increase in annual contribu-

tion, PGE will have to borrow to bridge its needs. As currently estimated, however, the cash flows will eventually be sufficient to fund the cost of decommissioning including repayment of the interim financing.

PGE has submitted a decommissioning plan for approval by the Nuclear Regulatory Commission (NRC). We approve PGE's plan subject to our review and monitoring of costs. There are a great many unknowns as regards decommissioning, and we need to retain the flexibility to modify PGE's plan if circumstances change significantly.

Decoupling. Another major issue in this docket is decoupling. Decoupling is a mechanism that eliminates the automatic connection between utility sales and profits. Breaking that connection [*8] is designed to encourage utilities to find cost-effective ways of reducing sales and conserving energy. If sales are linked to profits, a utility has every incentive to keep sales, and hence energy consumption, high.

Decoupling creates a mechanism to adjust for actual sales deviating from a preestablished level. A utility cannot increase its earnings by increasing sales, because additional sales margins are returned to ratepayers and the utility's net revenues are reset to the preestablished level. If the utility's revenues are less than forecast, the decoupling mechanism would restore those lost margins so that net revenues are again adjusted to reflect the preestablished level. The company does not gain or lose net revenues by selling larger or smaller amounts of power. The key step in decoupling is to establish the revenue targets.

In Order No. 92-1673, the majority of the Commission directed PGE to develop a decoupling mechanism suitable to its circumstances. Working as part of a collaborative, PGE designed a process that uses a two-year test period to establish revenue targets and deals with monthly revenue benchmarks, weather normalization, rate spread, and other issues.

[*9]

At issue in this docket is whether and how to implement decoupling. Some parties argue that decoupling has not proven to be as effective as hoped in other jurisdictions. Some contend that forecasting over the two-year test period introduces too much uncertainty. Other parties argue for decoupling, but suggest different ways of treating rate spread or other features of the collaborative's plan.

A majority of the Commission finds that decoupling should be implemented. It is a relatively simple mechanism to remove a variety of perverse incentives inherent in the existing structure of rate regulation and it has low administrative costs. Its benefits clearly outweigh its disadvantages. Chairman Smith writes separately in dissent on this issue.

We adopt the collaborative's mechanism, subject to certain reporting and monitoring requirements. The reporting requirements are designed to make it easier to administer and review the mechanism. The monitoring requirements are designed to protect ratepayers from the potential problem of a decline in the level of PGE's service.

Rate Spread. In setting electric utility rates, this Commission has traditionally been guided by the cost of [*10] serving various customer classes, as measured by marginal costs. The marginal cost study approved in this order indicates that commercial and industrial customers pay a higher rate relative to the costs of providing service than residential customers.

In this order, we reaffirm the use of a "4-to-1" rate spread methodology to help set rates more in line with the actual costs caused by each customer class. This 4-to-1 methodology, which was adopted in PGE's last general rate case (UE 79), assigns residential customers a percentage increase of four times that assigned to medium and large commercial and industrial customers. This rate spread methodology will not eliminate the current rate disparity, but will achieve a more balanced distribution of the costs of service without subjecting residential customers to rate shock.

Other Issues. Commission staff asked the Commission to impose on PGE an additional reduction in discretionary costs (operating and maintenance expense accounts excluding Trojan O&M, amortization of energy efficient balances, uncollectible accounts, regulatory expenses, and rents) if the Commission found that PGE's cost reduction efforts were insufficiently diligent [*11] in the circumstances. We have imposed an additional one percent cost reduction on PGE, which reduces PGE's revenue requirement by approximately \$ 1.6 million in each test year.

Most other major issues in this docket were resolved by stipulation between staff and PGE. We have reviewed these stipulations carefully, find that they are reasonable, and adopt them.

Overview of PGE's cost structure. This proceeding used a two-year test period to comport with the decoupling approach suggested by PGE's collaborative on decoupling. Due to the closure of Trojan, PGE's cost structure has changed significantly. The major factor causing the rate change authorized by this order involves power supply costs. As compared with the costs adopted in PGE's last rate order (UE 79, Order No. 91-186), fixed operation and maintenance costs decrease by \$ 49.8 million for 1995 and by \$ 47.6 million for 1996. However, power supply costs increase by \$ 147.7 million for 1995 and by \$ 152.7 million for 1996. Both of these factors are affected significantly, but not exclusively, by the closure of Trojan. Other factors offset to some extent the increases in costs, notably a lower rate of return to stockholders [*12] due to more favorable capital markets. In addition, the Commission has disallowed certain of the unrecovered Trojan costs. The decision on the Trojan cost recovery issue has the effect of reducing PGE's request by \$ 9.7 million for 1995 and by \$ 9.3 million for 1996.

INTRODUCTION

Procedural Background

On November 9, 1993, PGE filed Advice No. 93-26, a general tariff revision designed to increase rates to its Oregon electric retail customers, to be effective December 8, 1993. PGE's proposed price schedules are based on the company's expected revenue requirement for a two-year test period covering 1995 and 1996. The two-year test period reflects the decoupling mechanism designed by PGE and a collaborative work group pursuant to Order No. 92-1673.

On December 7, 1993, we found good and sufficient cause to investigate the propriety and reasonableness of the rates and initially ordered the suspension of Advice No. 93-26 for a period of six months. *See* Order No. 93-1754. Shortly thereafter, PGE waived the statutory suspension period and, on June 1, 1994, we ordered a further suspension of the Advice until January 1, 1995. *See* Order No. 94-899.

Prehearing Conference

[*13]

On December 13, 1993, Ruth Crowley, a Hearings Officer for the Commission, held a prehearing conference in Salem, Oregon, to identify parties and interested persons and to adopt a procedural schedule. A list of the parties to this proceeding is set forth in Appendix A.

Public Comment Hearings

In February 1994, we held public comment hearings in Portland, Gresham, Aloha, and Salem. At each hearing, a representative of PGE made an informal presentation explaining the terms of the proposed rate schedules and other aspects of the filing. A member of the Commission staff also appeared to explain staff's role in this proceeding and to answer questions from the public. Many PGE customers and interest groups attended the hearings and testified in opposition to the proposed rate increase. During the course of this proceeding, we also received numerous written comments from the public opposing PGE's proposed tariffs.

Bifurcation

On March 21, 1994, staff moved to amend the schedule and to defer examination of issues related to PGE's investment in the Trojan Nuclear Power Plant and cost of capital to a later phase of this proceeding. Staff requested the bifurcation to allow time [*14] to hire a consultant and time for the consultant to review Trojan-related issues. On May 3, 1994, the Hearings Officers granted the motion and bifurcated this proceeding into Phase I and Phase II.

UM 692 and Further Extension of Suspension Period

On May 26, 1994, staff moved to further amend the schedule to allow additional time for its consultant to complete work. Staff concurrently filed a motion for an order authorizing PGE to use, upon the expiration of the suspension period, deferred accounting treatment for increased revenues resulting from the implementation of PGE's revised tariffs.

Staff subsequently withdrew its motions. On July 29, 1994, PGE applied to defer for later ratemaking treatment 40 percent of the increased power costs resulting from the closure of Trojan for the period from January 1, 1995, until March

31, 1995, or the effective date of new tariffs approved in this proceeding, whichever is earlier. We docketed PGE's application as UM 692 and consolidated it with this proceeding. On September 30, 1994, we granted PGE's request for deferral of costs. See Order No. 94-1456. With approval of its application, PGE agreed to stipulate to a further extension [*15] of the suspension period to no later than March 31, 1995.

PHASE I

Issues List

After a review of PGE's tariff filing, staff identified 44 potential issues in what has been designated as Phase I of this proceeding. Staff listed those issues numerically in its preliminary issues list, filed on May 3, 1994. We use staff's numbering system in our discussion of those issues. A complete issue list is found on page 1 of Appendix F, Adjustment Summary, attached.

Stipulations

On July 1, 1994, PGE and staff submitted a stipulation intended to resolve many of the disputed issues in this portion of the proceeding, subject to our approval. The stipulation is attached as Appendix B. The stipulation was supported by joint testimony of Ray Lambeth of staff and Kelley Marold of PGE on numerous revenue, expense and rate base issues.

On July 15, 1994, PGE and staff submitted a stipulation supplement intended to resolve additional disputed issues not covered in the first stipulation. The stipulation supplement is attached as Appendix C. The stipulation was supported by joint testimony of Lynn Kittilson of staff and Chris Ryder of PGE.

On February 27, 1995, PGE and staff submitted [*16] an additional stipulation intended to resolve issues relating to Issue S-13: Variable Power Costs. The additional stipulation is attached as Appendix D.

All stipulations and supporting testimony were entered into the record of this proceeding as evidence pursuant to OAR 860-14-085(1).

Evidentiary Hearing

On July 14, 1994, Hearings Officers Ruth Crowley and Michael Grant held a Phase I evidentiary hearing in Salem, Oregon. Randy Childress and Melinda Horgan, Attorneys at Law, appeared on behalf of PGE. Paul Graham, Mike Weirich, and Kimberly Cobrain, Assistant Attorneys General, appeared on behalf of staff. Grant Tanner, Attorney at Law, appeared on behalf of the Oregon Committee for Equitable Utility Rates (OCEUR). John Stephens, Attorney at Law, appeared on behalf of the Citizens' Utility Board (CUB). Phil Carver appeared on behalf of the Oregon Department of Energy (ODOE).

Based on the record in these proceedings, we make the following:

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Stipulated Issues

The Phase I stipulations cover most of the issues identified by staff in this portion of the proceeding. ODOE and OCEUR are not parties to the stipulations and object [*17] to portions of the proposed resolution of Issue S-44: Rate Design. OCEUR also challenges the proposed resolution of Issue S-13: Variable Power Costs, and Issue S-37: Boardman Gain Acceleration. Accordingly, we will treat issues S-13, S-37 and S-44 as contested issues and address them with the other issues not covered in the proposed stipulations.

We have reviewed the Phase I stipulations with regard to the other noncontested issues (S-1 through S-12, S-14, S-17 through S-28 except for one issue in S-20, S-30, S-31, S-33, S-34 through S-36, S-39, S-40, S-42 and S-43). We find the stipulations on these issues reasonable. Accordingly, the stipulations on those issues, set forth in Appendices B, C and D, are adopted.

Contested Issues

The Phase I stipulation did not cover six identified issues (S-15: Wage and Salary; S-20: Medical Insurance Pooling; S-29: HVEA Promotions; S-32: PGC Allocations; S-38: Decoupling; and S-41, LRIC and Rate Spread). Furthermore, as discussed above, issues S-13: Variable Power Costs, S-37: Boardman Gain Acceleration, and S-44: Rate Design, are treated as contested issues. We address these nine issues separately in numerical order.

Applicable [*18] Law

As the petitioner in this rate case, PGE has the burden of proof on all issues. ORS 757.210 provides that, in a rate case, "the utility shall bear the burden of showing that the rate or schedule of rates proposed to be established or increased or changed is just and reasonable."

S-13: Variable Power Costs

PGE incurs variable power costs to meet its retail and firm wholesale requirements and to make economic wholesale sales in the secondary market. To estimate its variable power costs for the two-year test period, PGE used PRO-SCREEN, a computer forecasting model.

PGE and staff entered into a stipulation with respect to PGE's variable power costs. The parties propose to include in UE 88 base rates variable costs savings expected from the commercial operation of the Coyote Springs generating plant using a forecast in-service date of December 15, 1995. The parties also agree that PGE may file proposed revised rates to address a change in BPA's transmission and power rates through a tracking procedure when such change occurs. As a result of those proposals, PGE and staff further agree that the following amounts are a reasonable forecast of variable power costs for the [*19] test period: \$ 304,624,300 (1995); \$ 310,103,700 (1996).

OCEUR is not a party to that stipulation, however, and objects to the use of the PROSCREEN model because the model was developed for use in thermal-based systems. OCEUR does not suggest an alternative but urges caution in use of the model. For 1996, OCEUR proposes to increase the 1995 estimate only by a load growth factor. We find that proposal unacceptable, because OCEUR's approach does not rigorously forecast power costs for 1996 and hence is not factually based.

We have reviewed the stipulation between staff and PGE on variable power costs and find it reasonable. We adopt that stipulation, attached as Appendix D.

S-15: Wage and Salary

Staff proposes certain adjustments to PGE's filing with respect to estimated increases in wages and salaries. Specifically, staff recommends reductions in straight-time labor of \$ 504,691 in 1995 and \$ 923,640 in 1996, and allocates those reductions between operations and maintenance expense and capital. Staff also recommends a reduction in related payroll tax expense.

Staff and PGE arrive at their positions by using two different analytical methods. PGE relies on a market-based [*20] approach to determine its labor budget. PGE first defined five labor markets, differentiated in terms of size and demographics, in which it competes for employees. For each market, PGE reviews annual surveys from various sources to determine competitive base pay rates for its employees.

Staff relies on a three-year wage and salary formula to estimate appropriate payroll levels. As a starting point, staff's formula uses PGE's actual nonunion average wage and salary level for 1992 and 1993. From there, staff applies the Consumer Price Index change for each of the three subsequent years to establish a forecast of test-year wage and salary levels. In staff's method, if PGE's projected wage and salary level is within ten percent of staff's projection, the difference between projections is shared equally between customers and shareholders. Outside the ten percent band, shareholders keep all the benefit or pay all the cost.

We find the three-year wage and salary formula more reasonable than PGE's approach for this proceeding and adopt staff's recommendations. As staff points out, this Commission has relied on staff's model for over ten years to monitor energy utilities' wages and salaries [*21] for both general rate cases and earning tests associated with deferred accounting. The current model produces a reasonable and reliable result.

PGE faults staff's model for not being market based. Staff's model is based on market data. Its starting point is actual PGE wages for 1992 and 1993. Moreover, staff's method of sharing the difference between the two payroll projections equally between ratepayers and shareholders also allows for some adjustments to reflect changes in market conditions without allowing unchecked escalation.

Although we adopt staff's method for this proceeding, we do not preclude more extensive use of market data in future proceedings. We will not direct staff to investigate further the use of market data, as PGE requests. However, the company may introduce appropriate market data in support of its filings in the future.

S-20: Medical Insurance

Issue S-20 is covered by the stipulation with the exception of staff's proposal that PGE explore the possibility of becoming part of a larger insurance pool to reduce its medical insurance costs. Staff asks us to order PGE to assess the possibility of pooling arrangements with other companies. PGE objects [*22] and argues that the possibility of national health care reform creates uncertainty in the medical insurance area and notes that it unsuccessfully attempted medical insurance pooling in the early 1980s.

Staff counters that it requires only a feasibility study. Staff urges that PGE should submit a proposal for an assessment study within 45 days of the entry of the order in this docket. PGE opposes the requirement to perform an additional study on pooling costs because the requirement duplicates or contradicts other PGE efforts in this area; because staff's proposal is unclear; and because the required study may be very costly and time consuming. PGE argues that it should be allowed to provide staff a status report on its efforts to reduce medical insurance costs within 90 days from the date of this order. Once staff has had an opportunity to review the report, the Commission may hold a hearing to see what additional steps are needed to implement insurance cost reduction.

PGE's suggestion is the more efficient and reasonable approach. We adopt PGE's proposal for exploring ways of reducing medical insurance expenses. PGE's status report will be due within 90 days from the date of entry [*23] of this order.

S-29: HVEA Promotions

PGE's proposed revenue requirements for 1995 and 1996 include over \$ 1 million each year to provide customers with information about High-Value Electrical Applications (HVEA). These applications include electric forklifts, electric lawnmowers and grass trimmers, electric barbecues, and dual-fuel heat pumps. PGE contends that providing customers with information about HVEA is a valuable customer service and proposes to budget related expenditures under Federal Energy Regulatory Commission (FERC) Account 908.

Staff objects to PGE's proposal and recommends that the Commission disallow all expenses relating to HVEA promotions. Staff contends that the HVEA activities are intended to either promote or retain load. For that reason, staff argues that the costs related to the HVEA marketing activities are more appropriately treated as promotional expenses under FERC Account 912.

To recover HVEA expenses, PGE must demonstrate that the promotional activities are reasonable by quantifying net ratepayer benefits. In Docket No. UG 81, the Commission recognized that ratepayer benefits must be established by "a showing that the specific expenditures [*24] incurred provided a recognizable benefit to the people from whom the utility seeks reimbursement. . . . It may be difficult to quantify benefits, but the utility company needs to show the Commission that there is a sound basis for passing the costs on to the ratepayers." Order No. 89-1372 at 7.

After a review of PGE's testimony, exhibits, work papers, and other evidence submitted in this matter, we conclude that PGE has failed to establish specific benefits to ratepayers from HVEA expenditures. Although PGE maintains that

HVEA activities are a customer satisfaction strategy designed to help the company move into a more competitive environment, it acknowledges that HVEA may increase the use of electricity by up to an average of four to five MW per year. Thus, while the information provided may prove useful to some customers, a primary purpose of the activities is to create new customers or increase sales to existing customers. Because PGE has not demonstrated that the promotion of HVEA will provide specific benefits to its ratepayers, we adopt staff's recommendation that these costs not be allowed.

In reaching this decision, we note staff's concerns that PGE is inconsistent in [*25] promoting both energy efficiency and load growth when the company is acquiring new resources. PGE's efforts to promote load growth may undermine its ability to promote customer adoption of energy efficiency measures. We recognize that there are some circumstances in which the increased use of electricity can provide benefits that may not directly relate to rates, such as environmental benefits. PGE, however, must provide sufficient evidence to support a finding that those benefits exist.

S-32: PGC Allocation

PGE's filing allocates certain joint and common costs incurred by Portland General Corporation (PGC) to PGE, a wholly owned subsidiary. This issue concerns allocations to PGE of PGC's Board of Directors costs and PGC's Executive costs. PGE proposes to change its cost allocation method from the direct labor costs method to the Equity Method for Board of Directors costs and the Massachusetts Formula for the Executive costs. Staff has usually used the direct labor costs method. The Commission adopted that method in UE 79, Order No. 91-186. PGE's filing for FERC Account Nos. 921 (Office Supplies and Expenses), 926 (Employee Pensions and Benefits), and 408.1 (Taxes Other Than [*26] income Taxes) was \$ 6,294,769 for 1995 and \$ 6,844,271 for 1996. Those accounts reflect PGC cost allocations.

The Equity Method distributes costs on the proportionate investment of the parent company, PGC, in its various subsidiaries. The Massachusetts Formula distributes costs on an equal weighting of subsidiaries' payroll, revenue, and assets. PGE did not present reasons for changing from the direct labor costs method.

Staff argues that the proposed methods are inappropriate for the S-32 cost allocation categories. PGE's revision with respect to the Equity Method, staff contends, is based on assertions unsupported by verifiable cost causation linkages. There should be a high degree of correlation between PGC employees' time and the PGC Board of Directors' time allocation, according to staff, because both groups are concerned with shareholder wealth maximization. Staff further argues that if PGC has nonoperating subsidiaries with investment but no demand on PGC employees' or directors' time, the existing method will achieve a more correct allocation of cost than the Equity Method.

Staff points out that the Massachusetts Formula could be a fair and reasonable method for homogeneous [*27] subsidiaries, as measured by line of business and maturity. Staff contends that that is not the case here, however, because PGE has inherent biases as to capital and labor intensity when compared to the nonregulated subsidiaries of PGC. These biases, according to staff, skew costs to the utility and provide an improper cross-subsidization. Staff also expresses reservations about inclusion of revenues, which are cost derivative, not cost causative, in the formula. Staff takes the position that the best reflection of effort and resource expenditures by the parent is its directly assigned labor expense. Staff has recalculated PGE's original filing for FERC Account Nos. 921, 926, and 408.1 to \$ 5,793,297 for 1995 and \$ 5,992,097 for 1996. Those reductions reflect corrections of inflation errors and eliminate the effects of PGE's proposed allocations revisions.

PGE does not counter staff's arguments. We are persuaded that staff is correct and adopt staff's adjustments to the PGC cost allocations.

S-38: Decoupling

Definition of Decoupling. Decoupling is a regulatory tool designed to eliminate disincentives for a utility to promote cost-effective energy conservation. Decoupling [*28] mechanisms break the link between profits and sales by creating a mechanism to adjust for actual sales deviating from a preestablished level. Under this mechanism, a utility cannot increase its earnings by increasing its sales, because additional sales margins are returned to ratepayers and the utility's net revenues are reset to the preestablished level. If the utility's revenues are less than forecast, the decoupling mechanism would restore those lost margins so that actual net revenues are again adjusted to reflect the preestablished level. Thus, the company does not gain or lose net revenues by selling larger or smaller amounts of power.

Decoupling Policy and Collaborative Recommendations. In 1991, the Commission opened an investigation docket, UM 409, to develop a set of policies that would encourage utilities to acquire cost-effective demand-side resources. In Order No. 92-1673, at 13, the majority of the Commission made a policy decision to decouple utility profits from sales levels:

We are persuaded that the connection between profits and sales should be severed. As long as the regulatory system provides that increased sales may lead to increased profits, a conflict [*29] will exist between the motivation to sell energy and the motivation to promote reduction in energy consumption. No other change in the regulatory system can ensure that we will move toward the goals of this proceeding.

The Commission directed PGE to undertake collaborative processes to develop a decoupling mechanism suited to the company's particular circumstances. PGE, staff, and representatives of a broad group of interests worked together to develop a decoupling mechanism for PGE. The collaborative, as the working group was called, presented its mechanism at the Commission's April 20, 1993, public meeting.

To establish revenue targets for PGE, the collaborative decided to use a two-year test period. Revenue targets are to be set once for each two-year period, so that there is one rate change for the period. The mechanism also establishes monthly revenue benchmarks and incremental cost estimates; restates actual revenues and sales as if normal weather had occurred; implements decoupling-related rate adjustments every six months as needed; amortizes any decoupling adjustment over an 18-month period; spreads the decoupling adjustment among the customer classes using, in part, [*30] the rate spread adopted by the Commission in PGE's 1991 general rate order, Order No. 91-186 (UE 79); and caps the overall revenues collected from the decoupling rate adjustment at any time at 3 percent of base revenues.

How and Whether to Implement Decoupling. The Oregon Department of Energy (ODOE), and the Northwest Conservation Act Coalition (NCAC) do not oppose decoupling. Staff states that the Commission has already made the policy decision that profits should be decoupled from kilowatt hour (KWh) sales. Therefore, staff did not discuss whether decoupling should be implemented. PGE agrees to decoupling if the Commission finds that its benefits outweigh its disadvantages. PGE also conditioned its agreement on the Commission following PGE's request with respect to the treatment of variable power costs (Issue S-13). PGE signed a stipulation resolving that issue, so PGE's concerns in that regard have been met. ODOE and NCAC also support the collaborative's decoupling mechanism.

OCEUR raises a number of arguments against decoupling. First, OCEUR contends that decoupling abandons the regulatory premise that utility rates should be based on the utility's prudently incurred costs [*31] of providing service. It argues that decoupling not only leaves a utility indifferent to declining revenues from conservation, but also insulates it from revenue attrition resulting from any source, including warm weather, recession, or disappearing rate base. In short, OCEUR believes that decoupling makes a utility insensitive to costs and profits.

Second, OCEUR points out problems associated with decoupling, especially the difficulties of estimating costs for a two-year period with sufficient accuracy for ratemaking purposes. The two-year period, OCEUR contends, fails to account for the time value of money. Costs are estimated on a year-by-year basis and then averaged over two years. In a time of rising costs, this leads to collection of a greater amount in rates than is actually incurred for that year, and a subsequent lesser collection the second year. Therefore, OCEUR contends that the decoupling mechanism functions as an interest-free loan to the utility in such a case. OCEUR also believes that the mechanism gives the utility an incentive to overestimate its power costs in the second year of a two-year test period.

Staff noted that OCEUR's concern is less about decoupling [*32] than about accurately estimating variable power costs. Staff stated that the Commission frequently uses estimates of variable power costs in such areas as avoided costs and conservation cost effectiveness. Because these other areas are extensively scrutinized, staff does not believe an "error" exists in the methodology for estimating variable power costs and notes that OCEUR has not raised this concern in any of those other areas.

Finally, OCEUR contends that the decoupling mechanism allows the company to game the mechanism. OCEUR believes that the incremental costs used in the mechanism understate the "true" short-run variable cost. OCEUR contends that the company can inappropriately increase its profits through the decoupling mechanism by reducing its sales.

Consistent with its argument on Issues S-41 below, CUB requests that we undo the 4-to-1 rate spread for decoupling adjustments.

Disposition. We adopt the decoupling mechanism the collaborative presented, subject to the recommendations staff has made (see below). It is still the Commission's policy to encourage conservation by severing the link between sales levels and profits. The difficulties of forecasting a two-year [*33] test period are not significant enough to outweigh the potential benefits from decoupling.

Decoupling is an attempt to align the utility's financial interest with the interests of its customers. Decoupling removes the utility's incentive to promote new sales and does not provide utilities with an incentive to adopt ineffective demand-side management programs. The current system of regulation produces incentives for utilities to increase electricity sales and corresponding disincentives to the pursuit of energy efficiency. Because decoupling separates profits from fluctuating sales levels *regardless* of the cause of the changed sales, it addresses efficiency impacts resulting from *all* effects, including rate design, all utility-sponsored demand-side management activities, and all energy efficiency measures. Moreover, decoupling does not require sophisticated measurement or estimation. A utility that does not actually produce savings simply does not profit from demand-side management.

Decoupling does not take the next step and provide a positive incentive for good planning. But it does provide a relatively simple mechanism to remove a variety of short-term perverse incentives [*34] inherent in the existing regulatory structure.

Breaking the link between sales levels and profitability does not mean that the utility is left with no incentive to minimize costs and maximize profits. The utility can increase its profitability through activities not related to sales. Also, the collaborative's decoupling mechanism specifically chose to use expected rather than actual incremental power costs, giving the utility another opportunity to increase profits by minimizing its actual KWh costs.

The Commission is persuaded by staff's rebuttal of OCEUR's concerns about variable power costs. As to OCEUR's arguments about the time value of money, where rising costs are averaged over two years, the first year's actual average cost will be less than the two-year average, and the second year's actual average cost will be more than the two-year average. This is a natural outcome of averaging. This averaging also occurs in a single-year test year, the result being that a single set of rates for the test year will necessarily be overstated for the first six months and understated for the last six months. Normal regulatory practice does not make an adjustment to costs to take into [*35] account what may be considered an interest-free loan due to this type of stream of payments. As with other aspects of the collaborative's mechanism, the Commission is not inclined to dismantle the collaborative's recommendations. The Commission appreciates OCEUR's concern, however, and directs staff to consider this issue in future developments of regulatory mechanisms.

The fact that the decoupling mechanism presents the utility an incentive to inflate its second year's estimated costs raises a concern. However, we believe that problem has been contained by staff's monitoring of the costs in this docket. As to CUB's request, we will not dismantle the collaborative's recommendations piecemeal by changing the rate spread that the collaborative agreed on.

In terms of specific implementation, Paragraph 36 of the July 1, 1994, stipulation sets forth the agreement to use one set of weather normalization coefficients for both years of the test period. Further, staff recommends that we require a decoupling tariff design that contains information on monthly revenues, incremental costs, and margins that result from this rate case. Having this information in the tariff will make the task [*36] of administering the mechanism easier, staff maintains, and will allow review of the mechanism. Staff also recommends that the tariff include information on the weather normalization procedure that staff and PGE have agreed on. No party opposes these recommendations about the tariff, and we adopt them.

Because PGE will no longer have the incentive to sell more KWh or to sell at higher prices the KWh it currently markets, we need to consider service quality to PGE's customers. To address the issue of service quality, staff also recommends that we direct staff to monitor PGE's service to protect ratepayers and assess the impacts of decoupling on the utility's behavior. No party opposes this recommendation, and we adopt it.

Paragraph 8 of the July 15, 1994, stipulation covers implementation of the decoupling mechanism. The mechanism functions as a comparison of benchmark net revenues to weather-adjusted actual net revenues. Revenue targets are based on the assumption that the new rates, to be set in this docket, are in effect. Consequently, PGE and staff agree that the decoupling comparison should occur when revenues reflect new rates. Accrual adjustments for decoupling should therefore [*37] not begin until the effective date of the new rates.

Incremental Power Costs. PGE and staff disagree on how to treat incremental power costs under the decoupling mechanism. Monthly incremental power costs are needed to determine the margin earned or lost because of changes in sales from those forecast in the rate case. The decoupling collaborative stated that these 24 monthly estimates should be set in the rate case but did not specify a methodology. In its filing, PGE proposed using the PROSCREEN model to determine incremental power costs, using the actual differences between forecast loads and weather-adjusted loads. Staff proposed generating incremental power cost estimates by averaging the incremental power costs associated with positive and negative load increments of the same size. We adopt staff's rather than PGE's proposal, because the use of estimated incremental power costs is consistent with the collaborative's recommendation.

Staff originally proposed using +/- 5 MW as the increment for purposes of estimating incremental power costs. PGE countered with a proposal of +/- 10 MW, an increment, PGE contends, that is large enough to ensure meaningful results. Staff [*38] does not object to the 10 MW figure, provided staff has the right to review PGE's calculation of estimates. Lack of such review could result in inaccurate incremental cost estimates that could create perverse sales incentives. We adopt the +/- 10 MW increment figure for estimating incremental power costs, and order that staff shall have the right to review PGE's calculation of estimates.

The February 27, 1995, variable power costs stipulation between PGE and staff could result in revisions in late 1995 or early 1996 to the monthly targets contained in the decoupling tariff.

S-37: Boardman Gain Amortization

PGE had originally proposed accelerating the Boardman gain amortization to three years instead of the 27-year period approved in UE 47/48, Order No. 87-1017. Staff opposed the proposal, and PGE withdrew it. OCEUR still supports acceleration of the Boardman gain amortization for ratemaking purposes.

OCEUR argues in favor of the acceleration because it believes that customers paid a disproportionate share of overall Boardman costs in the plant's early years. According to staff, that is true of every plant. The Commission allows return on unrecovered investment. In the early [*39] years of a plant, staff points out, unrecovered investment is large; later it shrinks. Staff contends that OCEUR's argument assumes without stating that PGE sold Boardman for more than the book value of the plant. In fact, staff maintains, PGE realized no profit from sale of the plant.

Staff is correct about the Boardman sale. See Order No. 87-1017 at 28. That order established the Boardman gain amortization and found that most of the money PGE received from the transaction represented profit from a wholesale power sale between PGE and San Diego Gas & Electric. \$ 51.3 million of the \$ 78.7 million to be amortized came from the power sale. The power sale to San Diego Gas and Electric that generated the majority of the gain at issue was a system sale, and thus we continue to maintain that the gain be amortized as prescribed in Order No. 87-1017. We are persuaded by staff's argument and adopt the resolution of the issue contained in the Phase I stipulation, Appendix B at 13.

S-41: LRIC and Rate Spread

As part of its filing, PGE submitted a long-run incremental cost (LRIC) study. LRIC is a measure of the long-run costs or savings from providing one unit more or less of service. [*40] The Commission has traditionally used LRIC studies to determine cost causation and to help allocate those costs.

PGE's cost study indicates that commercial and industrial customers pay a higher rate relative to the cost of providing service than residential customers. The study, as revised by adjustments recommended by staff, shows that current residential rates collect 92.5 percent of average recovery of total LRIC, while large commercial and industrial rates collect 120.1 percent of the average. To help rectify this disparity and to achieve a more balanced distribution of the costs of service, PGE proposes to apply a "4-to-1" methodology in determining rate spread between customer classes. The 4-to-1 methodology assigns residential customers a percentage increase of four times that assigned to medium and large commercial and industrial customers. A 4-to-1 approach would increase residential rates to 95.6 percent of average recovery and reduce large commercial and industrial schedules to 113.0 percent of the average. The Commission adopted the 4-to-1 methodology in PGE's last general rate case. See UE 79, Order No. 91-186 at 25.

PGE's revised LRIC study and its proposed 4-to-1 [*41] rate spread are supported by all parties participating in Phase I of this proceeding with the exception of CUB. CUB argues that PGE's use of a "minimum system" approach to allocate distribution costs in the LRIC study assigns too many of those costs to residential customers. CUB suggests the use of a "basic customer allocation" method, which would assign a greater share of distribution costs to commercial and industrial customers. Using that approach to allocate distribution costs, CUB contends that a corrected cost study shows that residential customers would actually pay 102.6 percent of indexed costs under a 4-to-1 rate spread. Due to this fact, CUB argues that the marginal cost study does not support PGE's rate spread proposal and recommends that any increase in rates be spread equally among all rate classes.

We are not persuaded by CUB's recommendation for two reasons. First, as noted by PGE, when CUB recalculated the marginal costs for residential customers in preparing its cost study, it failed to adjust the marginal costs for the nonresidential customer classes. That error led CUB to overstate the indexed percent of marginal costs for the residential class at 102.6 percent. [*42] Using CUB's estimates of marginal distribution and customer costs and recalculating marginal costs for the nonresidential classes, the corrected figure for residential customers under CUB's approach is 101.0 percent of indexed costs, under a 4-to-1 rate spread. Because that figure is based on PGE's original filing and does not reflect revenue requirement reductions and other adjustments embodied in the stipulation, we add that a 4-to-1 rate spread will not likely raise residential rates as high as that reduced figure.

Second, CUB failed to use the appropriate definition of demand in allocating distribution costs under the basic customer allocation approach. Under CUB's proposed methodology, any costs other than service drops and meters are classified as demand-related costs. In applying that method, however, CUB improperly assigned marginal costs using a coincident peak (CP) allocator, rather than using a weighted allocation of distribution costs that considers both CP and noncoincident peak (NCP). Because distribution facilities are primarily designed to meet a customer's maximum NCP, the costs associated with the system must be allocated on that basis. Thus, CUB's vastly different [*43] distribution cost allocation results from its different definition of demand, not from inherent differences between allocation methods. Had CUB used a correct allocator for distribution demand costs, its spread of distribution costs to various rate classes would have been similar to that of PGE's study.

We have reviewed PGE's revised LRIC study and find the minimum system approach appropriate for allocating distribution costs in this proceeding. PGE has used that methodology in the development of its marginal costs for over 15 years. Moreover, while no unanimity exists on the treatment of distribution costs, a study by the National Economic Research Associates found that the minimum system approach was the most frequently used method in the treatment of distribution costs. Accordingly, we conclude that the revised LRIC study reasonably estimates marginal costs and should be used to guide rate spread and rate design.

We further conclude that PGE's revised rate study supports the 4-to-1 rate spread proposal. As noted above, the Commission previously adopted the use of a 4-to-1 methodology in PGE's last general rate case to help set rates more in line with the actual costs caused [*44] by each customer class. With increasing competition in the electric services industry, public policy dictates continued movement toward rate parity. We believe that the continued use of a 4-to-1 rate spread will help accomplish that goal without subjecting residential customers to rate shock.

In reaching these decisions, we request the parties to address and study other cost allocation methods for possible use in PGE's next general rate case. All marginal cost studies use simplifying assumptions and conventions to attempt to best estimate cost causation. While we have found that PGE's LRIC study reasonably estimates those costs and should be used in this rate proceeding, several parties, including PGE, OCEUR, and staff, have suggested possible improvements

to the study. These suggested improvements include the use of a "facilities approach" method for allocating distribution costs. In addressing possible adjustments to the marginal cost study, the parties should complete discussions in time to implement and recommend changes prior to PGE's next general rate case. PGE should take the lead in conducting such discussions.

S-44: Rate Design

PGE proposed several changes relating [*45] to its electric rate design. PGE's filing includes: (1) an increase in customer charges for the residential and small commercial classes; (2) the elimination of the seasonal differential in demand charges; (3) an increase in demand charges and reduction of energy charges for most commercial and industrial customers; (4) the addition of a time-of-day differential to energy charges for large commercial and industrial service (over 1 MW); and (5) an increase in power factor requirements.

Staff and PGE have stipulated that PGE should implement the proposed overall rate design, with the exception of proposed Schedules 103 (energy efficiency recovery adjustment) and 107 (add for the Boardman sale refund adjustment), and the increase to the customer charge on Schedule 7 (residential service). The parties also agree that minor deviations may be necessary in implementing these rate design changes to achieve a smooth transition between rate schedules. The stipulated agreement is set forth in the July 1, 1994 Stipulation, paragraph 41 (Appendix B, attached).

ODOE and OCEUR are not parties to the stipulation and raise several issues related to PGE's proposed rate design. ODOE advocates [*46] the addition of a new tailblock rate for residential rates and the inclusion of environmental adders in marginal costs. OCEUR objects to the proposed increase in power factor requirements and recommends a reduced level. We address each issue separately.

ODOE's Inverted Rate Design. PGE's present residential rate tariff employs a two-block inverted rate structure. Customers pay one rate for the first 300 KWh per month, then pay a higher rate for all additional KWh used in that month. ODOE contends that this rate design does not correspond to LRIC and recommends a three-block rate structure. ODOE's proposal would retain the current initial block of 0 to 300 KWh per month, but change the second block to 300 to 2,300 KWh per month and add a third block, priced at LRIC, for use greater than 2,300 KWh per month. ODOE contends that this inverted rate design will help send proper price signals and promote energy conservation.

To support its proposed rate design, ODOE asserts that households that use over 2,300 KWh per month have more opportunities for conservation than households that use less electricity. ODOE fails to provide any studies to support that assertion, however. PGE's [*47] 1992 Integrated Resource Plan found that over 60 percent of potential savings were related to lighting, water heating, and appliances. Thus, all customers, regardless of their usage levels, have opportunities to conserve. Moreover, as noted by PGE, less than six percent of its residential customers use more than 2,300 KWh per month. With so few customers facing this higher tailblock rate, it is uncertain that ODOE's proposal will actually promote energy conservation and reduce inefficient electricity use. Given these uncertainties, and in the absence of an supporting empirical studies, we are unwilling to adopt ODOE's proposed rate structure in this proceeding.

ODOE's Inclusion of Environmental Externalities. ODOE also recommends the use of externality costs in designing residential rates. Specifically, ODOE recommends that LRIC should include a \$ 10 per ton of carbon dioxide (CO₂) adder. ODOE contends that such an adder will account for the risk that carbon dioxide emissions will be taxed or otherwise internalized in the near future.

In UM 424, Order No. 93-695, the Commission adopted guidelines for the treatment of external environmental costs related to energy resources. [*48] Although this Commission decided that it was appropriate to consider external environmental costs in a utility's LCP, we recognized that our authority to impose such costs on a utility or its customers was limited by law. *Id.* at 2. Accordingly, we declined to determine whether to apply environmental externalities to rate design, and indicated that any decision doing so would require further examination of our authority and a full airing of views on the merits of including external costs and on the specific cost figures to be used. *Id.* at 16.

We are aware of numerous state, federal and international efforts to reduce CO₂ emissions. Uncertainties remain, however, whether future regulation will internalize the cost of CO₂ emissions by utilities. In light of questions re-

garding our authority to impose external environmental costs on a utility, and in the absence of a more complete record on this issue, we decline to adopt ODOE's recommendation to include a CO[2] adder in LRIC.

OCEUR's Opposition to Proposed Power Factor Requirements. Currently, PGE charges customers \$ 0.50 for each kilovolt-ampere of reactive demand in excess of 60 percent of the KW billing demand. [*49] This occurs when the customer's power factor drops below 85.7 percent. PGE and staff have stipulated to lowering the threshold level for its reactive demand charge from 60 percent of KW billing demand to 40 percent. Under that level, customers with power factors below 93 percent will be subject to the charge. OCEUR objects to the proposed increase in power factor requirement. OCEUR believes that raising the threshold from 85.7 to 93 percent would result in a too drastic rate increase for affected customers. It proposes the threshold be changed from 60 percent of KW billing to 50 percent. That proposal would result in a charge being imposed on customers with a power factor less than 89.4 percent.

We are not persuaded by OCEUR's argument and find the stipulated reduction to 40 percent of KW billing reasonable. We take official notice of staff's 1990 Research Report on Electric Energy Efficiency Opportunities in Oregon Industries. In that report, staff concluded that the power factor threshold should be raised to 90 percent or higher to promote customer energy efficiency and reduce energy losses on the utility's distribution system. The stipulated proposal would accomplish that recommendation. [*50] Furthermore, while we acknowledge OCEUR's concerns regarding the extent of the increase, the stipulated power factor requirement is similar to that of other Northwest utilities, such as the BPA, whose power factor requirement is set at 95 percent, and Pacific Power & Light, whose power factor requirement is at 93 percent.

PHASE II

Issues List

On September 15, 1994, staff filed a supplemental list of issues it identified for Phase II of this proceeding. As with staff's Phase I issues list, we use staff's numbering of Phase II issues in this section of the order. *See* Appendix F, Adjustment Summary, page 1, for a complete list of issues.

Stipulations

On November 15, 1994, PGE and staff submitted a stipulation intended to resolve rate of return and equity issuance cost issues. The stipulation is attached as Appendix E. The stipulation was supported by testimony of John Thornton, Jr., of staff and Joseph Hirko and Patrick Hager of PGE.

On February 27, 1995, PGE and staff submitted an additional stipulation intended to resolve Trojan balancing account issues. The stipulation is attached as Appendix D.

The stipulations and supporting testimony were entered into [*51] the record of this proceeding as evidence pursuant to OAR 860-14-085.

Evidentiary Hearing

During the week of January 9, 1995, Hearings Officers Ruth Crowley and Michael Grant held a Phase II evidentiary hearing in Salem, Oregon. Randy Childress, Melinda Horgan, and Rochelle Lessner, Attorneys at Law, appeared on behalf of PGE. Paul Graham and Michael Weirich, Assistant Attorneys General, appeared on behalf of staff. John Stephens, Attorney at Law, appeared on behalf of the Citizens' Utility Board (CUB). Geoffrey M. Kronick, Attorney at Law, appeared on behalf of the Bonneville Power Administration (BPA). John A. Kullberg, ratepayer, appeared on his own behalf.

Procedural Rulings

At the outset, we must address several procedural matters raised by URP in its Phase II brief. URP first asserts that the procedural history of this case has prejudiced the rights of the contested case participants, because the Hearings Officers issued a ruling on evidentiary matters the day before Phase II opening briefs were due. URP also argues procedural

harm from the fact that the Hearings Officers faxed their ruling to Linda Williams without checking that she was there to receive the [*52] fax, rather than to Daniel Meek, URP's counsel of record.

We conclude that URP has not suffered prejudice because of the procedural history of this case. URP did not ask for an extension to mitigate any prejudice it might have experienced from the ruling. Nor does URP demonstrate how it was prejudiced. In fact, although the ruling struck some of URP's evidence, URP included argument about that evidence in its brief. URP's argument about the fax is disingenuous. Ms. Williams specifically requested the Hearings Division to fax her the ruling, because Mr. Meek was out of the country.

Second, URP alleges that its request to hold hearings in Portland, made at the January 6, 1995, prehearing conference for Phase II, was denied "without any findings why access to the hearings was being arbitrarily denied to the vast majority of affected customers." That motion had already been made and denied almost a year earlier, by ruling dated January 19, 1994. It was not necessary to repeat the grounds for a ruling that had already been made.

URP further argues that refusal to hold hearings in Multnomah County violates the equal protection clause of the fourteenth amendment and the privileges and [*53] immunities clause of the Oregon constitution. We have reviewed URP's arguments and are not persuaded by them.

Based on the record in these proceedings, we make the following:

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Stipulated Issues

The Phase II stipulations submitted by PGE and staff cover three issues:

S-0: Rate of Return; S-33: Equity Issuance Costs; and an unnumbered issue relating to a Trojan Cost Balancing Account. The parties have agreed to: (1) a stipulated rate of return of 9.51 percent for 1995 and 9.60 percent for 1996; (2) a stipulated common equity issuance cost of \$ 1.75 million for both 1995 and 1996; and (3) a stipulated method to vary the amortization of the Trojan investment to take into account the actual revenue collected from ratepayers as a result of this order.

We have reviewed the stipulations and testimony and find the agreement on these three issues reasonable. Accordingly, the stipulations, attached as Appendices E and D, are adopted.

Contested Issues

The contested Phase II issues relate to PGE's Trojan Nuclear Power Plant (Trojan). The most significant of these issues concerns the ratemaking treatment of PGE's remaining investment [*54] in Trojan: S-50: Remove Additional Fixed Costs - Net Benefits Analysis. Other issues include: S-45: Trojan Overtime; S-46: Trojan Investment Reclassification; S-47: Added Trojan Salvage Recoveries; S-48: Trojan Decommissioning; S-49: Remove Plugging, Sleeving, Analysis and Spare Nuclear Reactor Coolant Pump Motor; S-51: Remove Trojan Power Cost Deferral; S-52: Trojan Income Tax Write-off; S-53: and Trojan Intangible Asset Reclassification.

We will begin with a brief history of Trojan and review of the legal framework of this case, including a discussion of the assumed facts and conditions for recovery set forth in DR 10, Order No. 93-1117. That will be followed by a review of staff's net benefits analysis (Issue S-50), succeeded by the other contested issues in numerical order.

History of Trojan

Trojan began commercial operation in 1976. It was licensed to operate until 2011. Trojan was a single-unit 1200 MW plant, the largest in the Northwest at the time of its construction. PGE owns 67.5 percent of the plant. BPA owns 30 percent under net billing agreements with the Eugene Water and Electric Board and several other publicly owned utilities. PacifiCorp owns 2.5 percent.

[*55]

Trojan was a pressurized water reactor (PWR) nuclear generating facility. PWRs rely on steam generators to heat and cool the water that powers the generating turbine. Steam generators are large pressure vessels that transfer heat from the water in the reactor coolant system (primary system) to the water in the turbine system (secondary system). The water in the primary system is pressurized to keep it from boiling. The heat transfer occurs through the walls of thousands of tubes in the steam generator. The primary system water flows inside the tubes and the secondary system water flows around the outside of the tubes. The heat transferred to the water on the secondary side of the steam generator causes it to boil, producing steam.

The steam produced in the steam generators flows through piping to the turbine generator, where it passes through and drives the turbine. The steam passes through a condenser, where it is turned to water, and the water flows through feedwater heaters and back into the steam generators.

The steam generators, particularly the generator tubes, contain the primary system radioactive water and prevent the release of radioactive water to the secondary system. [*56] Trojan contained four steam generators, each with 3,388 tubes, which PGE purchased from Westinghouse in 1968. PGE is currently engaged in a civil suit against Westinghouse with respect to the steam generators, which degraded badly starting in 1989. By 1991, PGE had plugged or sleeved (permanently attach another tube inside a degraded tube) more than 25 percent of its steam generator tubes.

During its least-cost planning process in 1992, PGE weighed Trojan's continued viability. Among other things, PGE considered the cost of replacing the four steam generators in 1996, the loss of generation that would occur until they were replaced, and the replacement power costs such a loss would entail. In its 1992 Least-Cost Plan (LCP), PGE decided to close Trojan in 1996. As further steam generator degradation became apparent, however, PGE realized that closing Trojan immediately was its least-cost option. On January 4, 1993, the company announced the permanent shut-down of Trojan. PGE's February 1993 Update to its LCP shows its analysis.

Applicable Law

As the petitioner in this rate case, PGE has the burden of proof on all issues. ORS 757.210 provides that, in a rate case, "the utility [*57] shall bear the burden of showing that the rate or schedule of rates proposed to be established or increased or changed is just and reasonable." The requirement applies to PGE's entire case, including the allocation of Trojan costs.

Further, ORS 757.140(2) provides:

In the following cases the commission may allow in rates, directly or indirectly, amounts on the utility's books of account which the commission finds represent undepreciated investment in a utility plant, including that which has been retired from service:

* * * *

(b) When the commission finds that the retirement is in the public interest.

This statute requires that PGE make an affirmative showing that retirement of Trojan was in the public interest in order to include Trojan costs in rates.

The Commission established the legal framework for the Trojan issues in this case in DR 10, Order No. 93-1117. In that order, the Commission adopted the reasoning of the Attorney General's Opinion Letter OP-6454, which advised that the Commission may allow a utility to recover undepreciated investment in retired plant and a return on that investment if the Commission finds such recovery to be in the public interest [*58] under ORS 757.140(2)(b).

In their Phase II briefs, CUB, URP, and the Public Power Council argue against our conclusions in DR 10. They contend that ORS 757.355 bars recovery of and return on undepreciated investment in retired plant. We fully addressed that

argument and rejected it in our resolution of DR 10. Our decision was appealed to and affirmed by the Marion County Circuit Court, and is currently pending before the Oregon Court of Appeals. We will not revisit that issue here.

Standard for Recovery of Undepreciated Investment

The Concept of Net Benefits. In Order No. 93-1117, we concluded that one way a utility may show that a plant closure is in the public interest is if there is a "net benefit" from early closure of the plant. In other words, if the costs of continued operation of the plant are greater than the costs associated with retiring the plant plus the expected long-term costs of replacing the plant's output, there is a net benefit to closure.

The DR 10 Requirements. The language of ORS 757.140 is discretionary: the Commission **may** allow the utility to recover undepreciated investment in rates. In Order No. 93-1117, we set forth the conditions [*59] under which we would favor allowing PGE to recover some or all of its undepreciated investment in Trojan and a return on that investment. First, we assumed six facts:

Assumed Facts:

1. Trojan began commercial operation in 1976. The Commission approved the inclusion in rate base of PGE's investment in Trojan in Order No. 75-832 as construction work in progress and in Order No. 76-601 as completed plant.
2. PGE has made additional investments in Trojan, most of which the Commission has approved for inclusion in rate base through 1991, the test year approved in Order No. 91-186 (UE 79).
3. Since January 1, 1992, PGE has made additional investments in Trojan. The investments were prudent and necessary for the provision of utility service.
4. PGE has depreciated and is presently depreciating its investment in Trojan over a useful life assumed to end in 2011. Since 1976, the Commission has set PGE's prices to include amounts for annual depreciation expense and a return on the undepreciated balance of PGE's Trojan investment.
5. PGE has accrued, and is presently accruing, and depositing in an external trust, funds to decommission Trojan based on a schedule of charges designed [*60] to produce the estimated amount necessary for decommissioning in 2011. Since 1976, the Commission has set PGE's prices to include amounts for future decommissioning of the plant.
6. Closing Trojan permanently in January 1993 was PGE's least-cost option.

Disposition:

PGE and staff agree that PGE has met its burden of proof with respect to five of the six assumed facts, including the fact that permanent closure of Trojan was PGE's least-cost option. They disagree on assumed Fact 3.

Facts 1 and 2. We find that Fact 1 is verified by Order Nos. 75-832 and 76-601, while Fact 2 is verified by Order No. 91-186.

Fact 3. We find that certain of PGE's post-1991 investments in Trojan were not prudent. We disallow costs for steam generator plugging, sleeving, and analysis and a spare reactor coolant pump motor. See discussion at S-49 below.

Fact 4. In Order No. 76-601, the Commission included the investment in Trojan in plant in service. The depreciation rates to be used on that investment were specified in a PGE memo dated January 8, 1976. Trojan has been included in plant in service in several general rate orders in the intervening years, the most recent being [*61] order No. 91-186. We find that this verifies Fact 4.

Fact 5. We conclude that Fact 5 is verified. In Order No. 76-601, which included Trojan in plant in service, the depreciation rates in use included a negative net salvage percentage to cover the cost of removing the plant from service. This percentage was not identified as decommissioning at that time, nor was a specific amount of money identified as a decommissioning cost. However, negative net salvage and a decommissioning accrual are conceptually equivalent (see discussion below, S-48: Trojan Decommissioning).

In Order No. 80-612, the Commission adopted a decommissioning study prepared by Nuclear Energy Services, Inc. That study estimated the cost of removing Trojan from service and established a decommissioning fund. PGE was to make regular accruals to that internal sinking fund. The fund was to finance decommissioning when the plant was removed from service. The internal sinking fund was maintained until Order No. 91-186 (UE 79). In that order, the Commission approved a new decommissioning plan; approved the cost estimate associated with the plan; provided for an external decommissioning fund to be established and managed [*62] by an independent trustee; and provided for annual contributions to be made to the fund, which would grow to an amount equal to the decommissioning cost estimate at the time of decommissioning in 2011. PGE is currently depositing the amount prescribed in Order No. 91-186 in the external trust fund.

Fact 6. PGE relies on its LCP to prove Fact 6. In the November 1992 Plan, PGE compared the costs of three Trojan options: continued operation through 2011, phase-out in 1996, when the steam generators would otherwise need to be replaced, and immediate closure with the plant kept on standby for two years. PGE compared these three options over a range of assumptions about future Trojan operation and the cost of replacement resources. In its LCP, PGE concluded that phase-out was the least-cost option. In its February 1993 Update, it compared phase-out with immediate closure and not keeping the plant on standby. Based on the analysis in its Update, PGE concluded that closing Trojan permanently in January 1993 was its least-cost option.

Staff agrees that the LCP proves Fact 6. Staff reviewed PGE's model design, Trojan cost and operating assumptions, and replacement cost assumptions and [*63] determined that PGE's analysis of its least-cost option was correct. Staff's review showed that PGE used two approaches to model the Trojan cost options. The probabilistic model used probability distributions on values for key inputs to generate a distribution of outcomes, measured in terms of the present value of avoidable costs. PGE used a range of values for Trojan capacity factor, fixed operations and maintenance costs, and capital additions. PGE used the Northwest Power Planning Council's (NWPPC) regional planning model as one basis for replacement power costs.

PGE also used a scenario approach, in which costs were derived from specific input values. The company combined different assumptions about loads, gas prices, nuclear and emission externalities, and Trojan operations and costs. Replacement costs in the scenario approach were based on resources available to PGE instead of the regional portfolio developed in the NWPPC model. In its Update, PGE changed its assumptions about Trojan costs and operations and about replacement power costs in 1993-1996. It examined scenarios based on different assumptions for forced outages, plant repair costs, and replacement costs.

After [*64] reviewing PGE's LCP and staff's evaluation, we conclude that PGE has proved Fact 6.

Although PGE has not proven Fact 3, PGE has substantially complied with the requirement that it prove all six facts in a rate case. We have the discretion to disallow those costs found to be imprudent and to allow a recovery of some or all of the undepreciated Trojan investment.

Conditions on Recovery:

After setting out the six assumed facts that PGE must prove, we listed six conditions that PGE must meet in order for the Commission to allow it to recover some or all of its undepreciated investment in Trojan:

1. PGE's questions are based on six assumed facts regarding Trojan. PGE must prove all six facts in a rate case or similar forum.

2. PGE must show that it has made a diligent effort to reduce other company costs to offset the inclusion of any Trojan costs in rates. For instance, PGE may show that the Trojan closure decision is consistent with least-cost planning criteria over the longer term, but that near-term rates may be higher as a result of the decision. PGE must show that it has made reasonable efforts to keep costs down, especially discretionary costs, before asking customers [*65] to pay higher bills in the near term to support its closure decision.
3. PGE must show why it is reasonable to allow 100 percent recovery of Trojan-related costs in rates. Issues regarding cost recovery are complex and significant. After review, the Commission may decide that PGE is entitled to full recovery of unrecovered plant costs, or it may determine that some cost sharing should occur between customers and investors.
4. PGE must show that it has aggressively attempted to maximize the salvage value of the Trojan facility. If customers are asked to bear some unrecovered costs, PGE must show it is making every reasonable effort to mitigate those costs.
5. PGE must report within 30 days any settlement or award related to replacement power costs, unamortized investment, or any other costs of owning or operating the Trojan plant.
6. PGE must provide satisfactory evidence with regard to any other matter the Commission deems relevant to this issue in a rate proceeding.

Disposition:

The first condition, proving the assumed facts, is addressed immediately above. As to cost reduction, the second condition, staff concluded that PGE had made good efforts to reduce company [*66] costs to offset Trojan cost recovery. However, staff compared PGE's administrative and general (A&G) costs with those of Puget Sound Power and Light, a comparable utility in terms of size and service area. PGE's costs were materially higher for 1989 through 1993, and staff concluded that PGE could find ways to reduce A&G costs still more.

We agree with staff that it is possible for PGE to be more aggressive in its efforts to reduce discretionary costs. Trojan's closure is having and will continue to have an adverse effect on customer rates in the near term. Amortization of replacement power cost deferrals will add approximately \$ 150 million to PGE's revenue requirement from 1992 through completion of amortization. While PGE has made some efforts at cost reduction, we believe that the company can and should do more to mitigate the adverse rate effects discussed above. Accordingly, PGE's rates should recognize a reduction of 1 percent in discretionary costs over and above that approved in Phase I of this Order. We find this a reasonable allowance for discretionary costs. We decline to identify particular program areas that may be susceptible to reassessment or to impose specific [*67] cost reductions. These discretionary costs are best managed by the company.

We acknowledge that these reductions will require difficult choices. Nonetheless, we expect the company to make those choices if it is asking customers to pay higher bills in the near term to support PGE's closure decision. This reduction in discretionary costs reduces PGE's revenue requirement by \$ 1.631 million in 1995 and \$ 1.687 million in 1996.

The third of the DR 10 conditions merely puts forth in condensed form PGE's entire Phase II case. We address this condition below as Issue S-50: Remove Additional Fixed Costs - Net Benefits Analysis. The fourth condition, dealing with salvage value, is also addressed below under Issue S-47, Added Trojan Salvage Recoveries. The fifth condition, requiring PGE to report any settlement or award, is not yet ripe. We continue to impose this requirement on PGE. We did not impose any additional requirements pursuant to the sixth condition.

The Net Benefits Test

As Order No. 93-1117 set out, the first step in determining whether closing Trojan was in the public interest under ORS 757.140(2) is to ask whether there is a net benefit from closure. In its initial [*68] filing in November 1993, PGE re-

lied on its least-cost planning analysis to justify its position that it should receive 100 percent recovery of Trojan costs. PGE maintains that closing Trojan was its least-cost option.

Staff agrees that closing Trojan was PGE's least-cost option. Staff argues, however, that an LCP analysis does not serve to determine whether an action is in the public interest for purposes of allocating undepreciated Trojan investment. The LCP takes the plant as it exists at the time of LCP review. It does not question whether actual costs *should* have been incurred. It then projects costs based on the plant's actual operation out over the time until Trojan's license would have expired. Under an LCP, a poorly run plant may be so expensive to operate that closure would be the least-cost option. That outcome is appropriate and desirable in the framework of the least-cost planning process.

Staff contends, however, that the LCP is not the appropriate tool to determine who should pay for the remaining undepreciated investment in a prematurely retired plant. Using the LCP to allocate remaining undepreciated costs could allow a utility to shift the capital or operating [*69] costs of its own imprudence to ratepayers. If PGE managed Trojan imprudently and the costs and capacity factor used to model continued Trojan operation were adversely affected as a result, the apparent benefit of closing the plant would be overstated.

Staff argues that the net benefits analysis is the appropriate vehicle for deciding how to allocate the remaining Trojan costs. A net benefits analysis is not used to decide whether a plant should be kept in operation. Instead, it compares the *allowable* projected costs of continuing to operate a plant with the allowable costs of closure. Allowable costs are those costs the Commission would deem reasonable and allow PGE to collect from its ratepayers.

Consequently, staff performed a net benefits analysis of PGE's operation of Trojan. Like the LCP, the net benefits analysis projected the costs of operating Trojan out to 2011, the year in which the plant would have closed. The starting point for staff's study was 1995, the first test year in this proceeding. Staff's review differed from an LCP analysis in two significant ways. First, it asked what projected costs are allowable, and disallowed those costs that it considered not reasonable [*70] to impose on ratepayers. Second, it used updated information, while the LCP used information as of the time the decision was made to close the plant.

PGE argues that it is bad policy for the Commission to modify the outcome of the LCP. The utility notes that its decision to close Trojan was reached in the least-cost planning process and acknowledged by this Commission. Actions pursuant to an acknowledged LCP are in the public interest, PGE argues. The utility maintains that it must be able to rely on cost recovery for prudent actions, such as taking a facility out of service where that is the least-cost option. If not, PGE contends, utilities will have no incentive to discontinue operation of such facilities.

Disposition:

We agree with staff that the net benefits analysis is the appropriate vehicle for determining whether closure of Trojan was in the public interest for purposes of determining recovery of undepreciated investment. PGE argues that failure to grant recovery for least-cost actions could lead to utilities operating plants that should be closed. The Commission responds that if an LCP dictates closure of a plant and a company continues to operate it, the company [*71] may not be allowed the full cost of operating the plant in rates. Thus a utility would have no incentive to keep a poorly run, expensive plant on line. Staff's net benefits methodology will be discussed and evaluated immediately below (S-50: Remove Additional Fixed Costs - Net Benefits Analysis). We also agree that the relevant study period for the net benefits analysis is 1995-2011.

Post-1991 Capital Expenditures

In addition to its net benefits analysis, staff reviewed PGE's post-1991 Trojan-related capital expenditures. Those expenditures have never been in PGE's rate base, because they were incurred after PGE's last general rate case, UE 79. These expenditures include all post-1991 steam generator costs (deferred or capitalized plugging, sleeving, and analysis activities), which amount to about \$ 14.9 million, and a spare reactor coolant pump motor, purchased in March 1991 for \$ 2.2 million and never used.

ORS 757.140 does not apply to these expenditures. They are evaluated simply as capital expenditures proposed for rate base treatment and excluded for reasons discussed under Issue S-49 below.

S-50: Remove Additional Fixed Costs - Net Benefits Analysis

As stated, [*72] a net benefit exists when the dollars saved by prematurely retiring plant are greater than the costs associated with building new plant. Here, staff made that determination with regard to the early retirement of Trojan by taking the difference between (1) the expected allowable long-term costs of continued operation of Trojan and (2) the costs associated with closing the plant plus expected long-term costs of replacing its output. Stated in algebraic terms, a net benefit exists if:

$$(X + Y) > (X + Z)$$

where: X = Unamortized investment in Trojan

Y = Expected allowable long-term costs of continued Trojan operation

Z = Replacement resource costs

Calculating the long-term costs of Trojan's operation and replacement resources is a difficult matter. Staff's net benefits analysis is necessarily detailed and complex. Difficulties arise in quantifying the long-term effects of a series of past choices and projecting them out 17 years. Relatively small changes in some key allowable cost inputs adjustments produce a large change in results. This sensitivity is a result of the fact that Trojan closed 19 years prior to the expiration of its 35-year license life.

To explain the net benefits analysis, [*73] we will describe briefly the numerous steps involved in staff's review and summarize staff's findings. PGE and, to a lesser extent, CUB, recommend a number of changes to staff's analysis. We address those arguments as they arise, and resolve disputed issues in the course of our discussion.

1. Least-Cost Plan (LCP) as a Starting Point

As noted above, staff concluded that PGE's least cost planning analysis was not appropriate for determining the net benefits of closing Trojan. However, staff determined that the company's LCP was a good starting point to establish both the long-term cost of replacing Trojan's output and the expected allowable long-term total capital and operating cost of the plant. For purposes of the net benefits analysis, however, staff found that it had to resolve two basic problems with the LCP before beginning its review. First, because PGE prepared the LCP in two parts--the November 1992 Plan and the 1993 Update--staff first had to combine and reconcile the results. Second, because the LCP relied on different planning "scenarios," staff had to identify and select the scenarios most compatible with a net benefits review.

Staff began its analysis by choosing [*74] the results of: (1) Case 1b in the 1992 Plan, which showed that continued operation of Trojan until 2011 would cost \$ 110 million more than phase-out in 1996; and (2) Scenario 3 in the Update, which concluded that phase-out would cost \$ 78 million more than immediate shutdown. Staff then combined the results of the two planning scenarios to obtain a beginning estimate of the higher cost of continued operation of Trojan relative to immediate shutdown, i.e., \$ 188 million. Staff further determined that two additional adjustments were necessary to account for different assumptions about phase-out in Case 1b and Scenario 3. Staff removed additional O&M and A&G costs that PGE included in the 1993 Update. Staff also adjusted for capacity factor differences in 1993-1995 as part of the first step in its overall capacity factor adjustment

PGE raises two arguments relating to staff's use of the LCP as a starting point for its net benefits analysis. First, PGE challenges staff's reliance on Case 1b from the 1992 Plan. It believes that the LCP's probabilistic analysis, not the scenario approach, provides a more complete view of all potential outcomes and should be used in staff's net benefits [*75] test. Using the \$ 168 million expected net present value of phase-out over continued operation determined from the probabilistic analysis instead of the \$ 110 million figure from Case 1b would reduce the negative net benefit to about one-third of staff's estimate.

We are not persuaded by PGE's argument. As staff notes, the discrete input values used in Case 1b closely approximate the expected values of the probability distributions PGE constructed for the Trojan inputs. Moreover, Case 1b is based on replacement resources available to PGE, unlike the probabilistic analysis run with replacement costs derived from the Northwest Power Planning Council's regional model. Staff's use of Case 1b also allowed it to use the sensitivity

analysis results reported by PGE for various Trojan and replacement cost inputs. For these reasons, we agree with staff that the Case 1b result, combined with Scenario 3, should be the starting point of the net benefits analysis.

PGE next contends that the least-cost planning results should be modified to reflect the use of different nuclear fuel assumptions in the 1992 Plan and the Update. We find PGE's proposed adjustment reasonable and accept it. This [*76] adjustment is further addressed below as part of our resolution of Issue S-50.

2. Adjustments to Update the LCP with Current Information

Staff next revised the least-cost planning results to incorporate currently available information. Staff made a total of four such adjustments. Three of the adjustments are not disputed: (1) to reflect lower transition costs experienced and projected by PGE for 1993-1995; (2) to recognize lower replacement power costs in 1993-1995, based on PGE's recent experience and current projections; and (3) to show lower gas prices, using the gas price forecast it sponsored in Phase I of this proceeding.

Staff's fourth adjustment revised the LCP to incorporate new information about the capital costs of long-run replacement resources. Staff modified the LCP to reflect (1) lower estimates of the installed cost of new gas-fired resources; and (2) a 100 MW reduction in PGE's reserve margin requirement. PGE challenges both elements of this adjustment.

First, PGE contends that staff's analysis overstates the costs of a new gas-fired resource by not correcting an error in the carrying charges used in the 1992 Plan. We find PGE's proposed adjustment reasonable [*77] and adopt it. We address this adjustment below as part of our resolution of Issue S-50.

Second, PGE contends that the net benefits analysis should assume a 145 MW reduction in its planning reserve margin requirement, rather than staff's proposed 100 MW reduction. PGE contends that, in addition to a 100 MW reduction in its forced outage reserve requirements brought about by Trojan's closure, its operating reserve needs have also decreased by approximately 45 MW as a result of replacement power purchases. Because these power purchases carry their own operating reserves, PGE contends that staff's adjustment should reflect this additional reduction in the company's operating reserve requirements.

We find that staff's 100 MW reduction is more appropriate for a net benefits analysis. Although PGE claims to have experienced a reduction in its operating reserves, it admitted that it has not completed studies required to quantify any effect of closing Trojan on its operating reserve requirements. Furthermore, as staff points out, the replacement power purchases that purportedly reduce PGE's operating reserves are short-run replacements for Trojan. When long-run resources become operational, [*78] PGE's required operating reserves will increase.

3. Adjustment to LCP for 1995-2011 Study Period

To reflect a 1995-2011 study period, staff adjusted the LCP to remove the costs of continued Trojan operation and immediate shutdown for 1993-1994. Because the costs of continued operation are less than the costs of shutdown in 1993-1994, the adjustment increases the net benefits of closing Trojan.

4. Adjustments to LCP to Reflect Allowable Costs

As previously stated, a net benefits analysis compares the allowable costs of continuing to operate a plant to the costs of closure. To help determine the correct amount of present and future allowable costs, staff retained the services of Theodore Barry and Associates (TBA), an independent firm specializing in providing consulting services pertaining to the energy and telecommunications industries. TBA has performed many nuclear plant reviews, management assessments, and audits, and it has testified in numerous power plant rate case proceedings. We find TBA qualified to advise staff in its net benefits review.

TBA evaluated the reasonableness of PGE's operation and management of Trojan from its initial commercial operation in [*79] 1976 through current delicensing and decommissioning activities. TBA described its standard of review as follows:

Whether PGE personnel, in managing activities associated with operations, maintenance, outages, engineering, modifications, quality assurance, and other activities at Trojan, made the decisions and took the actions, including the allocation of resources and the implementation of management and control systems, that a reasonable, experienced and competent manager of a licensed nuclear power facility would be expected to take, to operate and maintain the Trojan Nuclear Plant in a safe, reliable and cost effective manner. Where it appeared that such actions had possibly not been taken, and systems not implemented, we looked to see whether PGE management personnel took reasonable and timely actions to correct the situation.

TBA focused on those factors that represented the controllable elements of plant-related activities, in the context of information that was known, or was available to, and should have been known by PGE at the time. We were careful not to judge PGE's actions based on the results of its actions; rather we ascertained whether PGE made a reasonable choice [*80] from among the alternatives that were, or should have been available, i.e., we were careful to avoid the use of hindsight in our assessments.

In addition, we recognized that one or more courses of action can be deemed reasonable for a given set of circumstances, and did not limit our determination of reasonableness to only the best course of action, but considered the applicable range of reasonable actions in making our assessments.

TBA examined key areas of PGE's management and operation of Trojan to determine its reasonableness as well as its impact on key inputs for staff's net benefits analysis. Generally, TBA's evaluation can be divided into three major areas: (1) comparative performance analysis; (2) review of management issues; and (3) analysis of steam generator issues. TBA's evaluation and findings in these three areas are addressed separately, followed by a discussion of TBA's quantification of its findings for the net benefits analysis.

A. TBA's Comparative Performance Analysis

TBA compared Trojan's performance to that of other nuclear plants to help quantify the cumulative impact of the numerous controllable and uncontrollable factors on the plant's performance [*81] in the context of the performance achieved by comparable plants. TBA included several factors in its comparative analysis, including capacity factors, availability factors, O&M expenditures, Nuclear Regulatory Commission (NRC) Systematic Assessment of Licensee Performance (SALP) Report ratings, NRC Maintenance Team Inspection (MTI) Report ratings, and planned refueling outage duration.

Using these factors, TBA compared Trojan's performance to: (1) other single-unit nuclear plants; (2) other single-unit nuclear plants with pressurized water reactor (PWR) nuclear supply systems; (3) nuclear plants that began commercial operation between 1971 and 1981; and (4) all domestic nuclear plants. TBA selected those comparison groups to provide the maximum number of comparable nuclear plants for each parameter and include the plants with the characteristics most suitable for comparative purposes. In each comparison, TBA attempted to use as large a comparison group as possible in order to avoid skewing the data presented in the comparisons. At the same time, TBA was careful to exclude certain plants when the use of all nuclear plants would have been unfair to PGE. For instance, TBA excluded [*82] multiple-unit nuclear plants from O&M cost comparisons, because they typically have a lower O&M than single-unit plants such as Trojan. These comparison groups typically included from 26 to 40 nuclear units out of a total of approximately 100 units currently operating in the United States.

After its review, TBA determined that Trojan's lifetime performance on a total O&M cost/MWh generated basis was good, compared to plants that faced similar regulatory and management challenges. TBA further determined, however, that the favorable cost comparison was largely due to Trojan's relatively low O&M costs for most years prior to 1987, which compensated for the plant's relatively poor capacity factor performance. O&M costs increased significantly beginning in 1987, and TBA concluded that Trojan did not compare favorably to other single-unit nuclear plants in 1993, the year PGE decided to close Trojan.

TBA also drew several conclusions regarding specific factors identified above to be used in its analysis. Stated briefly, TBA found that:

- . Trojan's lifetime capacity and availability factors were significantly lower than the same factors for all domestic nuclear power plants through [*83] 1992.
- . Trojan had an economy of scale advantage over smaller single-unit plants.
- . Trojan performed favorably over its life on a nonfuel O&M cost/MWh generated basis, but significant O&M cost increases in 1987 and thereafter were an important factor in PGE's decision to close Trojan.
- . Trojan's low average capacity factor, together with its increasing O&M costs, caused the plant to be more costly in the early 1990s than the average for other single-unit plants.
- . PGE's SALP scores deteriorated from the early 1980s through the early 1990s.
- . Trojan's MTI performance was in the lowest (worst) quartile of plants reviewed, suggesting that PGE did not pay appropriate attention to Trojan maintenance activities.
- . Trojan's outage performance had a negative impact on capacity factor.

PGE disputes the validity of TBA's comparative analysis. It contends that TBA's findings are suspect for several reasons, including: (1) biased and improper comparison group selection; (2) biased and improper time period selection; and (3) incomplete data selection. PGE provides its own comparative performance analysis, which it believes establishes that Trojan cost performance throughout the [*84] period from 1976 through 1992 was exceptional as compared to a cross section of subgroups of nuclear plants.

After a review of both comparative analyses, we find TBA's study more reliable to help quantify the impact of numerous factors on Trojan's performance. TBA's conclusions are well reasoned and based on the most complete and appropriate information. We do not find PGE's comparative analysis persuasive and, for the following reasons, give it little weight. First, PGE's conclusions are based on a comparison of average performance over the life of Trojan and other nuclear plants. The use of lifetime performance averages, however, inappropriately masks Trojan's declining performance from 1987 through 1992, as well as industry trends in outage durations. Moreover, PGE did not base its LCP inputs on Trojan's lifetime average performance, but rather on Trojan's performance immediately prior to the formulation of the LCP.

Second, PGE inappropriately compared Trojan's performance to small subsets of plants that masked the impact of Trojan's regulatory compliance problems on its performance. For example, for its most comparable group of plants, PGE used selection criteria that resulted [*85] in a comparison group of only five other plants, many of which had poor performance characteristics. Similarly, PGE limited its comparison group for capacity factor and availability factor to 12 plants, eight of which were on the NRC's Watch List of Troubled Plants. We are more persuaded by the comparative analysis performed by TBA, which appropriately used minimum selection criteria to produce a large data set to dampen the effects of the best and worst performing plants, as well as the effects of individual plant performance anomalies.

We acknowledge that PGE made two comparisons that TBA did not--comparisons on the basis of revenue requirements and capital expenditures. However, revenue requirements are heavily influenced by historical factors, such as initial capitalization and subsequent capital additions. These factors are generally not as controllable by management as other cost components, such as O&M. Furthermore, PGE inappropriately assumed an identical return on book value for all nuclear plants. To adopt that assumption, PGE erroneously assumes an identical capital structure for all nuclear plants as well as equivalent authorized rates of return on each category of capital [*86] fund. PGE made additional errors that cast doubt on the reliability of its comparisons. For example, PGE compared initial and total nuclear plant capitalization costs after inflating to 1993 dollars, when annual revenue requirements are based on historical costs.

Finally, PGE criticizes TBA's use of SALP scores. The NRC generates a SALP report approximately once a year for each licensee. For the functional areas reviewed, the NRC assigns a numerical rating of 1, 2, or 3, with 1 being the highest rating and 3 the lowest. PGE argues that TBA's use of SALP scores to define reasonable management performance is improper. We agree that a determination of imprudence should not be based solely on a licensee's SALP score. Nonetheless, TBA properly used SALP scores to identify areas warranting further investigation, such as quality assurance, engineering management, and other areas addressed below.

B. TBA Review of PGE Management

TBA next examined PGE's management of the Trojan plant. Based on the comparative performance analysis and a preliminary review of Trojan documentation, TBA identified and examined several areas it believed had the greatest impact on Trojan's performance, [*87] particularly during the years immediately prior to PGE's decision to close the plant. The areas reviewed by TBA included PGE's quality assurance, engineering management, operations management, maintenance management, outage management, and regulatory compliance performance.

TBA's review found several areas where PGE's performance was good or exceptional. TBA found that Trojan placed twelfth among thirty-nine plants on the basis of lifetime O&M costs/MWh generated. TBA characterized PGE's overall emergency preparedness as good, noting that Trojan was one of the first plants to have a public warning system. TBA also rated PGE's performance in nuclear fuel management, steam generator inspection and repair, and delicensing as excellent. With regard to nuclear fuel management, TBA found that Trojan's fuel costs since the mid-1980s were generally ranked among the lowest of all domestic PWR plants. It concluded that PGE's actions to address steam generator degradation, once it realized that serious problems existed, were extensive, timely, and appropriate. Finally, TBA noted that PGE's delicensing activities allowed it to reduce staffing at the plant more rapidly than anticipated and achieve [*88] significant costs savings.

TBA further concluded that PGE's operations management was generally good. Although PGE's operations management of Trojan deteriorated significantly from 1980 through 1984, TBA found that PGE was able to sustain improved performance into the 1990s. By the late 1980s, TBA believes that PGE's operations management was so good that it may have saved Trojan from being added to the NRC's Watch List of Troubled Plants.

TBA also found several areas where PGE's performance was poor or deficient, however. Those areas are as follows:

Quality Assurance: Quality assurance (QA) comprises all planned and systematic actions necessary to ensure that the plant and its components will perform satisfactorily in service. QA requirements are prescribed in Title 10 of the Code of Federal Regulations (CFR), Part 50, Appendix B, and are enforced by the NRC.

TBA found that PGE's QA program was either deficient or seriously deficient throughout most of Trojan's commercial operation. TBA determined that the root causes for the deficiencies were: (1) insufficient management involvement in the QA program direction and review; and (2) an inappropriate focus on administrative [*89] audits rather than performance audits. TBA concluded that, despite warnings and opportunities to improve QA performance, PGE did not make the necessary changes until the 1990s. TBA believes that these avoidable deficiencies had a noticeable impact on PGE's regulatory compliance and engineering and maintenance performance in the mid-to-late 1980s.

Engineering Management: The primary engineering activities associated with an operating nuclear plant include the design and engineering of plant modifications and additions; providing technical input regarding the operation of plant equipment, components and systems; providing technical support regarding the resolution of plant problems; providing technical input regarding plant licensing issues; and directing and coordinating activities regarding the nuclear fuel cycle.

TBA found that PGE's overall engineering and engineering management performance was significantly deficient. TBA determined that: (1) PGE's propensity to minimize the use of outside engineering firms, and to maintain relatively low salaries for permanent engineering personnel, required it to rely heavily on contractor personnel, which caused dissatisfaction among [*90] permanent employees and affected performance;

(2) PGE's cost consciousness tended to limit opportunities for PGE's engineers to interface with others in the nuclear industry; (3) PGE's delay in moving engineers to the site limited their ability to become involved in plant-related activities; and (4) PGE's overall inability to effectively manage its engineering work force limited the effectiveness of its engineering support of plant activities. TBA concluded that the deficiencies were avoidable and severely affected PGE's regulatory compliance performance.

Maintenance management: Maintenance management comprises the management of the activities necessary to keep plant equipment, components, and systems in a state suitable for safe and reliable operation.

TBA found that PGE's overall maintenance performance deteriorated during the 1980s. TBA believes that these deficiencies contributed to PGE's overall declining performance in the mid-to-late 1980s and that the resulting cost impacts, while not as significant as in quality assurance and engineering, were avoidable.

Outage planning and management: Outage planning comprises the actions necessary, prior to an outage, to [*91] plan, schedule and prepare for outage activities in an efficient and timely manner. Outage management comprises the actions necessary to coordinate and perform the outage activities in an efficient and timely manner, including revising plans and schedules to accommodate changing conditions and emerging problems.

TBA found that Trojan's refueling outage performance was dismal starting in 1987. Among other things, TBA determined that Trojan's outages generally took significantly longer than planned. TBA concludes that the outage management deficiencies were avoidable and had a negative effect on Trojan's capacity factor.

Regulatory compliance: TBA examined PGE's recognition of and compliance with the regulatory requirements governing the engineering, design, operation, maintenance, and testing associated with Trojan's safety-related structures, systems, equipment and components. In its examination, TBA reviewed (1) the frequency of NRC-assessed violations at Trojan in the 1980s; (2) the impact of PGE's actions that were at the root of the violations; (3) the need to significantly improve PGE's performance on Trojan expenditures; and (4) the impact of all of the above factors [*92] on PGE's decision to close the plant prematurely.

TBA found that PGE's Trojan regulatory compliance was poor. This inadequacy, TBA determined, was caused by previously discussed management deficiencies, particularly in the areas of QA, engineering, operations management in the early 1980s, and maintenance management. TBA concluded that an important impact of PGE's poor regulatory compliance was increased O&M expenditures as the company attempted to "catch up" and improve performance. TBA noted that, during the period from 1986 to 1989, Trojan's nonfuel O&M expenditures increased from approximately \$ 52 million to \$ 102.3 million, an increase of almost 100 percent.

TBA also concluded that PGE ran a considerable risk in adopting a management strategy to minimize regulatory margin. The NRC defines minimum regulatory requirements for every aspect of nuclear operations. A nuclear plant's performance should exceed this minimum level to provide additional assurance that the plant operator will meet the minimum requirements. The level of performance above minimum regulatory requirements is called regulatory margin; the greater the margin, the greater assurance that the minimum requirements [*93] will be maintained. In order to maintain relatively low costs, PGE adopted a strategy of minimizing regulatory margin. TBA concluded, however, that the company's implementation of that strategy was seriously deficient. TBA found that PGE had failed to adopt appropriate criteria to guide its implementation activities, which prevented it from reacting appropriately to NRC feedback and concerns regarding its regulatory performance. TBA further found that the cumulative effect of these prior deficiencies made the implementation of corrective action in 1986 difficult, costly, and time consuming. TBA finally observed that, throughout the 1980s, the NRC assessed PGE with several Severity Level II and III violations and associated civil penalties as a result of the deficient regulatory compliance performance that resulted from its precarious strategy.

Summary: To summarize, TBA drew the following conclusions:

. Trojan was among the best performing nuclear plants in the early 1980s in terms of O&M cost/MWh generated and regulatory compliance.

. After 1982, Trojan's regulatory compliance began to deteriorate and, by 1987, Trojan's economic performance was declining due to significantly [*94] increased O&M costs with no offsetting improvement in capacity factors.

. By 1988, Trojan was among the worst nuclear plants.

. By 1992, Trojan had lost virtually all the prior cost advantage over other single-unit plants that it had achieved in the early 1980s through good management.

C. TBA's Analysis of the Steam Generator Issue

As a final area of its analysis, TBA examined numerous issues relating to the design, operation, and maintenance of the Trojan steam generators. TBA's review began with PGE's purchase of the steam generators from Westinghouse in 1968 and ran through PGE's decision to close Trojan in 1993.

TBA reviewed the steam generator design, PGE's purchase decision, and PGE's operation and care of the steam generators to determine, in part, how the equipment's degradation factored into the LCP and the net benefits analysis. TBA concluded that PGE acted prudently with regard to its steam generator degradation activities.

D. Quantification of Deficiencies for Net Benefits Analysis

In addition to its review of PGE's operation and management of Trojan, and partly in reliance on the findings from that investigation, TBA helped staff forecast certain [*95] key allowable costs of future Trojan operation. These three key components of the continued operation forecasts include: (1) O&M costs; (2) capacity factor; and (3) steam generator costs. In quantifying the impacts of PGE's management deficiencies, TBA applied a performance standard of what PGE could reasonably have achieved. TBA's quantification methodologies resulted in a range of values for the various inputs. The two extremes of each range are equally likely for the purpose of determining allowable costs. However, because the range reflects a prediction of costs that would have been allowed in future rate cases, only one value in the range would have been allowed and any amount above that would have been disallowed.

For the purposes of the net benefits analysis, staff used the midpoint of each range, because it represents the middle point between equally likely higher and lower values. Staff assumed a flat distribution, because it had no basis for concluding that any one point in the range was more likely than another. PGE challenges staff's use of midpoints, asserting that staff's methodology ignores other potentially acceptable values in the ranges of assumptions. We disagree. [*96] Staff supported its use of the midpoint values with a probabilistic analysis by: (1) assuming a uniform probability distribution over each range, i.e., assuming that all values in a range are equally probable and values outside the range have zero probability of occurring; (2) selecting a value from each range at random; (3) calculating the net benefit with the values selected; (4) repeating the input selection and the net benefit calculation many times; and (5) averaging the resulting net benefits estimates. Staff's analysis determined that the average expected net benefit is approximately the same as that determined by selecting the midpoint values. Furthermore, staff's approach is similar to the one PGE used in its least-cost planning analysis. PGE reported the expected value of the difference in costs between continued plant operation and phase-out from its probabilistic analysis, just as staff has done for net benefits.

As discussed above, TBA's review of PGE's operation of Trojan revealed management deficiencies that resulted in significant cost increases from 1987 to 1992. From those findings, TBA concluded that PGE's least-cost planning analysis forecasted significantly [*97] greater, and inappropriate, O&M costs, an inappropriately low capacity factor, and inappropriate costs related to steam generators. We address each issue separately.

O&M Costs and Escalation Rates: TBA considered three primary factors in determining a reasonable level of Trojan's 1993 O&M expenditures: (1) PGE's actual budget for Trojan's 1993 expenditures; (2) the impact of the steam generator issue on Trojan's 1993 O&M budget; and (3) the impact of PGE's management deficiencies, prior to and during 1992, on Trojan's O&M budget. On a related issue, TBA also calculated appropriate O&M cost escalation factors for use in staff's updated net benefits analysis.

In its cost calculation, TBA started with Trojan's 1993 nonfuel O&M budget of \$ 115.8 million. It then reduced that figure by \$ 5.3 million to account for avoidable steam generator inspection and repair costs. This left \$ 110.5 million. TBA then reduced the \$ 110.5 million O&M cost level by 5 to 10 percent. TBA concluded that this additional reduction was necessary to reflect a previous management cost advantage that PGE should have been able to maintain due to its management strategy of minimizing costs while attempting [*98] to minimize regulatory margin. TBA's result is an allowable 1993 nonfuel O&M range of \$ 99.5 to \$ 105.0 million. The midpoint of TBA's range, \$ 102.3 million, is within a range for the average nonfuel O&M expenditure for single-unit plants in 1993, adjusted for Trojan's economy of scale and management strategy cost advantage.

With regard to O&M cost escalation factors, TBA looked at industry data for the period 1981 through 1993. Based on that historical industry data, as well as current regulatory reform initiatives and increased competitiveness in electricity markets, TBA believes a 0 percent real O&M escalation factor is appropriate for the period from the present through 1996, while an O&M projected real growth rate of 0 to 3 percent is appropriate for the period 1997 through 2011.

PGE challenges both of TBA's calculations. First, PGE contends that TBA's projection for Trojan's 1993 O&M expenditures is too low, asserting that TBA applied a standard of perfection in determining the input for the net benefits analysis. PGE contends that the proper standard of performance for quantifying the company's imprudence should be based on industry average performance, rather than the [*99] performance PGE could reasonably have achieved with its management strategy advantage and the economy of scale advantage inherent in a plant with Trojan's capacity. We disagree. In recognition of the fact that Trojan was located in a low-cost market, PGE adopted a management strategy that minimized costs while also attempting to minimize regulatory margin. TBA's quantification of PGE's imprudence, therefore, is appropriately based on PGE's failure to maintain its management strategy, while also recognizing that PGE's actual regulatory margin was inappropriate. In other words, TBA did not apply a standard of perfection, but rather an appropriate performance standard of what PGE could have reasonably achieved.

PGE also challenges TBA's inclusion of newer single-unit plants in its comparison group to verify the reasonableness of the results of its quantification of Trojan's 1993 nonfuel O&M expenditures. PGE contends that Trojan costs are more appropriately compared with those plants that began operation between 1971 and 1981. We find TBA's comparison group appropriate. Trojan's MW rating made it the largest single-unit plant placed into operation prior to 1982. Trojan's economy of [*100] scale advantage, therefore, can and should be measured against the average of all single-unit plants. Similarly, PGE's management advantage was a function of economics, which relates to all single-unit plants, not merely a particular vintage of plant.

PGE further argues that Trojan's 1993 budget is not appropriate to use as a starting point for determining the nonfuel O&M cost input, because PGE had already made a decision to phase out the plant in 1996 and had begun to cut back on programs and costs. However, PGE's 1993 budget was approximately \$ 11 million greater than its actual 1992 nonfuel O&M expenditures, a significantly greater increase than the average nonfuel O&M costs increases for other single-unit plants for that period. Moreover, PGE identified a reduction in its 1993 budget of only \$ 2.2 million for programs that were to be either scaled back or eliminated due to its decision to phase out the plant in 1996.

With regard to TBA's O&M escalation factors, PGE claims that O&M escalation should be three percent real from 1993 forward, rather than TBA's proposed 0 percent real until 1997 and a range of 0 to 3 percent thereafter. However, TBA reviewed the nuclear industry's [*101] real nonfuel O&M per KW for 1989-1993 and found that it declined by an average of 0.53 percent per year. This fact was partially anticipated by PGE in its 1992 Plan, in which PGE stated:

In addition, hindsight now shows that increased regulatory activity following Three Mile Island (TMI) caused many of the historical increases above inflation in fixed O&M and capital costs. The industry has essentially completed the TMI-related work, and industry data indicates that recent nuclear O&M expenditures have leveled and may possibly indicate a decreasing trend.

Moreover, TBA persuasively argues that this downward trend is sustainable and may even intensify because of: (1) industry-wide efforts to reduce regulatory costs; and (2) increasing competition in the electric utility industry. For these

reasons, we find TBA's 1993 O&M cost estimates and O&M escalation factors appropriate for inclusion in staff's net benefits analysis.

Capacity Factor: To determine an appropriate capacity factor for Trojan for 1993, TBA considered the following five factors: (1) PGE's capacity factor projections for Trojan; (2) the capacity factor achieved at similar plants; (3) the impact of the steam [*102] generator issue on Trojan's capacity factor; (4) the impact of PGE's outage planning deficiencies; and (5) the impact of Trojan's twelve-month operating cycle.

To make its determination, TBA utilized the median of 1991-1993 average design electrical rating net capacity factors for 50 large domestic reactors like Trojan, rated at 1020 MW and above. It then adjusted that figure to eliminate the impact of steam generator tube problems, then credited Trojan for the adverse impact of its twelve-month operating cycle. TBA's quantification determined that Trojan's capacity factor should have been at least 67.6 to 71.6 percent. Staff chose the midpoint of this range, 69.6 percent, as its imputed capacity factor for Trojan.

PGE contends that staff's projection is too high. It first challenges TBA's use of the median 1991-1993 average design electrical rating net capacity factors for domestic reactors rated at 1020 MW and above. It contends that the most appropriate comparison group for a capacity factor quantification consists of plants larger than 1000 MW and placed in service between 1971 and 1981. We disagree. Again, PGE's narrowly defined comparison group inappropriately skews the [*103] results of its analysis. Its comparison group consists of only twelve plants, many of which were out of service during extended periods of time, thus lowering the capacity factor average. It is also important to note that TBA's comparison group included many boiling water reactors (BWR), which had an average capacity factor that was 8.6 percent less than pressurized water reactors like Trojan in 1991-1993. The influence of BWR units in TBA's comparison group, combined with PGE's own projection for a significant capacity factor improvement after steam generator replacement, supports TBA's conclusion that Trojan's capacity factor should have been at least 67.6 to 71.6 percent.

PGE also challenges TBA's adjustment to the capacity factor to account for steam generator problems. TBA's adjustment was based on an Electric Power Research Institute (EPRI) report formulated specifically for the purpose of determining the impact of steam generator problems on capacity factor. We do not find PGE's argument persuasive and reject it.

Steam Generator: PGE's least-cost plan analysis includes steam generator repair costs in O&M expenditure projections, steam generator replacement costs in capital [*104] expenditure projections, and capacity factor reductions for steam generator repair and replacement activities through 1996. TBA concluded that PGE's liability for the steam generator problems was not accounted for in its LCP. This issue is further addressed below as part of Issue S-49, Steam Generator Plugging, Sleeveing, and Analysis and Spare Reactor Coolant Pump Motor. We disallow both the inclusion of steam generator replacement costs from the LCP (approximately \$ 183.1 million) and the post-1991 capital expenditures.

As an additional issue, PGE contends that staff's use of the LCP inappropriately assigns the benefit of a planned 45 MW uprate to the ratepayers. An uprate is an increase in a plant's electrical production capacity and usually comprises a change in plant operating parameters, such as pressure or temperature, that allow existing plant equipment to produce a greater amount of electricity. PGE's 1992 Plan includes a 45 MW increase in Trojan capacity at the time of planned steam generator replacement in 1996. PGE argues that the benefits of the added capacity should be removed if no steam generator replacement is included in the net benefits analysis. PGE explains in [*105] its rebuttal testimony:

If we must assume that customers would not pay for the cost of the new steam generators, then we must also assume that they do not receive any incremental benefits associated with the new steam generators.

The replacement of the Trojan steam generators would have provided PGE with the opportunity to "piggyback" the costs associated with obtaining regulatory approval for a power uprating onto the costs necessary to obtain regulatory approval for operation with the replacement steam generators. TBA concluded, however, that PGE could have achieved the 45 MW uprate with the original steam generators, had they not been defective. In fact, PGE considered a 45 MW uprate using the original steam generators in the late 1980s. PGE ultimately determined that the uprating was not feasible, however, due to the defects in the original steam generators that required a significant number of tubes to be

plugged. Moreover, without the many plugged tubes, an uprating could have been accomplished at a cost of only a few million dollars, as compared to the significant costs of steam generator replacement. For these reasons, we conclude that the benefits of the additional [*106] 45 MW of additional capacity that PGE included in its least-cost plan scenario are properly included in the net benefits analysis.

Staff's Conclusions from Net Benefits Analysis

Adjusting PGE's least-cost planning results, staff concluded that, for the 1995-2011 test period, the premature closure of Trojan resulted in a negative net benefit of approximately \$ 23.6 million. In reaching that conclusion, staff used the midpoints of the ranges developed by TBA for 1993 fixed O&M, fixed O&M escalation factors, and capacity factors. Staff also removed the costs of steam generator replacement from the LCP results, for reasons addressed below as part of Issue S-49, Steam Generator Plugging, Sleeving, and Analysis and Spare Reactor Coolant Pump Motor.

Based on its net benefits analysis, staff concludes that continued operation of Trojan would have cost less than immediate shutdown in the absence of steam generator defects and management errors at Trojan. Accordingly, staff recommends that we should hold PGE's ratepayers harmless from the effects of the steam generator defects and management failures by disallowing \$ 23.6 million of the company's remaining investment in the plant.

[*107]

Position of Other Parties

As an additional issue, CUB and Kullberg argue that the decision to build Trojan was imprudent in and of itself. CUB compares Trojan's cost with the cost and performance of coal plants after Trojan was completed and brought on line. The comparison is not well supported. A prudence review takes into account the information that was available to decision makers at the time the decision was made. It does not engage in hindsight or second-guessing; to do so would be unfair. PGE could not have known those data about coal plants at the time it decided to build Trojan. The record does not contain evidence about what information was available to PGE when it decided to build Trojan, and it cannot support a decision of any kind on that issue.

Moreover, every rate case the Commission has decided since Trojan began operating has included Trojan in rate base. It would be inappropriate now to overturn the decisions in each of those rate orders from 1976 on.

Disposition - S-50: Remove Additional Fixed Costs--Net Benefits Analysis

We conclude that the allocation of the remaining Trojan investment is properly determined by a net benefits analysis. The purpose [*108] of a net benefits test is to identify the point at which ratepayers are indifferent between the options of continued operation of Trojan and shutdown and construction or acquisition of replacement resources. Application of the test is intended to hold ratepayers harmless for a utility's poor operation or management.

Staff evaluated numerous issues presented by a net benefits review. It retained an expert witness, TBA, to review PGE's operation and management of Trojan. In its review, TBA applied a reasonable person standard, similar to that commonly employed in utility prudence review proceedings. TBA based its evaluation on information available to a decision maker at the time of the decision. Based on TBA's findings, staff completed a quantitative analysis to determine whether assessing ratepayers 100 percent of Trojan's remaining costs is in the public interest. After revising its net benefits analysis to incorporate some changes suggested in PGE's rebuttal testimony, staff determined that the premature closure of Trojan resulted in a negative net benefit of approximately \$ 23.6 million. With the adjustments described below, we adopt staff's net benefits analysis.

Adjustments [*109] **to Staff's Net Benefits Case:** Staff's initial net benefits analysis did not include seven potential adjustments that were not quantified or that were raised during the Phase II hearings. We have reviewed those adjustments and adopt them with the correction and exception noted below. We also adjust the estimated net benefit to recognize the interaction among the individual adjustments, as discussed below.

1. 45 MW Increase in Trojan Capacity. Staff's analysis assumed that the 45 MW uprate would have taken place in 1996, along with the steam generator replacement, as PGE had assumed in its LCP. However, if the steam generator degradation had not occurred, the increase could have been achieved without replacing the steam generators. Assuming

a date earlier than 1996 would reduce the net benefit of closing Trojan, because the extra 45 MW would obviate the need for 45 MW of power from other resources. Staff included the 45 MW capacity increase in its net benefits analysis starting in July 1996.

CUB calculated that moving the start date back to the beginning of the test period (January 1995) would reduce the net benefit of closing Trojan by \$ 7.7 million (PGE share, 1995 dollars). [*110] We find that CUB's calculation is incorrect because: (1) it does not account for the variable O&M associated with additional generation; (2) it does not recognize that the costs used are expressed in 1993 dollars; and (3) it does not discount the value of the additional generation properly. The corrected figure (using CUB's assumed 65 percent capacity factor) is \$ 6.1 million.

We find the corrected adjustment reasonable and adopt it.

2. Capacity factor. In its capacity factor quantification, TBA determined that the industry median capacity factor was depressed as a result of steam generator problems. Relying on a study by EPRI, TBA concluded that the capacity factor should be increased by 2.6 percent to adjust for the steam generator tube problems. At hearing, however, CUB demonstrated that TBA had overlooked the fact that the EPRI study also indicated that steam generator replacement activities reduced capacity factors by an additional .65 percent. TBA testified that its imputed capacity factor range should be increased by this amount to accurately account for all of the effects of the steam generator problems. Staff, in turn, testified that such an adjustment in TBA's range [*111] would also increase its mid-point imputed capacity factor by .65 percent, for a value of 70.25 percent. Increasing capacity factor by .65 percent reduces the net benefits of closure by \$ 20.5 million (PGE share, 1995 dollars).

We find this adjustment reasonable and adopt it.

3. Fixed O&M . Staff's base case used the mid-point of TBA's O&M range, \$ 102.25 million, for allowable fixed O&M for 1993. TBA's nonfuel O&M, however, is not the same as PGE's fixed O&M. PGE treated variable O&M as separate from nuclear fuel costs. Therefore, allowable fixed O&M should be determined by subtracting variable O&M from TBA's nonfuel O&M estimates.

At the 60 percent Trojan capacity factor assumed for 1993, variable O&M totals \$ 5.8 million. Subtracting this figure from TBA's nonfuel O&M produces a range for fixed O&M of \$ 93.7 million to \$ 99.2 million, with a midpoint of \$ 96.45 million. This \$ 5.8 million reduction in fixed O&M, extrapolated out over the study period, and using the O&M escalation figure in staff's surrebuttal testimony, reduces the net benefit of closure by \$ 51.8 million (PGE share, 1995 dollars).

We find this adjustment reasonable and adopt it.

4. Nuclear Fuel [*112] **Costs.** Nuclear fuel estimates are necessary to compare the cost of operating Trojan at a given capacity factor to the cost of replacement resources used to generate an equivalent amount of energy. In combining the results from the two parts of the LCP, staff assumed that the 1992 Plan numbers for fuel costs in Case 1b were calculated in the same manner and contained the same assumptions as the Update's Scenario 3. Based on that assumption, staff combined the results of Case 1b and Scenario 3 for use in its net benefits analysis. PGE explained, however, that it used lower nuclear fuel costs during phase-out in the Update than in the 1992 Plan. Accordingly, the net benefits analysis should use consistent assumptions to estimate nuclear fuel costs. This correction increases the net benefit of closure by \$ 25.7 million (PGE share, 1995 dollars).

We find this adjustment reasonable and adopt the updated figure.

5. Transition Costs. Staff reduced the cost of the immediate shutdown alternative to recognize the fact that PGE has experienced lower transition costs than assumed in the least cost plan. Staff's net benefit estimates do not include any corresponding transition cost savings [*113] under continued Trojan operation with shutdown in 2011. If transition costs in PGE's LCP were overestimated for immediate closure, staff believes that they may also have been overstated for continued plant operation. Staff concluded that some savings in transition costs after 2011 would be likely. Recognizing these savings would reduce the net benefit of immediate closure. Staff does not suggest a figure to represent sav-

ings in transition costs after 2011, although CUB quantifies the savings at \$ 30.8 million, starting from the same \$ 65.6 million for which staff adjusted the cost of immediate closure (PGE share, 1995 dollars).

PGE describes its reduction in transition costs over its LCP projections as the result of aggressive and quick cutting of costs. Staff does not challenge that description.

We do not adopt this post-2011 adjustment. Staff was not certain that transition costs were actually overstated for continued plant operation, and did not quantify the amount. CUB's quantification, in view of staff's circumspect approach to this issue, is not supported by the record. CUB simply assumes that the savings would be the same for continued operation. Moreover, PGE achieved [*114] some of the savings by aggressive action. Imputing a lower than projected cost to transition in 2011 is tantamount to penalizing PGE for acting quickly to cut costs.

6. Carrying charges. It is standard industry practice to recognize a small amount of capital replacement in the fixed O&M assumptions for combustion turbines. While PGE's fixed O&M assumptions were consistent with this practice, the company also accounted for capital replacement costs in carrying charges in the 1992 Plan. To conform with other forecasts in the industry, and to eliminate any double-counting of costs, PGE subsequently reduced the carrying charges to eliminate the allowance of capital replacements beginning with its 1993 avoided cost filing.

PGE argues that the net benefit analysis should also use the carrying cost rate from the 1992 Plan corrected to eliminate the inclusion of interim capital additions for new combustion turbine generating plants. We agree. Although the reduction in capital costs exceeds PGE's fixed O&M assumptions, the adjustment to the carrying charges reflects industry practice of assuming very small capital additions for combustion turbines. Moreover, we approved PGE's projections [*115] of the capital costs of combustion turbines in acting on the company's 1993 and 1994 avoided cost filings. The net benefits test should use the capital additions assumptions as updated in those avoided cost filings. Using corrected carrying cost rates increases the net benefit of closure by \$ 68.9 million (PGE share, 1995 dollars).

We find this adjustment reasonable and adopt it.

7. Capital Costs of New Gas-Fired Resource. Staff's net benefit figures for the cost of replacement resources are based on PGE's least-cost planning estimate of the capital cost of a combined-cycle combustion turbine, the principal resource replacing Trojan. PGE's figure is lower than those being used by PacifiCorp and the NWPPC in their current planning processes. PGE estimates the capital costs for the turbine at \$ 550/KW, PacifiCorp at \$ 586/KW, and NWPPC at \$ 630/KW. PGE has not shown why its estimate is so much lower than that of the other entities. Substituting PacifiCorp's estimate for PGE's would make the net benefits analysis more negative by \$ 16.0 million (PGE share, 1995 dollars).

We conclude that PGE has not shown why its estimate is more reasonable than the other, higher estimates [*116] in question. We find it more reasonable to adopt the middle estimate, \$ 586/KW, and adjust staff's analysis accordingly.

Adjustment for Interactions. A further change in the net benefits estimate is needed to account for interactions among the individual adjustments described above. Increasing capacity factor by .65 percent, for example, increases the value of advancing the 45 MW capacity increase at Trojan to January 1995. Revising carrying charges changes the effect of updating the capital cost of replacement resources. Using the staff's net benefits model, we find that recognizing all the interactions increases net benefits by \$ 3.0 million, and we adjust the net benefits estimate accordingly.

Summary of Adjustments

The following table summarizes the effects of the adjustments discussed above:

Staff's net benefits analysis result	-\$ 23.6 million
Adjustments to Staff's Calculations	
January 1995-June 1996 uprate to 45 MW	-\$ 6.1 million
Increase capacity factor by .65 percent	-\$ 20.5 million

Decreasing Imputed Fixed O&M by \$ 5.8 million	-\$ 51.8 million
Update to nuclear fuel assumptions	+\$ 25.7 million
Update to staff's carrying costs	+\$ 68.9 million
Update to capital costs of replacement resources	-\$ 16.0 million
Adjustment for interaction	+\$ 3.0 million
Total effect of adjustments	+\$ 3.2 million
Total of adjustments and staff's net benefits calculation	-\$ 20.4 million
Post-1991 disallowances	-\$ 17.1 million
Total disallowance including post-1991 expenditures	-\$ 37.5 million

[*117]

Remaining Ratepayer Share

Trojan Investment

\$ 288.2 million \$ 250.7 million 87 percent

We find that with these adjustments, the net benefits analysis approximates the point at which ratepayers are indifferent between continued operation of Trojan and shutdown, with replacement of the generating resource. We also find that this recovery under the adjusted net benefits analysis is in the public interest. ORS 757.140(2).

Transition Costs

TBA also reviewed PGE's 1993-1996 transition costs. PGE defined transition costs as "the operations and corporate overhead costs associated with closing Trojan, operating and maintaining the spent fuel pool, and securing the plant until dismantlement can begin." TBA determined that the transition costs included in the proposed test years are reasonable, and staff recommends full recovery of the amount requested by PGE. We adopt staff's recommendation.

S-45: Trojan Overtime

Staff proposes the removal of all overtime compensation budgeted by PGE for the Trojan plant in its filing. Staff notes that the plant was permanently shut down in January 1993, and requires only security, monitoring, and maintenance staff. Staff believes that [*118] PGE's personnel levels are adequate to accomplish those activities without the need for overtime. PGE disputes staff's proposed adjustment, but does not provide sufficient explanation to justify recovery of those costs. After a review of this matter, we agree that the budgeted overtime should be removed.

S-46: Trojan Investment Classification

The Commission has adopted the FERC Uniform System of Accounts as a basis for utility accounting requirements. The Uniform System of Accounts is a comprehensive basis of accounting and provides, among other things, distinct accounts for assets and other debits.

In its filing, PGE proposes to leave certain Trojan assets in FERC Account 101, Plant in Service, an account designated for original costs of electric plant owned and used by the utility in its electric utility operations. PGE believes that the assets, which primarily include the spent fuel pool and related systems, as well as the administrative buildings, should

continue to be classified as plant in service because they remain used and useful for the purpose for which they were intended. Staff disagrees with PGE's proposal and recommends that all net investment in Trojan systems, [*119] including Trojan Material and Supplies Inventory, be placed in FERC Account 182.2, Unrecovered Plant and Regulatory Study Costs. That account is defined to include significant unrecovered costs of plant facilities that have been prematurely retired. Because both accounts are included in PGE's rate base, transferring investment between the accounts will not affect the rate base.

PGE and staff agree that the placement of plant in FERC Account 101 means that the plant is "used and useful in the public service." PGE contends that that requirement is met, because the Trojan plant remaining in that account protects public health and safety, provides security, or provides office space and facilities for the employees that remain on the site. As staff notes, however, the original purpose of the assets in question was to be part of an operating plant that was providing service to rate payers. That plant has now been permanently shut down, and those assets are now used only to provide the service necessary for safety and asset preservation pending decommissioning and dismantling of the plant. Moreover, while the spent fuel at Trojan is the result of "used and useful" service by the plant, [*120] it is being stored at Trojan only because the United States Department of Energy (USDOE) has failed to establish a permanent federal repository for nuclear waste. In short, the continuing activities at Trojan are related to decommissioning, not productive operation of the facility.

We acknowledge that there is no prescribed method of accounting for nuclear plants that are in the process of being decommissioned. FERC is currently working on a position paper regarding this issue, but it has not yet been issued. The Financial Accounting Standards Board (FASB), however, has taken a position on accounting for plant that is removed from service. In its Statement 90, the FASB states:

When it becomes probable that an operating asset or an asset under construction will be abandoned, the cost of that asset shall be removed from construction work-in-progress or plant-in-service.

For these reasons, we find that the Trojan plant is no longer used and useful. All the Trojan plant investment, including accumulated depreciation, accumulated deferred income tax, and deferred investment tax credit, as well as Trojan Materials and Supplies Inventory, should be transferred to FERC Account 182.2, [*121] Unrecovered Plant and Regulatory Study Costs. PGE's filing should be modified accordingly.

S-47: Trojan Salvage Proceeds

Staff also recommends that the unrecovered Trojan plant placed in FERC Account 182.2 be reduced to reflect a greater amount of projected recovery through salvage sales of surplus Trojan assets. Staff believes that PGE's original estimate of salvage recovery of \$ 6.7 million is reasonable for the equipment that was included in the estimate, but adds that the estimate does not include any recovery for the buildings or certain installed plant equipment. Because the costs of the installed plant equipment and unused buildings are significant, staff proposes that the estimated salvage proceeds be increased by \$ 6 million, for a total amount of \$ 12.7 million, PGE share.

PGE acknowledges that the revised estimate of salvage recovery does not include any recovery for buildings and only \$ 506,000 for installed plant equipment. The company argues, however, that it is unrealistic to expect that salvage sales will exceed the level predicted. PGE notes that it has aggressively attempted to market installed plant equipment to foreign nations, but adds that no major [*122] sales are pending. It also cites numerous efforts to market the approximate 149,000 square feet of space available for sale or lease at Trojan. Those efforts, however, have generated little interest.

Both PGE and staff agree that the sales of surplus Trojan assets through 1995 and 1996 are difficult to determine. The book value of the underlying Trojan assets, however, is significant. According to PGE's numbers and classification, the value of plant items and materials and supplies is approximately \$ 232 million after reductions of PGE's estimated salvage sales. We share staff's concern that the use of low salvage estimates for those assets would cause the rate base and amortization expense to be too high.

Accordingly, we find staff's proposed adjustments reasonable and adopt them. If actual salvage is less than staff's projection, PGE's loss will be limited to the return on the difference between staff's estimate and the company's estimate for the period between the end of this rate case and the end of the next one. Actual recovery will have been determined by the time of that next rate case, and any shortfall can be returned to PGE's rate base.

S-48: Trojan Decommissioning

[*123]

Definition of Decommissioning. According to the Rules and Regulations of the NRC (10 CFR 50.2), "'Decommission' means to remove [a facility] safely from service and reduce residual radioactivity to a level that permits release of the property for unrestricted use." In this docket, staff has used a more inclusive definition of decommissioning. The NRC's definition refers only to those portions of a facility affected by radioactivity, but staff uses the term to include all activities related to removing total plant from service and restoring the site to unrestricted use. We adopt staff's usage of "decommission." We also adopt staff's definition of decommissioning cost as the total cost of removing Trojan from service, net of any salvage recovery.

Decommissioning Costs: Capital or Noncapital? When we entered our decision in DR 10, staff considered decommissioning costs to be a noncapital expense. See Order No. 93-1117 at 14. In the meantime, staff has reconsidered its position. It now considers decommissioning costs to be capital costs. Capital costs may be recovered under ORS 757.140(2).

Staff reached its current conclusion about [*124] decommissioning costs by determining that decommissioning costs are conceptually equivalent to the negative net salvage value of property removed from service. If that equivalence is valid, decommissioning costs are capital costs because salvage value is associated with capital investment (property).

Net salvage value (the difference between salvage value and cost of removal) is a depreciation concept. Depreciation is the method this Commission uses to provide for the recovery of the total investment in property and the cost of removal of that property from service at the end of its estimated life. Positive net salvage value reduces the rate of depreciation. Negative net salvage value increases the depreciation rate. If the cost of removal is greater than the salvage value of the property, then the sum to be recovered will be greater than the original investment.

The following formula expresses the equivalence of decommissioning costs and net negative salvage:

$$D = SV - CR$$

where D = decommissioning costs; SV = salvage value; and CR = cost of removal. We agree with staff that decommissioning costs are equivalent to negative net salvage value and are therefore capital costs.

[*125] **Background of Trojan Decommissioning.** When Trojan went into service in 1976, PGE included an allowance for net salvage in its depreciation rates. Negative net salvage percentages were attributed to the Structure & Improvements account and the Reactor Plant Equipment account. By Order No. 79-055, the Commission required the company to make a decommissioning cost study as the basis for estimating the cost of taking the plant out of service. PGE submitted the study and a funding proposal in 1979. The Commission approved the plan and the funding proposal in Order No. 80-612, issued August 18, 1980.

PGE's 1979 plan called for the plant to lie dormant for 100 years after its closing, at which time it was to be dismantled. PGE proposed to fund the decommissioning through an internal sinking fund account within its depreciation reserve.

In Order No. 91-186 (UE 79), consistent with rule changes of the NRC, the Commission adopted a new decommissioning plan and cost estimate. The new plan called for the immediate dismantling of the plant at the end of its estimated life (2011). The decommissioning fund was changed from an internal fund to an external trust fund administered by an independent [*126] trustee, pursuant to NRC requirements. The fund balance was \$ 48.9 million at the end of 1993.

Current Plan. In this docket, PGE has proposed a revised decommissioning plan. The principal elements of its plan are:

1. Early large component removal. The company plans to remove the steam generators and pressurizer for burial by December 1995.
2. Construction of a "dry" on-site fuel storage facility for long-term storage of spent nuclear fuel. The facility would be completed by 1998 and the spent fuel would be stored there until shipment to a permanent federal storage facility (target date: 2018).
3. Removal and dismantling of all contaminated systems and some building demolition from 1998 through 2002.
4. Site restoration activities. After the shipment off-site of the spent fuel in 2018, all facilities with no further value will be dismantled and the site made available for unrestricted use. This will occur from 2018 through 2023.

PGE notes that early implementation of decommissioning will give its customers the benefit of current low burial rates and mitigate the risk of losing access to a low-level radioactive waste burial site.

Funding of the Current Decommissioning [*127] **Plan.** Beginning in 1995, PGE proposes to contribute \$ 14,041,000 annually to the external trust fund. The contribution will continue through the year 2011. The period ending in 2011 was chosen for distributing decommissioning costs because that is the period over which the Trojan closure is expected to produce benefits. After 2011, Trojan would have been replaced by other resources in any case, so the generation of ratepayers after 2011 should not share in decommissioning costs.

PGE's proposal to contribute an equal amount each year to the external trust fund is a departure from the method of contribution adopted in UE 79. In that docket, it was assumed that Trojan would operate until 2011, and the Commission adopted a funding plan under which each generation of customers would contribute equally on a real levelized basis, with payments increasing over time to offset the effect of inflation. The real levelized funding plan would have matched costs with benefits received by the ratepayers. That is, ratepayers receiving the benefit of the plant would pay for its decommissioning. PGE's current contribution under this plan is \$ 11,220,000 in 1994, which would have increased to \$ 21,120,000 [*128] by 2011.

Trojan was shut down in 1993, however. The company now proposes a nominal level contribution. The payment into the decommissioning fund will be the same each year. Under this plan, in real terms, decommissioning costs to future ratepayers will decline because of inflation. The increased level of current contribution is required because Trojan shut down earlier than expected. The current payment to the decommissioning fund is inadequate and must be increased.

Even with the proposed increase in annual contribution, the company will have to borrow to bridge its needs. As currently estimated, however, the cash flows will eventually fund the cost of decommissioning including repayment of the interim financing. The company's investment strategy concentrates on municipal and corporate bonds.

PGE's Efforts to Involve Other Entities. In DR 10, we imposed the condition that PGE involve other entities in its decommissioning efforts. PGE has held discussions with the NRC, USDOE, EPRI, and other utilities. It has performed work relating to steam generators for Duke Power's Catawba plant, and has other proposed programs. The NRC has shown interest in performing containment tendon [*129] grease leakage studies and electrical cable aging studies at the Trojan facility.

Staff's Review of PGE's Plan and Funding Proposal. As part of its case, staff reviewed both PGE's decommissioning plan itself and the proposal for funding it. Staff asserts that PGE's decommissioning plan meets all criteria of the NRC and the Oregon Energy Facility Siting Council and recommends that we adopt it. In addition, staff states that PGE's proposal is the least-cost decommissioning option. Staff also notes that, as the process of decommissioning evolves, PGE will doubtless find it necessary to make changes in its total cost estimate. The plan and its funding mechanism should therefore be subject to regular, ongoing review by the Commission and staff. Necessary changes in authority granted to PGE by the Commission can be made in future dockets.

Positions of URP and Kullberg. URP first contends that PGE's proposal is not prudent under the circumstances and that ratepayers should not have to pay for it. URP believes that PGE's decommissioning plan disadvantages PGE in its pending suit against Westinghouse because the large component removal destroys evidence that PGE needs in its lawsuit [*130] and possibly in other forums.

Second, URP contends that the NRC may order modifications to PGE's decommissioning plan and that Commission approval is therefore premature. Kullberg also argues that decommissioning costs should not be reflected in rates prior to NRC approval of the plan. Kullberg has specific disagreements with PGE's plan as well, and urges that decommissioning should be delayed to gather more information and reduce uncertainty about a number of elements of the plan.

In response to URP's first contention, we are not persuaded that PGE's removal of the steam generators will harm ratepayers, especially since this order disallows the post-1991 steam generator costs. The first of URP's arguments is rejected.

As to waiting for NRC approval, we understand that the final plan may differ in some respects from the current proposal. We also understand that as decommissioning proceeds, it may be necessary to make still further revisions in the plan or its financing. We acknowledge that there is a great deal of uncertainty in the whole area of decommissioning. Therefore, PGE's decommissioning plan and its funding mechanism will be subject to regular, ongoing review by the [*131] Commission and staff. Necessary changes in authority granted to PGE by the Commission can be made in future dockets. We conclude that it is not necessary to wait for NRC approval before approving PGE's decommissioning proposal.

As to the request that decommissioning be delayed pending further study, we find it more likely than not, based on the record before us, that delay in implementing the plan will increase the costs of decommissioning. That is an undesirable outcome. Moreover, early decommissioning allows PGE to take advantage of disposal site availability. Continued Commission oversight of the decommissioning process will address the question of changing circumstances as decommissioning proceeds. The arguments for delay are rejected.

DR 10 and Recovery of Decommissioning Costs. In DR 10, Order No. 93-1117, we concluded that we would consider favorably allowing PGE to recover Trojan's decommissioning costs in rates, if PGE met the following conditions:

1. PGE must prove all six assumed facts in a rate case or similar forum. (See the section above, "Applicable Law," for the six assumed facts.)
2. PGE must show that it pursued the least-cost decommissioning option [*132] consistent with directives from the Nuclear Regulatory Commission and other agencies.
3. PGE must show that it has made a reasonable effort to ascertain if other entities wishing to gain valuable experience in decommissioning a nuclear plant of this size would participate in and support its decommissioning activities.
4. PGE must report within 30 days any settlement or award related to decommissioning costs for the Trojan plant.
5. PGE must provide satisfactory evidence with regard to any other matter the Commission deems pertinent to a decision in a rate proceeding.

Disposition of the DR 10 Conditions. We conclude that PGE has met the DR 10 conditions. The first condition, proof of the six assumed facts, was discussed above, in the section titled "The DR 10 Requirements," p. 27. We found that PGE has shown all but one of the six facts. We have discretion to allow recovery of decommissioning costs, however, in view of PGE's substantial compliance with the requirement that it prove the assumed facts.

As to the second condition, based on current information, PGE's chosen plan is the least-cost option. Third, PGE has made good faith efforts to involve other entities [*133] in its decommissioning efforts; we note its efforts to contact

the NRC, EPRI, the USDOE, and other utilities. The fourth condition, report of any settlement or award related to decommissioning costs, is not yet ripe. We continue to impose this requirement on PGE. We have not imposed the fifth condition.

We approve PGE's decommissioning plan and funding plan for inclusion in rate base on the effective date of the tariffs adopted in this order.

S-49: Steam Generator Plugging, Sleeving, and Analysis and Spare Nuclear Reactor Coolant Pump Motor

Steam Generator Issues:

The steam generators figure in the analysis of Trojan-related costs in two ways. First, the cost of *replacing* the degraded steam generators was imputed in PGE's 1992 Least-Cost Plan and 1993 Update. Second, PGE incurred capital expenses relating to *repairing* the steam generators in the time between its last general rate case, UE 79, and this rate case. TBA's evaluation of the steam generator issue addresses both of these costs.

Replacing the generators: In its least-cost planning process, PGE considered replacing the steam generators. PGE included the cost of replacement in its least-cost analysis [*134] of closing Trojan. The expected cost of replacing the generators in 1996 is \$ 183.1 million. Staff recommends removing from the net benefits analysis all costs associated with replacing the steam generators. If the cost of replacing the steam generators were included in the net benefits analysis, the cost of continued operation would be higher and the net benefit of closure would therefore be greater. Staff's proposal imputes to PGE the cost of replacing the steam generators, for purposes of the net benefits analysis.

Repairing the generators: After January 1, 1992, PGE incurred capital costs for plugging and sleeving the generators and analyzing the problem. Post-1991 Trojan-related capital expenditures have never been in PGE's rate base. PGE proposed to have them become rate base items for UE 88 recovery purposes. Staff recommends disallowance of the steam generator capital expenditures. The total amount of recommended disallowance is approximately \$ 14.9 million.

In considering how to treat the cost recovery associated with the steam generators, TBA reviewed Westinghouse engineering and design activities and PGE's purchase, operation, maintenance, and care of the Trojan [*135] steam generators. The review covers the period from 1968, when PGE purchased the generators from Westinghouse, through 1993, when PGE decided to close Trojan.

PGE noted significant degradation of the steam generators in 1989. By 1991, over 25 percent of the steam generator tubes were either plugged or sleeved. The generators had degraded to the point that PGE had planned to replace them in 1996. TBA concluded that Westinghouse design flaws were the root cause of the steam generator degradation. TBA found no imprudence on PGE's part with respect to its maintenance and operation of the generators.

Staff argues that we have the discretion to hold PGE responsible for the costs associated with the steam generator problems and recommends that we exercise our discretion in favor of the ratepayers. Staff's position derives from TBA's recommendation that PGE be held liable for steam generator costs even absent a finding of negligence on PGE's part.

Staff notes that the Commission has broad discretion when it comes to ratemaking. As the Oregon Supreme Court said, "The [Commission] appears, therefore, to have been granted the broadest authority--commensurate with that of the legislature [*136] itself--for the exercise of [its] regulatory function." *Pacific N.W. Bell v. Sabin*, 21 Or App 200, 214 (1975). Staff concludes that we have the discretion to disallow the costs associated with steam generators and to remove the cost of replacing them from the net benefits analysis.

Staff supports its conclusion by referring to *Pennsylvania Public Utility Commission v. Philadelphia Electric Company*, 561 A2d 1224 (1989). In that case, the Pennsylvania Supreme Court dealt with an order of the Pennsylvania Public Utility Commission in which that commission disallowed replacement power costs stemming from two shutdowns of a nuclear power plant. The second shutdown occurred because of a manufacturing defect, which the court said could not be attributed to the utility. The court nevertheless held that the commission was correct in assigning replacement power costs to the utility rather than to ratepayers. The court reasoned:

By disallowing the replacement costs, the Commission held that the utility and not the ratepayers were in a far superior position to seek redress for the defects and negotiate contractual protections [*137] to minimize any future problems. We believe a utility company is in a better position to prevent an occurrence or provide for protection against any such occurrence. After all, it was the utility which chose the contractor, negotiated the contract, and is in a position to seek damages for any losses sustained under the contract. While the utility may have to bear the initial losses incurred as the result of its contractor's negligence, it is in a far better position to aggressively pursue the tort-feasor for reimbursement. If we were to hold otherwise, the utility would have no incentive to pursue the tort-feasor, having already received full compensation for its losses. 561 A2d at 1228.

Staff also supports its position with reference to product liability law, which illustrates that the law can impose a burden on a party not judged to be at fault. If a customer is injured by a product through no fault of her own, for instance, product liability law imposes liability on the merchant, even if faultless, because the merchant is better situated than the customer to pursue remedies against the manufacturer. Restatement (Second) of Torts, Section 402A [*138] .

PGE argues that there is no legal precedent for holding it strictly liable for the defective steam generators; that TBA took a contrary position in another case; that staff's various legal analogies (see below) are inapposite because this is not a tort case but a ratemaking proceeding; and that to hold it strictly liable would be to set a dangerous new precedent. PGE also makes the policy argument that if we impose steam generator costs on PGE without a showing of imprudence, it will eliminate a protection now available to utilities when they seek cost recovery for expenditures.

Disposition:

We are persuaded by staff's arguments. Even if PGE is faultless, PGE is better situated to pursue remedies against Westinghouse than its ratepayers are. PGE is correct when it argues that this is a rate case, not a tort case, and that the legal precedent staff cites can be distinguished factually from the present case. However, someone must bear the costs relating to the steam generator defects. As between PGE and the ratepayers, we find it fairer to assign the costs to PGE, based on the reasoning in *Pennsylvania Public Utility Commission v. Philadelphia Electric Company*. That case [*139] is different on its facts because the vendor and the utility were in an ongoing contractual relationship, but the principle enunciated applies to the present case, as does the principle of product liability law stated above.

The fact that TBA took a contrary position in another case does not decide the issue now before us.

Finally, PGE argues that imposing steam generator costs on it in the absence of imprudence means that utilities lose the protection of prudence as the basis for cost recovery when they purchase goods or services from another. The Commission decides cost recovery issues on a case by case basis. No future outcome is determined by the decision to impute the cost of steam generator replacement to PGE by removing their cost from the net benefits analysis and disallowing the post-1991 plugging, sleeving, and analysis costs.

Spare Reactor Coolant Pump Motor:

This is another post-1991 Trojan-related expense that staff recommends should be disallowed. Trojan had four coolant pump motors that circulated water to cool the reactor. These pumps were required for the safe operation of Trojan, and if one motor had failed, Trojan would have had to be taken off line. [*140] It could have taken up to nine months to repair or replace a motor.

In 1986, PGE assessed the need for a spare motor. PGE inspected the existing motors, which had operated since 1976, and found them to be in excellent condition. PGE decided against purchasing a spare motor. In 1988 and 1989, PGE again studied the issue of purchasing a spare motor and explored several options, none of which involved PGE's sole purchase of a spare motor. PGE explored sharing a spare motor with another plant, for instance, and purchasing a motor stator (a motor component subject to the highest proportion of motor problems). PGE again decided against purchase. In Spring of 1991, it decided to purchase a spare motor from Westinghouse for \$ 2.2 million. When PGE decided to close

the plant in 1993, the motor had not yet been delivered. PGE decided not to accept delivery, because to do so would significantly reduce the motor's salvage value.

PGE argues that its decision to purchase the motor was prudent, pointing out that between 1984 and 1988, 19 reactor coolant pump motors failed in the industry. Moreover, PGE is aware of at least 20 other nuclear power plants that purchased or had access to a spare [*141] reactor coolant pump motor. PGE argues that the costs of the motor should therefore be included in rates.

Staff opposes including the cost of the spare reactor coolant pump motor in rates. Staff argues that the 1991 decision to purchase the motor is not supported by an adequate analysis. Although PGE assessed its need for a spare motor in 1986 and 1988, it did not do a new assessment in 1991. There is therefore no record to show why PGE decided to purchase the spare motor by itself, or why it purchased an entire motor rather than a stator. Staff maintains that PGE's general discussion of the impact of an outage and its relatively old data on motor failures do not support such a large capital investment.

Disposition:

We conclude that the \$ 2.2 million investment in the spare reactor coolant pump motor was not prudent and that the investment will not be allowed in rates. The 1988 studies explored options that are different from the one PGE chose in 1991, so PGE cannot use those studies to support its 1991 decision. The data from 1986 are too remote to rely on. Here, as with all issues in a rate case, PGE has the burden of proof, and has not carried it.

S-51: Remove Trojan [*142] Power Cost Deferral

S-52: Trojan Plant Income Tax Write-off Revision

PGE's initial filing included an estimate of the accumulated deferred income taxes associated with Trojan, including the write-off for tax purposes of the portion of Trojan that PGE considered to be no longer in service. Accumulated deferred taxes reduce rate base and give customers the time value of the income tax reductions. Total Trojan accumulated deferred income tax includes amounts related to several timing differences other than the Trojan write-off, including depreciation, decommissioning, retention plan, and other costs.

Staff originally accepted the amounts that PGE included in its filing for deferred taxes and write-off. In its rebuttal testimony, however, PGE revised the amount of accumulated deferred taxes for two reasons: to remove deferred taxes associated with Trojan excess power cost deferrals (Issue S-51) and to reflect a substantially reduced actual Trojan income tax write-off (Issue S-52).

On Issue S-51, PGE proposes to remove from rate base included in PGE's November 1993 filing the accumulated deferred income taxes for Trojan excess replacement power costs. The November filing [*143] incorrectly included \$ 24.4 million of deferred taxes related to PGE's UE 85 and UM 594 power cost deferrals in the 1995 and 1996 rate bases. We will address those deferrals in separate dockets. That removal increases revenue requirement by \$ 3,305,000 in 1995 and \$ 3,337,000 in 1996. Staff agrees with PGE that these excess accumulated deferred taxes should be removed from rate base, and agrees as to the amount of taxes to be removed. We conclude that the Trojan excess power cost deferrals should be removed from rate base.

Issue S-52 deals with PGE's November 1993 filing, which forecast a Trojan tax write-off of \$ 120.5 million. The actual write-off was only \$ 66.6 million, which, PGE argues, increases the 1995 and 1996 rate base by \$ 21.4 million and \$ 22.3 million, respectively. According to PGE's revised calculation, the January 1, 1995, rate base reduction for accumulated tax deferrals related to a write-off would be \$ 26.2 million, a \$ 21.0 million change from the \$ 47.2 million in PGE's initial filing.

Staff agrees that write-off tax deferrals should be revised, but differs with PGE on the proper amount. Staff challenges two elements of PGE's revisions. First, PGE's figures [*144] do not incorporate the effects of a tax write-off associated with the property it continues to classify as utility plant in service. In the discussion of Issue S-46 (Trojan Plant Classification) above, we concluded that Trojan assets are no longer used and useful for providing service, and are thus no

longer to be classified as plant in service. According to staff, PGE's recommended rate base increases should be reduced by an initial amount of about \$ 13 million, with appropriate changes for each of the test years.

Second, staff argues that we should use a different reserve for salvage than PGE does when it calculates the effects of a full tax write-off. PGE uses \$ 19.3 million, or 20 percent of original cost, to lower the estimated total write-off. In its investment projections, PGE estimated salvage sales at \$ 3.9 million. We have determined that the value of salvage sales should be set at \$ 12.7 million (see discussion of Trojan salvage sales, Issue S-47 above). Staff proposes to use the same figure, \$ 12.7 million, for both the reserve for salvage and the value of salvage sales. Staff's proposed figure is lower than PGE's, produces a higher initial deferred tax reserve, and [*145] lowers rate base by \$ 2.6 million.

To summarize the effects of these two proposed changes, PGE supports a beginning amount of write-off of accumulated deferred taxes of \$ 26.2 million. Staff proposes a beginning write-off of \$ 41.7 million. \$ 13 million of the difference derives from whether a full write-off is taken and \$ 2.6 million is associated with the amount of salvage reserve to be included in estimates.

We previously found that Trojan should no longer be considered plant in service (Issue S-46). Accordingly, we adopt staff's position that the revision should incorporate the effects of a full write-off. We also determined that \$ 12.7 million is the appropriate figure to use for Trojan salvage sales (Issue S-47). Therefore, we also adopt staff's position that \$ 12.7 million is appropriate to use for salvage reserve. These adjustments increase revenue requirement by \$ 871,000 for 1995 and \$ 1,119,000 for 1996.

S-53: Trojan Intangible Asset Reclassification

PGE's November 1993 filing included Trojan Intangible Assets in total rate base but did not specifically identify them as Trojan rate base and did not include them in the "Trojan Only" analysis. Reclassifying them [*146] now will make them part of any Trojan Only analysis and result in a proper matching of Trojan rate base to the Trojan intangible depreciation expense. This adjustment increases 1995 and 1996 Trojan revenue requirement by \$ 303,000 and \$ 156,000, but is offset by a matching reduction to non-Trojan revenue requirement. Staff supports this reclassification. We find that Trojan intangible assets should be reclassified as PGE proposes.

Trojan Balancing Account

In the February 27, 1995, stipulation, PGE and staff agree that it is appropriate to vary the amortization of the Trojan investment to take into account the actual revenue collected from customers as a result of our decision in this case. Rather than creating a balancing account, the parties agree that incremental or decremental amortization expense amounts generated as a result of the stipulation will be accumulated in a Trojan Investment Recovery Account (TIRA). The TIRA is designed to provide a procedure to precisely accumulate actual revenue received by PGE as recovery of the Trojan investment based on amounts authorized in this order.

No party opposes the balancing account. We have reviewed this stipulation, attached [*147] as Appendix D, and find it reasonable. We adopt the stipulation in its entirety.

Other Adjustments

Staff and PGE agree on the following adjustments as well:

- (1) To correct the nuclear fuel construction work in progress;
- (2) To remove from all staff-proposed Trojan-specific revenue requirement recommendations and alternatives, all amortization expense, deferred income tax expense, and deferred investment related to the United States Department of Energy Decommissioning and Decontamination payment.
- (3) To incorporate in the calculation of Trojan deferred income taxes the proper Schedule M adjustments, including the Trojan materials inadvertently left out of staff's Phase II Trojan deferred investment.

After reviewing these matters, we find these adjustments reasonable and approve them.

Appendix F attached shows the stipulated and unstipulated adjustments to PGE's original filing, along with their revenue requirement effect for 1995 and 1996. Appendix G shows the rate consequences of our decision, broken down by rate class, without and with the BPA residential exchange credit. Appendix H, attached, shows the percent of marginal costs attributable to each customer [*148] class.

CONCLUSIONS

1. Portland General Electric Company is a public utility subject to the Commission's jurisdiction.
2. The Commission should adopt the stipulations attached as Appendices B, C, D, and E.
3. Based on the record in this case, Portland General Electric Company's rates that result from the stipulations and the Commission's conclusions in the body of the Order are just and reasonable.

ORDER

IT IS ORDERED that:

1. The stipulations attached as Appendices B, C, D, and E are adopted in their entirety.
2. The other adjustments the Commission has made in the body of this Order are adopted.
3. PGE may file revised tariffs consistent with the stipulations and the findings of fact and conclusions in this Order to be effective April 1, 1995. PGE shall file such tariffs by March 30, 1995, or as soon thereafter as possible.

Made, entered, and effective ____.

Ron Eachus, Commissioner

Roger Hamilton, Commissioner

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of this order. The request must comply with [*149] the requirements of OAR 860-14-095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-13-070(2)(a). A party may appeal this order to a court pursuant to ORS 756.580.

DISSENTBY: SMITH

Chairman Smith concurs in part and dissents on the following issue:

S-38: Decoupling

I dissent from the Commission's conclusions and direction to PGE to proceed with decoupling, for the same reasons I dissented in Order No. 92-1673 (UM 409).

Decoupling was designed to promote energy efficiency and demand-side management (DSM). It is meant to remove disincentives to a utility's acquisition of demand-side resources from the traditional rate of return regulation framework.

Order No. 92-1673 asserts that "no other change in the regulatory system can ensure that we will move toward the goals of [reducing energy consumption]."

That assertion is even less supportable today than it was at the conclusion of UM 409. The marketplace has changed and will continue to change dramatically, requiring traditional regulation to evolve toward a more market-based approach. In the face of competition in generation and the prospect of comparability in the transmission [*150] system, electric utilities are responding by looking for ways to be and become lowest-cost providers.

This need (or perceived need) to be competitive drives inefficiencies out of the utilities' systems and produces a new, lower set of price signals. By definition, neither the customer nor PGE is likely to make uneconomic energy decisions. In the short term, the effect on DSM programs will be more than "perverse"; it could be close to fatal. That is, regulators may not have the leverage to require energy efficiency or DSM programs, because it will be even more difficult for programs to meet cost-effectiveness standards while remaining price competitive.

Not only will market prices be the controlling factor in customer response choices, but the inherent inability of traditional regulation to promote DSM will surface as well. Managing the proposed decoupling mechanism may well prove even more difficult, costly, and problematic than administering past and current DSM programs. For example, the administrative costs may be high, because the tariff will require "information on monthly revenues, incremental costs, and margin" as well as six-month reviews. I note that with regard to [*151] incentive mechanisms, the SAVE tariff (Schedule 101), which was considered a particularly effective DSM incentive mechanism, bogged down early in administrative burdens and disputes over measurements. Now the Commission has no way to require its continuation, and PGE has determined that its benefits do not outweigh its costs and rate impacts.

As this order issues, the legislature is considering alternatives to traditional rate-of-return regulation. States are studying how to restructure the electric industry. The FERC is aggressively promoting comparability in wholesale transmission access and wheeling. In the West, regions and subregions are forming transmission groups to manage cooperative arrangements for wheeling power across systems. The federal marketing agencies face the first real change in how they do business since their formation.

Decoupling is not consistent with these and other movements toward greater competition, because decoupling insulates a utility from lost margins that result from lost retail sales. For example, if PGE should lose a customer to self-generation, decoupling would restore those lost margins to PGE. I believe these business risks are more appropriately [*152] left with PGE than shifted to the ratepayers through decoupling. PGE is better situated to manage these risks and compete on price or service quality whenever necessary. As the market becomes more competitive and firms compete for their share of energy sales, it does not seem apposite to institute a policy that essentially guarantees the utility a fixed level of sales and resulting margins. The standard competitive framework does not guarantee each company a fixed sales level and resulting margins. Rather, the sales level and profitability of a company is directly related to how well and efficiently the company satisfies the needs of its customers.

The time for decoupling has passed. The changes in energy markets, the burdens and difficulty in administration, and PGE's reluctance all militate against use of this mechanism to meet the Commission's goals of promoting energy efficiency. Decoupling should not be implemented.

Nevertheless, the goal of using energy resources efficiently and wisely remains. The goal of diversifying the resource base remains. It is just that circumstances have loosened regulators' grip on traditional levers. We must find other ways of meeting the need [*153] and the challenge. Decoupling is not the solution. The doubts and questions voiced in my dissent in Order No. 92-1673 have not been answered. It is time to consider other forms of regulation more attuned to the evolving energy marketplace.

Joan H. Smith, Chairman

Legal Topics:

For related research and practice materials, see the following legal topics:

Energy & Utilities LawElectric Power IndustryRatesRetail RatesEnergy & Utilities LawUtility CompaniesBuying & Selling of PowerEnergy & Utilities LawUtility CompaniesRatesRatemaking FactorsGeneral Overview



15 of 99 DOCUMENTS

In the Matter of the Application of Golden State Water Company (U133W) for an order authorizing it to increase rates for water service by \$ 14,926,200 or 15.77% in 2007; by \$ 4,746,000 or 4.31% in 2008; and by \$ 6,909,300 in 2009 in its Region II Service Area

Decision 07-11-037; Application 06-02-023

California Public Utilities Commission

2007 Cal. PUC LEXIS 648

November 16, 2007, Dated; February 14, 2006, Filed

PANEL: [*1] MICHAEL R. PEEVEY, President; DIAN M. GRUENEICH; JOHN A. BOHN; RACHELLE B. CHONG; TIMOTHY ALAN SIMON, Commissioners

OPINION: (See Attachment D for List of Appearances)

OPINION GRANTING RATE INCREASES FOR THE REGION II SERVICE AREA AND GENERAL OFFICE OPERATIONS OF GOLDEN STATE WATER COMPANY

1. Introduction

In this decision we resolve two rate cases filed by Golden State Water Company (GSWC), which was formerly known as Southern California Water Company. The first case concerns GSWC's Region II, which serves a number of cities and unincorporated areas in Los Angeles County. n1 Virtually all of the issues concerning Region II rates were resolved in a stipulation that GSWC and the Commission's Division of Ratepayer Advocates (DRA) submitted on August 4, 2006. As part of this decision, we approve all but one of the terms of this stipulation.

n1 GSWC has divided Region II into four "customer service areas," or CSAs. About 50,000 customers in Carson, Lawndale, Gardena, Hawthorne, Inglewood, Torrance and portions of Compton are served by GSWC's Southwest CSA (which also serves unincorporated areas including Athens, El amino Village, Lennox and Liberty Acres). The entire community of Culver City is served by the Culver City CSA, where GSWC has about 9,300 connections.

About 19,600 customers in Artesia, Norwalk, Hawaiian Gardens, Downey and portions of Cerritos, South Gate and Lakewood receive service from GSWC's Central Basin East CSA. In addition, approximately 19,200 customers in Bell, Bell Gardens, Cudahay, Florence, Graham, Willowbrook and Hollydale are served by GSWC's Central Basin West CSA.

[*2]

The second rate case concerns GSWC's general office, which is located in San Dimas, California and provides support Services to all three of GSWC's California regions. Despite lengthy negotiations, GSWC and DRA were unable to resolve their differences over the amount of the rate increase appropriate for GSWC's general office. Two of the largest issues with respect to the general office rate case are (1) the percentage of general office costs that should be allocated to the three regions versus GSWC's unregulated affiliates, and (2) the number and types of new personnel po-

sitions that should be authorized for GSWC's general office. Eight days of hearings were held concerning the general office issues, and in this decision we resolve them.

As a result of our decision, GSWC will be authorized a rate increase for its Region II operations of \$ 6,370,300, or 6.74%, in 2007, \$ 4,456,300, or 4.40%, in 2008, and \$ 4,701,000, or 4.44% in 2009. In addition, we determine that general office costs that cannot be charged directly should be allocated as follows among GSWC and its affiliates not regulated by this Commission: GSWC 91.5%, Chaparral City Water Company (CCWC) 2.8%, American States Utility [*3] Services (ASUS) 5.6%.

2. Procedural Background

GSWC filed the instant application in mid-February 2006. Even before the protest period had run, a discovery dispute arose between GSWC and DRA, which caused the latter to file, on March 17, 2006, a motion to compel responses to some of DRA's data requests. DRA also filed a protest on March 30, 2006.

Because of the parties' scheduling constraints, a prehearing conference (PHC) could not be held until May 2, 2006. At the PHC, the parties proposed essentially equivalent schedules based on the Rate Case Plan adopted in Decision (D.) 04-06-018. After some discussion with the Administrative Law Judge (ALJ), the following schedule for testimony and hearings was agreed to:

Action	Date
DRA files responsive testimony	May 25, 2006
GSWC files rebuttal testimony	June 9, 2006
Hearings held	June 26-30, 2006

The parties submitted their testimony on the dates indicated. However, DRA expressed concern because of the very large volume of rebuttal testimony that GSWC served, and - as described below - DRA filed a motion to strike all of one witness's rebuttal testimony and portions of another witness's on June 28, 2006, during the first week [*4] of hearings.

Prior to commencement of the hearings, two public participation hearings (PPHs) were also held. The first was held on June 21, 2006, in Placentia, which is one of the communities GSWC serves in Orange County. The second PPH was held in the City of Gardena, which is located in Los Angeles County, on June 22, 2006. Both PPHs were well-attended, and many of the people attending them asked for and were granted an opportunity to speak.

On June 14, 2006, the City of Claremont, California (Claremont) filed a petition to intervene in the proceeding. Neither GSWC nor DRA opposed the petition, and the ALJ granted it on the first day of hearings. Claremont's attorney made clear, however, that his client's participation in the proceeding would be limited to the filing of briefs.

Although hearings began as scheduled on June 26, 2006, they were not concluded within the five days originally allotted for them, and additional hearings were held on July 6, 11 and 12, 2006. Pursuant to a schedule worked out on the last day of hearings (and subsequently extended at the requests of both DRA and GSWC), all parties filed opening briefs on August 10, 2006, and reply briefs on August 30, 2006. [*5]

A "true-up" hearing to answer any questions the ALJ might have about the August 4, 2006 stipulation between DRA and GSWC was scheduled for September 11-12, 2006, but was canceled due to a death in the ALJ's family.

Owing to the slower-than-expected pace of decision writing brought about by this family death and other matters, on December 14, 2006 we issued D.06-12-017, which granted interim rate relief to GSWC pursuant to the terms of Pub. Util. Code § 455.2. The interim rate relief for GSWC was made effective on January 1, 2007, and the decision provided that the interim increase would be subject to refund, and could be adjusted upward or downward back to January 1, 2007, consistently with the final rates adopted by the Commission.

3. The Provisions of the August 4, 2006 Settlement Stipulation Between DRA and GSWC are Reasonable and Should Be Accepted

Although GSWC and DRA strongly disagree on many issues relating to the company's general office operations, they did reach a settlement as to some, and they also agreed on a settlement of the large majority of issues between them relating to Region II. We have examined this stipulation [*6] in detail, and except for the allocation factor agreement in Paragraph 5.10, we accept the stipulation's provisions as a reasonable compromise of the parties' positions.

Pursuant to the schedule agreed upon at the last day of hearings, the parties' stipulation was served on all parties and the ALJ on August 4, 2006. The stipulation is appended to this decision as Attachment A. The actual stipulation itself comprises 26 pages and contains many subparagraphs, to which we will refer below.

Also attached to the stipulation are Appendices A, B and C. Appendix A is a so-called "reconciliation exhibit," summarizing the differences between GSWC's position and DRA's for the three years covered by this rate case. Appendix B sets forth the agreed-upon capital budgets for each CSA in GSWC's Region II for 2006, 2007 and 2008. Appendix C sets forth the capital budget items for these same years as to which the parties were able to agree for GSWC's general office. However, as the stipulation notes, many of the items in Appendix C are marked "TBD" (i.e., to be determined), because GSWC and DRA could not reach agreement and await our decision on the disputed items.

In the paragraphs below, we discuss [*7] some of the more significant provisions of the settlement stipulation.

Cost of Capital - On this important item, DRA favored a return on equity (ROE) of 9.68%, while GSWC argued for an ROE of 11.2%. In P 10.01, the parties agreed the ROE should be 10.1%. The parties agreed that the cost of debt should be 7.46%, and that GSWC's capital structure should consist of 49.2% debt and 50.8% equity. (PP 0.02 & 10.03.) Using all these figures, the parties agree that the return on ratebase will be 8.80%. (P 10.04.)

Overhead Rates - All of the stipulated capital budget items reflect the overhead rates that GSWC requested: 21.8% in 2006, 24.9% in 2007, and 22.1% in 2008. The parties agree that these rates will be recalculated depending on the Commission's ruling on disputed items, and this will be done consistent with the methodology used by GSWC's witness. (PP 2.01, 2.02, 2.15.) As noted in the Ordering Paragraphs, we conclude that when our rulings on the disputed items are taken into account, and using the methodology the parties have agreed to, the revised overhead rates for capital budget items are as follows: 24.73% in 2006, 26.12% in 2007, and 26.37% in 2008. n2

[*8] **Capital Additions Contingent on Approval of New General Office Positions and Retention of Certain Departments** - In PP 2.04-2.09, DRA and GSWC agree on the amount of certain capital additions that are contingent on how the Commission resolves certain general office issues, and whether it approves certain general office positions to which the capital additions relate. The issues are (1) whether a Capital Projects Department should be approved, and (2) whether the Employment Development University (EDU) and the Internal Audit Department should be retained in GSWC's general office. The positions at issue are (1) three new customer service specialists, (2) a Senior Human Resources Specialist, and (3) a Risk Manager. As indicated in our discussion of disputed general office positions, we are (1) approving all of the positions described in the preceding sentence, (2) ruling that the EDU and Internal Audit Department should be retained in GSWC's general office, and (3) approving the positions requested in connection with the Capital Projects Department.

Advice Letter Projects - In P 2.11, the parties agree that upon completion of two projects, GSWC may file advice letters [*9] seeking authorization to include these costs in rates, up to a capped amount in each case. The projects are Bissell Well No. 1 and the WB-01 Emergency Chlorination Station.

Construction Work in Progress (CWIP) for Region II and General Office - In P 2.12, GSWC and DRA agree on an overall amount of CWIP for Region II projects to be amortized from 2006-2008 pursuant to an agreed-upon schedule. In P 2.13, these parties agree that it is reasonable to include in rates \$ 900,000 for general office CWIP to be closed in 2006. With respect to the latter, GSWC agrees that in future rate cases, its CWIP requests will be supported by workpapers and testimony to facilitate DRA's review of the requests. This is one of at least two instances in the stipulation where GSWC acknowledges that its showing on certain issues was insufficient.

Income Taxes Associated with Gross-Up of Taxable Advances - This is another instance in which GSWC conceded that its direct showing was insufficient. After DRA recommended that the amounts requested by the company should be disallowed for lack of supporting calculations, GSWC furnished workpapers along with its rebuttal testimony. DRA agrees that [*10] the amounts shown in the rebuttal

testimony and workpapers are consistent with the governing authority, Method 5 in D.87-09-026, and the parties have agreed to substitute these amounts in place of the requests in GSWC's direct case, with no credits for Region II: \$ 3,550,646 in 2006; \$ 3,339,173 in 2007; and \$ 3,250,726 in 2008. The company also agrees that in future rate cases, it will "provide computational support and a narrative describing the application of Method 5 to GSWC's computational approach." (P 2.18.)

Depreciation Accrual Rates - Although they used the same methodology, DRA and GSWC disagreed upon the composite accrual rates. DRA recommended 2.67%, GSWC 3.08%, and the parties compromised on 2.89%. (P 2.19.)

Water Sales - Although the parties agreed on their forecasts of customer growth using the methodology prescribed in the Rate Case Plan, they have a significant disagreement in their usage forecasts for Region II commercial class customers. This disputed issue is resolved in Section 9.5 of this decision. (PP 3.01-3.02.)

Region II Labor - GSWC's labor forecast for Region II was based on its current organizational structure and actual salaries, [*11] to which was added allowances for inflation, merit increases, overtime, etc. DRA's labor recommendation was based on 2005 recorded labor expense inflated to 2007. After discussion, the parties agreed upon the 2007 labor expenses set forth in P 4.01.

General Office Labor - Although the parties used largely the same forecasting methodology, DRA contests the inclusion of 36.5 positions the company has requested for its general office. The disputes over these positions are discussed at length in this decision. On other issues, the parties have compromised their differences and agreed that an overtime rate of 1.185% is reasonable for the test year, that an adjustment of \$ 474,428 should be made for general office vacancies, and that a merit adjustment of 0.7% should be used to derive general office labor expense for the test year. (PP 4.03-4.08.)

Injury and Damage Insurance - The parties are sharply divided on the amount that should be allowed for general office injury and damages; DRA recommends a 12.52% reduction from the company's forecast for these insurance costs. This issue is discussed in Section 9.4 of this decision. The only items DRA and GSWC were able to [*12] agree on were the brokers' fee, the so-called "DM&A fee" n3 and the loss reserve for workers compensation, as to which GSWC is self-insured. (P 5.02.)

Property Insurance - Although the parties have agreed to capitalize 21% of the total cost of property insurance, while the remaining 79% will be expensed and booked into the General Office Summary of Earnings, they otherwise remain divided on this issue, with DRA taking the position there should be no allowance for excess property insurance. Property insurance issues are discussed in Section 9.4 of this decision. (P 5.03.)

Pensions and Benefits - The calculation of pensions is determined by Standard No. 87 of the Financial Accounting Standards Board, so the principal difference between the parties is over how many additional positions, if any, the Commission should authorize for the general office. The other contested issues are what amounts, if any, should be allowed for dividend equivalent rights and annual incentive bonuses, and how to handle a DRA computational error. These issues are discussed in Sections 9.6 to 9.8 of this decision. (P 5.04.)

Business Meals - Although the parties resolved their differences [*13] over how much should be allowed for business meals in Region II, they remain divided over how much should be allowed for the general office meals. We resolve this question in Section 9.3 of this decision. (P 5.05.)

Outside Services - Despite their sharp differences over the appropriate number of general office positions, DRA and GSWC were able to stipulate that \$ 5,698,000 should be allowed for general office outside Services for the test year. For the Central District Headquarters in Region II, they also agreed to continue using the memorandum account treatment approved in D.04-08-053 for legal costs necessary to

secure the amendment of court judgments that govern GSWC's water rights in the Central and West Basins. (P 5.07.)

Miscellaneous Expenses - The parties stipulated as to these amounts with respect to Region II, but remain about \$ 600,000 apart for miscellaneous general office expenses. Most of the difference is accounted for by dues to such organizations as the National Association of Water Companies (NAWC), the California Foundation on the Environment and Economy (CFEE), and the American Council on Education (ACE). We resolve this question in Section 9.1 [*14] of this decision. (P 5.08.)

Allocation of General Office Expenses and Common Customer Accounts - Both GSWC and DRA allocated these expenses to the Metropolitan CSA using their own respective allocation studies. (P 5.09.) As we discuss later in this decision, the Commission rejects both GSWC's and DRA's allocation studies and develops its own allocation factors. However, in P 5.10, in place of the results their own allocation studies would produce, the parties stipulated as to certain amounts for the Region II headquarters and the Central and Southwest District Offices to be allocated to the Metropolitan CSA for 2007. Because we consider the stipulated amounts in P 5.10 to be inconsistent with the allocation approach we are adopting in this decision, we reject these stipulated amounts.

Rent - The parties stipulated as to the proper amounts of office rent for Region II, but remain about \$ 225,000 apart over the proper amounts of rent for general office space. We resolve this question in Section 9.2 of this decision. (P 5.12.)

Water Supply and Cost - The parties agreed on methodology to determine the level of production from wells and purchased water, but, [*15] as noted above, differ in their usage estimates for commercial customers. The parties also agreed to use GSWC's methodology to determine purchased water, purchased power and pump tax costs, once the Commission rules on the usage issue for the commercial class. (PP 8.01-8.02.)

Inflation - The parties agree that the inflation factors set forth in the February 28, 2006 memo attached to Exhibit 22, DRA's Report on Region II Results of Operations, should be used, as should the "Established Factors" set forth in the decision adopting the Rate Case Plan, D.04-06-018. (PP 9.01-9.02.)

Low-Income Program - GSWC requested recovery of the accumulated balance of the cost of its low-income program for Region II through a rate surcharge. The parties agreed that when the balance reaches 2% of adopted Region II revenues, the company may file an advice letter providing for recovery of the balance through a rate surcharge. (P 11.01.)

n2 In its August 20, 2007 reply comments on the Proposed Decision, DRA objects to the inclusion in the Ordering Paragraphs of this decision, "the definition of zeroing out the balance in the Overhead Pool Account" described in paragraph 2.15 of the August 4, 2006 stipulation. DRA contends that to include such a requirement in the Ordering Paragraphs would be unfair, because "GSWC never discussed this idea with DRA in settlement negotiations," and because DRA would never have entered into the settlement if it had thought it would be bound by such a principle. (DRA Reply Comments, pp. 4-6.) We think that the while other provisions of the August 4 stipulation are clear, the language of paragraph 2.15 is vague. Accordingly, our solution to DRA's objection is to require GSWC to develop the zeroing-out methodology for the Overhead Pool Account in consultation with DRA. We have further ordered that the methodology may not be implemented unless and until DRA's approval of it has been obtained.

[*16]

n3 The DM&A fee is the fee paid to David Morse & Associates, a third-party administrator that provides Settlement Services to GSWC for all non-litigated claims. (Ex. 13, p. 46.)

4. The Cost Allocation Studies Submitted by Both GSWC and DRA Contain Significant Flaws, So a Study Developed by the Commission Will Have To Be Used

A major topic in GSWC's testimony on general office issues was GSWC's cost allocation study. Such a study is used to assign costs that cannot be directly assigned between the three Commission-regulated GSWC water districts, on the one hand, and the company's unregulated and out-of-state affiliates, on the other. In view of the very large revenue increase that GSWC is seeking here for its general office operations, the cost allocation study became a major issue in this proceeding.

4.1. Overview of GSWC's Position on Cost Allocation

In his testimony in support of the allocation study, GSWC vice president Keith Switzer begins by describing the cost allocation approach the company has used in the past, and then argues that a new approach should be used in this case: Previously, [*17] GSWC relied on the four factor methodology to allocate its general office costs. With that method, the general office costs were totaled and then the total amount was allocated based on a single set of [four] allocation factors. Those allocation factors were derived with the four factor methodology that the Commission has authorized for many years. n4

In contrast to previous GRC applications, GSWC is proposing in this application to develop, whenever possible, a cost determinant factor for certain functional activities within the general office and to use that factor as the basis for assigning costs associated with that functional activity rather than allocating the total general office costs with a single cost allocation factor. As explained below, GSWC is proposing four different allocation/assignment factors for the general office costs. These four allocation factors will be applied to different cost items within the general office. Once the individual cost items have been allocated with their specific allocation factor, then the allocated costs will be summed by entity to derive an allocation factor for GSWC's regulated operations, CCWC and. ASUS. (Ex. 6, Switzer Testimony, [*18] pp. 5-6.)

n4 As set forth in a 1956 memorandum introduced by GSWC, the four factors are (1) direct operating expenses (excluding uncollectibles, general expenses, depreciation and taxes), (2) gross plant, (3) number of employees (using direct operating payroll and excluding general office payroll), and (4) number of customers. (Ex. 41.)

GSWC emphasizes that it is not proposing to abandon the four-factor approach entirely. On the contrary, Switzer states, the company intends to use the four-factor approach "for these broad-based functional activities where there is not a natural single cost determinate." (*Id.* at 6.) He continues, however, that many of the types of costs that are incurred in general office operations - costs that GSWC has grouped into 42 "cost centers" - lend themselves to a single natural cost determinant.

GSWC's opening brief gives the following summary of how the approach described above was used in the GSWC cost allocation study sponsored by Switzer in his testimony:

In its study, GSWC identified [*19] three ways to attribute cost-causation directly per the Commission's directive. First, for the Customer Service Center, GSWC's call center, GSWC allocated costs based on the number of phone calls received. GSWC Switzer, Ex. 6 at p. 10. Similarly, GSWC allocated costs for billing and cash processing based on the number of bills generated. *Id.* at p. 11. Finally, GSWC allocated Human Resources costs based on the number of employees. *Id.* at p. 12. These three cost allocation factors are based on cost causation for each cost center to which they are applied. The resources of the call center are spent in direct proportion to the calls received; the resources of billing and cash processing are spent in direct proportion to the bills generated; and, the resources of human resources are spent in direct proportion to the number of employees served. (*Id.* at p. 9-12.)

Where such natural determinants are not available, GSWC used the four factor allocation method. The costs to be allocated using the four factor include, but are not limited to, the costs for corporate executives, regulatory affairs, accounting and finance function, risk management, water quality, environmental, legal [*20] affairs, and corporate communications. These functions are very broad based in scope and are therefore appropriately assigned using the four factor methodology. (GSWC Opening Brief, pp. 12-13.)

Using the approach advocated by Switzer, GSWC concludes that 95.45% of its general office costs should be allocated to the three GSWC water districts regulated by this Commission, 2.34 % to its unregulated affiliate, ASUS, and 3.21% to 54% (CCWC), a water company in Arizona that is regulated by the Arizona Corporation Commission. Under GSWC's allocation proposal, customers in GSWC's Region II would bear 34.67% of overall general office costs while customers in Region III would bear 33.46% of these costs. (Exhibit 6, Switzer Schedule D.) n5

n5 As noted in the application, Region II is made up of the Central Basin West, Central Basin East, Culver City and Southwest CSAs mentioned on Schedule D to Switzer's testimony.

4.2. Overview of DRA's Position on Cost Allocation Issues

In its testimony and briefs, DRA has severely [*21] criticized GSWC's cost allocation study. DRA's opening brief sums up DRA's criticisms as follows:

GSWC's cost allocations basically involve determining [] two components: the allocation base and the allocation factors to apply to bases. According to GSWC, GSWC assigned the total actual [general office, or GO] costs to 42 cost centers; aggregated these individual cost centers to form various combinations of allocation bases; and applied a single allocation factor to many of these bases. GSWC claims that it applied the 'traditional four-factor' to the bulk of the GO costs.

DRA finds that the allocation bases formed by GSWC are unreasonably [] limited and disregard [] including other related cost centers. As for the allocation factors, DRA recommends rejecting both GSWC's single factors and its purported 'traditional four- factor,' which actually [are] not the four factors GSWC utilized in past GRCs and which [were] found acceptable.

For example, when allocating the costs associated with Customer Service Center (CSC), GSWC chose to combine only 4 out of the 42 Cost Centers . . . However, GSWC fails to justify restricting the CSC allocation base to only these 4 Cost Centers. (DRA [*22] Opening Brief, pp. 10-11; footnotes omitted.)

DRA is particularly critical of GSWC's decision to use the number of calls, number of bills generated and number of employees to allocate some, but not all, general office costs. On this issue, DRA states:

The Commission should reject GSWC's use of single cost allocation factor[s]. GSWC has failed to justify that any of its proposed single factors - number of phone calls, number of bills generated, and number of employees - is more reasonable to use than the four-factor cost allocation methodology. The Commission should adopt DRA's cost allocations . . . which are based on the four-factor methodology. (*Id.* at 13.)

Based on its own analysis, DRA recommends that 18.21% of the GSWC's general office expenses should be allocated to ASUS, 3.21% to CCWC, and 9.70% to Bear Valley Electric Company (BVEC). (DRA Opening Brief, p. 9.)

In addition to advocating that substantially more of GSWC's general office expenses should be allocated to GSWC's affiliates than does the company, DRA argues that GSWC's general office revenue requirement should be reduced by \$ 2.96 million for each of the three years covered by this GRC (2007-2009). According [*23] to DRA, such a reduction is appropriate because "this is the amount of indirect costs that should have been but were not assigned to ASUS for the nonregulated contracts in effect from 1999-2003, because no cost allocation had occurred during those periods or subsequently." (DRA Reply Brief, p. 14.) Although only adverted to in DRA's testimony (Ex. 23, pp. 4-13

and 4-15), the development of this calculation is set forth in a DRA workpaper that was the subject of extensive cross-examination. (Ex. 45, p. 7; Tr. pp. 780-787.) DRA takes the position that GSWC's general office revenues should be reduced by \$ 2.96 million for each of the years involved in this rate case (for a total of \$ 8,872,314) because, in DRA's view, GSWC has failed to comply with D.98-06-068, the Commission decision that authorized GSWC's predecessor, Southern California Water Company (SCWC), to establish a holding company.

4.3. Discussion

For the reasons set forth below, we conclude that neither the cost allocation approach advocated by GSWC nor that advocated by DRA is satisfactory. However, based on the testimony of GSWC witness Switzer and the schedules attached to this testimony, we believe that the data in [*24] GSWC's study (along with approximations from other recent GSWC cases) can be used to produce a cost allocation approach that is acceptable for this general rate case. We do not believe the approach advocated by DRA is susceptible to such repairs.

4.3.1. DRA's Proposed Reduction of the General Office Revenue Requirement by \$ 2.96 Million Annually to Account for "Missed Allocations" is Unjustified

We begin our discussion by observing that there is no merit in DRA's contention that GSWC's general office revenue requirement should be reduced by \$ 2,957,438 m each of the three years covered by this GRC. As noted above, DRA seeks this reduction to make up for indirect costs that, in DRA's view, should have been but were not charged to GSWC's non-regulated affiliates during the years prior to 2003. We reject DRA's position because we think it is clear from D.04-03-039 that the Commission has already made a revenue adjustment to account for the incorrect implementation of D.98-06-068, the decision that authorized GSWC's predecessor to form a holding company.

In D.04-03-039, the Office of Ratepayer Advocates (ORA) - the predecessor of DRA - challenged SCWC's proposal to account for the [*25] costs of transactions with its affiliate, ASUS, through the Other Operating Revenue (OOR) sharing mechanism established by D.00-07-018. ORA contended that such sharing was inappropriate because the OOR was not intended to apply to a water utility's transactions with affiliates, and that the proper guidance on affiliate transactions was to be found in D.98-06-068.

The Commission agreed with ORA that the requirements of D.98-06-068 governed, and that the OOR mechanism was not intended to apply to affiliate transactions:

[D.98-06-068] adopted specific guidelines for the various transactions conducted between SCWC, the holding company and affiliates. The overriding theme is that ratepayers should not subsidize affiliate operations. *The justification for allowing SCWC to establish the holding company structure and the implementation principles are directly applicable to the issue of allocating costs to unregulated operations in this GRC.* SCWC should follow the policies and guidelines adopted in D.98-06-068.

Rather than following the principles and guidelines of the holding company settlement, SCWC has instead used the principles established in D.00-07-018, which established [the [*26] OOR] mechanism applicable to water utilities that intend to offer non-tariffed Services. *SCWC has misinterpreted the intent of that decision.* The revenue sharing mechanism is intended to apply to a water utility (1) providing non-tariffed Services, (2) sharing the gross revenues with ratepayers, and (3) absorbing all incremental costs. *It does not apply to non-regulated affiliates of the water utility.* While we regulate water utilities, we have no direct authority over non-regulated affiliates. Rather than imposing a sharing mechanism on the revenues of non-regulated affiliates, we instead attempt to ensure that utility and affiliate costs are properly separated and common costs are fairly allocated. In that way, sharing of non-regulated revenues with ratepayers is unnecessary. (D.04-03-039, *mimeo.* at 28-29; emphasis supplied.)

To carry out its determinations, D.04-03-039 ordered SCWC to conduct a cost allocation study "to be included in [SCWC's] next Region III GRC." (*Id.* at 29.) However, the Commission declined to "suspend" the affiliate revenue sharing procedure advocated by SCWC until the required cost study was completed. Instead, the Commission adopted ORA's [*27] suggestion to increase the company's general office revenues by \$ 101,300, an adjustment that D.04-03-039 described as "a proxy for potential adjustments that might result from a cost study." (*Id.*) In other words, pending SCWC's completion of the cost study, the Commission decided to accept the \$ 101,300 adjustment in lieu of the full range of adjustments that an immediate cost study might have required.

In view of this discussion of the general office revenue adjustment in D.04-03-039, there is no basis for the \$ 2.96 million annual reduction to general office revenues that DRA proposes to make here. Although D.04-03-039 chided SCWC, GSWC's predecessor, for its failure to adhere to the requirements of D.98-06-068 in accounting for affiliate transactions, it is clear that the Commission chose to deal with the problem prospectively by (1) increasing the amount of OOR revenue sharing that SCWC had proposed, and (2) awaiting a proper cost study in the company's next GRC. Nothing in D.04-03-039 suggests that the Commission would be inclined to deal with improper cost allocations in the past by making retroactive adjustments to the company's general office revenue requirement.

In its [*28] opening comments, DRA argues that the proposed decision (PD) errs in rejecting DRA's claim that \$ 2,957,438 should be deducted from GSWC's general office revenue requirement for each of the three years covered by this rate cycle to make up for "missed allocations" of general office expenses that were not made to ASUS for the years 2000-2003. DRA argues that the PD misreads D.04-03-039 in concluding that the Commission dealt with this issue by (1) increasing the amount of OOR revenue sharing the company had proposed by \$ 101,300, and (2) awaiting a proper cost allocation study to be submitted in this GRC. By reading D.04-03-039 in this way, DRA argues, the PD ignores Conclusion of Law (COL) 14 in D.04-03-039, which in DRA's view makes it clear that "the Commission could not have intended to remediate ratepayers with the proxy amount of \$ 101,300," because that amount applied only "prospectively after 2003 to the rate cycle years addressed in D.04-03-039 . . ." (DRA Opening Comments, p. 9.)

DRA's argument is unpersuasive for two reasons. First, the discussion of the \$ 101,300 adjustment in D.04-03-039 leaves no doubt that it was intended to be a substitute for whatever adjustments might [*29] be required as a result of the cost allocation study mandated by the decision. On this issue, the Commission said:

ORA requests that the Commission suspend the affiliate revenue sharing procedure proposed by SCWC, until the cost study is implemented. ORA's adjustment amounts to an increase of \$ 101,300 in GO revenues. *We adopt ORA's adjustment but characterize it as a proxy for potential adjustments that might result from the cost study.* Under the circumstances here, where the utility has apparently not been following procedures adopted in its holding company decision, the adjustment is reasonable. (*Mimeo.* at 30; emphasis supplied.)

The second reason DRA's argument is unpersuasive is that COL 14 in D.04-03-039 dealt with an issue entirely separate from the question of how much general office expense should be allocated to GSWC's unregulated subsidiaries. COL 14 states:

SCWC customers should be reimbursed, in some manner, for the cash that was diverted from the water operations, due to the CPP. To do otherwise would result in a windfall for shareholders.

The "CPP" referred to in COL 14 stands for "Cash Preservation Plan," a program the Commission discussed in a [*30] section of the decision that is separate from the discussion of whether the affiliate rules set forth in D.98-06-068 had been properly implemented. In its discussion of the CPP, the Commission noted that the program, which was first implemented in 2001, was designed to limit cash expenditures on capital projects and O&M for SCWC's electric and water operations during the California energy crisis, which had caused a deterioration in SCWC's cash flow due to the sharp increase in energy prices. Because of this increase, the rates collected from SCWC's Bear Valley customers were insufficient to cover the costs of providing these customers with electric service. The CPP "included measures such as a hiring freeze, reductions in operating expenses, and elimination or deferral of all capital projects except for those projects that were considered essential either to meet public safety and health requirements or to provide continued service." (D.04-03-039, *mimeo.* at 30-31.)

While ORA did not argue that the CPP was unreasonable in view of the energy crisis, it did urge a \$ 3.6 million reduction in SCWC's O&M revenue requirement, and a reduction of \$ 3.2 million for the carrying charges on [*31] capital projects that had been deferred during 2001 and 2002. ORA was concerned that as a result of the CPP, "ratepayers were denied the benefit of funds that the Commission approved for those purposes," and that ratepayers were being asked to "pay[] twice for the same O&M expenses and projects." (*Id.* at 30.)

In its discussion, D.04-03-039 noted that while SCWC had deferred a substantial amount of capital expenditures in 2001 and 2002, the recorded capital additions for those years were nonetheless somewhat higher than the amount autho-

rized in the company's previous GRC decision. Thus, it appeared that ratepayers were not being asked to pay for capital projects that had been deferred from the prior GRC. (*Id.* at 33.)

With respect to O&M expenses, however, the Commission agreed with ORA that a reduction was appropriate, because the proposed maintenance expense amounts included items deferred from previous years. (*Id.* at 34.) The Commission determined that in order to avoid a windfall to shareholders (who alone would benefit from the balancing account that had been set up to keep track of electric cost undercollections), water ratepayers should receive "the difference between [*32] what should have been spent for maintenance for 2001 and 2002 and what was actually recorded for those years." (*Id.*) After determining that this difference was \$ 1,056,600 for Region III of the company, the Commission ordered that this amount should be amortized over a three-year period "as a reduction to the [water] ratepayers' obligation to fund maintenance expenses." (*Id.* at 35.)

It is evident from this discussion that COL 14 in D.04-03-039 has nothing to do with the question of how much general office expense should be allocated to ASUS. Moreover, the "windfall" referred to in COL 14 was one that might have arisen from the special-purpose balancing account, an issue that is not present here. Accordingly, we conclude the PD's reading of D.04-03-039 is correct, and we endorse it.

4.3.2. DRA's Proposal to Allocate About 30% of GSWC's General Office Costs to the Company's Affiliates is Unreasonable

In addition to arguing that GSWC's general office revenues should be reduced by \$ 2.96 million annually to make up for "missed" allocations to ASUS in the past, DRA takes the position that a proper application of the four-factor methodology in this case should result in 18.21% [*33] of the GSWC's general office expenses being allocated to ASUS, with 3.21% allocated to CCWC.

GSWC has savagely attacked DRA's position in its briefs:

In contrast to GSWC's strict adherence to the Commission's guidelines, DRA ignored the Commission's instructions to allocate costs based on direct causation and randomly added or subtracted factors from the four-factor allocation methodology . . . This random methodology resulted in DRA's recommendation that 21.86% of the General Office expenses be allocated to GSWC's non-regulated affiliates. DRA's recommendation has no relationship to a reasonable estimate of the relative obligations or burdens imposed on GSWC's resources by ASUS. (GSWC Opening Brief, p. 13; emphasis in original.)

GSWC also argues that DRA's position defies economic logic when one compares GSWC and ASUS operations. On this issue, GSWC witness Switzer states in his rebuttal testimony:

The first indicator of the unreasonableness of DRA's proposal is simply to look at DRA's recommendation from an overall cost perspective by comparing the cost allocation to revenues generated by the Company. DRA recommends that nearly 20 percent of the general office costs [*34] be allocated to ASUS even though ASUS operations represent only about 1.5 percent of the Company's annual revenues (based on the latest recorded year).

In terms of dollars, DRA proposes allocating \$ 5.5 million to ASUS, whose total revenues (as reported in GSWC's latest annual report) are \$ 3.6 million. This \$ 5.5 million figure is based on DRA's recommended level of general office costs of \$ 27.8 million. GSWC, however, has requested general office expenses in Test Year 2007 of \$ 42.3 million. Based on the level of expenses requested by GSWC, DRA's proposed allocation factor of 18.21 (or corrected to 19.96) percent would allocate to ASUS between \$ 7.7 and \$ 8.4 million in general office costs, which is **more than double ASUS's annual revenues**. It defies logic to think that ASUS would continue to operate at such a loss.

The second indicator of the unreasonableness is to look at DRA's recommendation for ASUS compared to DRA's allocation to GSWC's PUC-regulated water operations. As noted previously, DRA recommends that 18.21 percent of the general office costs should be allocated to ASUS. By comparison, DRA's calculation, as shown in its workpapers, would allocate only 13.74 [*35] percent of the general office costs to GSWC's PUC-regulated operations in Region I. It is inconceivable that DRA would propose an

allocation to ASUS in excess of the allocation to one of GSWC's own operating regions. GSWC's Region I is a \$ 33 million operation that is fully supported by every department at the general office. By comparison, ASUS is a \$ 3.6 million operation that receives limited support from some, but not all, departments in the general office. (Ex. 13, pp. 5-6; footnote omitted.)

As explained below, we have concluded that DRA's proposed allocations of general office costs to ASUS cannot be accepted because of the inconsistent and unexplained way in which DRA has applied the traditional four-factor methodology. In addition to these deficiencies, we agree with Switzer that the anomalous results produced by DRA's approach raise serious doubts about its soundness. Even if one assumes that ASUS's new contracts will generate significantly more revenue in the future, the amounts of general office expense that DRA proposes to allocate to ASUS are so large that they would require special justification. DRA has not provided such a justification here.

4.3.3. DRA's Application [*36] of the Four-Factor Methodology is Too Quixotic and Unexplained to Justify Acceptance of its Cost Allocation Proposals

In addition to arguing that DRA's proposal would result in excessive cost allocations to GSWC's affiliates in view of the revenue these affiliates generate, GSWC also argues that DRA's proposal should be rejected because "DRA ignored the Commission's instructions to allocate costs based on direct causation and randomly added or subtracted factors from the four-factor allocation methodology." (GSWC Opening Brief, p. 13.) As indicated below, we conclude that this criticism has merit.

The four factors that have traditionally been used to allocate indirect costs not capable of direct assignment are set forth in the 1956 Commission memo that was admitted as Exhibit 41. As noted in the memo, the four factors to be used in allocating indirect costs are (1) direct operating expenses, (2) gross plant, (3) number of employees, and (4) number of customers. These factors have been used with a high degree of consistency over the years, and when the Commission has approved allocation formulas based on factors other than these four, it has clearly stated its reasons for doing so. [*37]

Although DRA claims that it followed the four-factor methodology in making recommendations about how much general office expense should be allocated to GSWC's affiliates, it is apparent from the record that this is not the case.

One of the key documents about allocation issues is Exhibit 45, a DRA workpaper that was introduced during the cross-examination of DRA's witness of general office issues, Mehboob Aslam. Exhibit 45 shows the allocation factors DRA applied to each of the 15 contracts held by ASUS. In most cases, three factors were applied, but the number of factors applied to a particular contract ranged from two to five. After a factor was applied to a particular contract and a percentage developed, the percentages for all the factors deemed relevant were then summed and divided by the number of factors used to yield the ultimate allocation percentage. n6 Exhibit 45 itself does not explain why some factors were applied to particular contracts and not others.

n6 For example, the factors used for the Fort Bliss, Texas contract were gross plant, expenses and the number of wells, which were assigned the following respective percentages when compared with these same factors for GSWC: 728%, 1.19% and 5.78%. These percentages were then summed ($7.28 + 1.19 + 5.78 = 14.25$) and divided by 3 to yield the overall percentage of 4.75%, which in turn was applied to that portion of the \$ 30,924,483 in GSWC general office expenses for the 12 months ending September 30, 2005 that Aslam considered relevant.

[*38]

During cross-examination, Aslam freely admitted that he added and subtracted factors for particular contracts, depending on his assessment of the factor's importance and on the quality of the available data:

Q. If we went all the way through your Exhibit 45 and we looked under each contract at the bold headings, we would see what factors you used as your methodology, right?

A. That is true, right.

Q. So sometimes there is three factors and sometimes there is five factors, right?

A. No. Five factors are only for two of the [ASUS] contracts. There are about 13 contracts listed here. So I would not adhere to [your] generalization.

* * *

Q. I'm directing your attention to Contract 12, Andrew[s] Air Force Base; Contract 13, Fort Monroe; Contract 14, Fort Lee . . . You used two factors in your allocation methodology for those specific contracts, right?

A. These are the two [factors] that were available, yes.

Q. You stated in your report that in thinking about applying the four-factor test you used your judgment and excluded one or more of the factors if such factor was likely to skew the costs. Do you recall that? GSWC counsel then refers Aslam to Ex. 23, p. 4-8, lines 6-7. [*39] n7

* * *

A. Yes. That is the general, premise [] which I have used, yes.

Q. And what did you mean by 'skew'?

A. 'Skew[,]' that is basically making [the] allocation lopsided. Going - allocating more toward one entity and kind of deliberately not allocating a fair share to the other entities. That is what I meant by 'skew.' (Transcript, pp. 799-801.)

n7 The DRA paragraph referred to by GSWC's counsel provides in full:

As far as the Allocation Factors are concerned, DRA tried to use the basic Four Factors Allocation Factors. However, if the use of any one of the four factors was likely to skew the costs to either the Regulated or the Non-regulated entity, it was simply excluded. (Ex. 23, p. 4-8, lines 5-8.)

Unfortunately, this colloquy is the clearest explanation that exists in the record for the approach Aslam used. At no point in its briefs or testimony did DRA present a clear explanation that would enable us to determine whether it is appropriate in a particular case to add to, or subtract from, the [*40] four factors traditionally used for cost allocation purposes. Without such a showing, we cannot accept DRA's recommendations. n8

n8 DRA's best attempt to outline its general approach appears in its August 13 opening comments, where it states that its approach takes into account the variation in Services that ASUS provides to its contracting parties "by assigning a specific 'cost allocation base' for each non-regulated contract. For example, . . . regarding the Rowland Water District contract, DRA reduced the cost allocation base for this contract from \$ 30,924,483 to \$ 21,287,614 by excluding costs such as 'Customer Service-Day shift, because the contract only requires 'after-hour' call center activities. This adjustment eliminates the need for [the] 'weighted' number of customers [provided for in the PD.]" (GSWC Opening Comments, pp. 5-6; footnote omitted.)

While an approach like this might be a reasonable alternative to the weighted-number-of-customers approach we are using in our interim cost allocation methodology, the central problem remains: DRA never provided a clear

explanation in its testimony or briefs of the "cost allocation base" concept, or of how DRA chose to apply it to each particular ASUS contract.

[*41]

4.3.4. GSWC Has Not Shown That the Use of Single Factors to Allocate Nearly Half of GSWC's General Office Revenue Requirement is Justified

Although GSWC is correct in asserting that (1) DRA's proposed \$ 2.96 million reduction in the annual general office revenue requirement is unjustified, and (2) DRA's application of the four-factor methodology cannot be accepted, this does not mean that the company is entitled to prevail on its contention that under D.03-09-021, it is reasonable to allocate nearly half of GSWC's general office costs on the basis of single allocation factors. As we shall see, although there have been some exceptions, the Commission has generally frowned on the use of single allocation factors, and there is good reason to reject them here.

GSWC's claim that it is appropriate to use single allocation factors rests upon a passage in D.03-09-021, which accepted a settlement negotiated in a general rate case involving California Water Service Company (CalWater or CWS). Although the Commission accepted the settlement, it criticized CalWater for failing to have in place a methodology for allocating indirect general office costs to affiliates, and it directed the company [*42] to develop such a methodology. In so ruling, the Commission made the following statement, on which GSWC relies:

In developing an allocation methodology, we direct Cal Water, where feasible, to rely on a cost-causation based factor to allocate common expenses, costs, or plant. *For example, for billing Services, it would be meaningful to allocate expenses by the number of bills sent out or by the hours the employees and equipment were used for regulated and non-regulated Services.*" (Mimeo. at 27-28; emphasis supplied.)

This statement - a dictum describing two approaches that seemed theoretically reasonable for allocating the costs of bill preparation - stops well short of being "an allocation methodology approved by the Commission," as GSWC's Switzer claims.

We acknowledge that in a handful of cases over the years, the Commission has suggested that the use of a single factor can be appropriate for allocating some kinds of indirect costs. For example, in D. 80207, 73 CPUC 597 (1972), the Commission agreed with the applicant that it was more reasonable to allocate the costs of maintaining customer accounts and preparing bills on the basis of the number [*43] of customers rather than on the traditional four-factor methodology. n9 However, no decision we are aware of suggests that it is appropriate to allocate nearly half of a company's indirect, general office costs on the basis of individual allocation factors, as GSWC is proposing to do here. n10

n9 In D.80207, the Commission said the following about the allocation of billing and record maintenance costs:

Staff Exhibit No. 19 states that the difference between applicant's original estimate and the staff's estimate of customer records and collection expense was predominantly due to differences in allocation percentages for payroll. The staff developed four-factor allocation percentages, whereas applicant's general manager testified that applicant spreads these expenses in proportion to the number of customers. For the rendering of bills and maintaining of customers' accounts there appears to be no justification for considering (1) direct operating expenses, (2) number of division employees and (3) division gross plant, the three additional factors used by staff. Applicant's allocation method more properly relates customer records and collection expense to the numbers of customer accounts and bills rendered. (73 CPUC at 603.)

In addition to D.80207, Exhibit 41 - the 1956 memo describing the four-factor methodology - notes that "indirect expenses which have a significant relationship to a particular factor, such as pension expense to payroll, should be segregated and prorated on the basis of an appropriate single factor.

[*44]

n10 In Switzer's direct testimony, he advocates that \$ 14.9 million of the \$ 30.9 million in general office costs that GSWC booked for the year ending September 30, 2005 should be allocated using individual allocation factors. Specifically, he advocates allocating \$ 2.1 million in customer service costs based on the number of calls, \$ 05 million in billing and cash processing costs based on the number of bills prepared, and \$ 12.3 million in human resources costs based on the number of employees. (Ex. 6, Switzer, pp. 11-13.)

Contrary to GSWC's position, Commission decisions in recent years have either approved the use of the traditional four-factor methodology, or the use of less than four factors if it can be demonstrated that one or more of the traditional factors are irrelevant or would skew the allocation study results in unreasonable ways.

In D.03-05-078, for example, one of the issues was how much of the expenses of the corporate parent of Suburban Water System (Suburban) should be allocated to Suburban. The company argued that the Commission should use the traditional four-factor analysis, [*45] whereas ORA argued that only three factors should be used. In accepting ORA's position, the Commission explained that using four factors in the manner advocated by Suburban would shift costs on to ratepayers:

In allocating parent company expenses to subsidiaries, the Commission generally follows a four-factor approach, measuring each subsidiary's (1) direct operating expenses, (2) end-of-year gross plant, (3) total customers, and (4) payroll. The results are applied to determine a subsidiary's share of its parent company expenses. Suburban applied these four factors to its allocation. ORA applied a three-factor test, eliminating 'customers' of each subsidiary because non-regulated subsidiaries like ECO reported that they had clients rather than customers. By entering '0' for ECO customers, ECO's share of parent company expenses was reduced, and Suburban's share was increased, despite ECO's annual revenue of \$ 62 million or more.

ORA notes that it has used two- or three-factor analyses for other Class A water companies where appropriate . . . ORA's analysis is persuasive, and we adopt the ORA [three-factor] allocation formula in this proceeding. Suburban thus is allocated 32.6% [*46] of the parent company costs, rather than the 45.2% recommended by Suburban. (D.03-05-078, *mimeo.* at 21-22.)

In this case particularly, the single factor that GSWC is proposing to use to allocate nearly 40% of its general office costs - an entity's number of employees - seems likely to result in a shift of costs away from GSWC's unregulated affiliates and toward its ratepayers.

The allocation study attached to Switzer's direct testimony indicates that as of September 30, 2005, GSWC and its affiliates had 505 employees, of whom only 14 were employed by ASUS. (Ex. 6, Switzer Schedule B, p. 2.) But it is obvious from the annual reports of GSWC's corporate parent, American States Water Company (ASWC), that ASWC hopes for and anticipates substantial growth in ASUS's operations over the next few years. The 2004 annual report states that ASUS had submitted bids to operate the water systems of over 20 military bases, while the 2005 annual report indicates that ASUS has won contracts through subsidiaries to operate the water and wastewater systems of Fort Bliss, Texas; Andrews Air Force Base, Maryland; and Fort Monroe, Fort Eustis and Fort Story in Virginia. (ASWC 2005 Annual Report, [*47] Letter to Shareholders of Lloyd Ross and Floyd Wicks.) n11

n11 In addition, the Ross-Weeks letter in the 2005 annual report indicates that ASUS has been awarded a contract to operate the wastewater system of Fort Lee, Virginia.

It is difficult to believe that over the next three years, the small number of personnel employed by ASUS at the end of 2005 could operate the water and wastewater systems of these military bases, some of which are quite large. Moreover, it seems likely that as ASUS (or its subsidiaries) add employees to handle the increased workload from the bases, the new employees will need significant assistance from more-experienced GSWC operating personnel. Thus, allocating

nearly 40% of GSWC's indirect costs on the basis of 2005 headcounts for GSWC and its affiliates - and just before an expected ASUS growth spurt - seems likely to produce results that do not fairly approximate the demands GSWC's unregulated affiliates place on its personnel. n12

n12 We recognize that ASWC's 2005 annual report states that ASUS has formed several subsidiaries to operate the water and wastewater systems at the military bases for which ASUS has won contracts. We also recognize that it is possible the growth in personnel needed to operate these systems at the bases will take place through hiring by the new subsidiaries, and that the new personnel hired may not need significant assistance from GSWC.

However, the record in this case does not indicate whether ASUS's increased personnel needs are being met through hiring by the new subsidiaries, or the amount of GSWC personnel expense that is being directly charged to ASUS and its subsidiaries. Indeed, for the years 2000-2003, the relevant excerpts of the annual reports concerning affiliate transactions that D.98-06-068 required SCWC, GSWC's predecessor, to file, state only that "shared employees charge their time on affiliate projects directly. Timesheets are prepared and the payroll expenses and associated labor burden expenses are charged to the various contracts." (Ex. 57, pp. 2, 5, 8, and 10.) The amounts of these charges, even in aggregate form, are not set forth in these reports.

As we recently said with respect to GSWC's predecessor, SCWC, "the burden rests heavily upon a utility to prove that it is entitled to rate relief and not upon the Commission, the Commission staff, or any interested party, or protestant to prove the contrary." (D.99-04-060, 86 CPUC2d 54, 62.) Here, the burden is on GSWC to show that it is, in fact, properly charging ASUS and GSWC's other non-regulated affiliates for employee time devoted to affiliate business. While the affiliate transaction reports for 2004 and later summarize the expenses charged directly to the affiliates, there is no way to tell for the prior years whether the company has satisfied its burden of properly charging expenses.

[*48]

In D.01-06-077, which was cited with approval in D.03-09-021, the Commission noted that using traditional cost allocation formulae when substantial growth is taking place at a utility's new, unregulated affiliates can produce unreasonable results. In D.01-06-077, one of the issues was whether the Commission should use a three-factor allocation formula advocated by Roseville Telephone Company (RTC), or a general allocator based on expenses that had been approved by the FCC and was favored by ORA. ORA opposed the three-factor formula favored by RTC on the ground, among others, that it placed undue emphasis on past asset accumulation, since RTC's new affiliates had not had time to accumulate significant assets. n13 The Commission agreed with ORA:

We are persuaded by ORA that RTC's three-factor formula does not reflect cost causation and instead over-allocates costs to RTC. ORA correctly points out that the three-factor formula over emphasizes asset accumulations, both through the gross plant factor and through depreciation expense reflected in the expense factor. As a mature company, RTC has accumulated considerable assets over a long period of time. In contrast, in a dynamic and [*49] fast changing period in the telecommunications industry, most of RTC's affiliates . . . were just coming into existence during the audit period. Even though these affiliates obviously required the expenditure of general and administrative costs, they have had little time to accumulate assets. Consequently, the use of accumulated assets as a significant factor in allocating common costs -- as reflected in the gross plant factor and the depreciation component of the expense factor -- does not provide a reasonable approximation of the extent to which affiliates caused common costs to be incurred. (D.01-06-077, *mimeo.* at 47.)

n13 Another ground for ORA's opposition was that RTC's formula automatically "classifies employees with administrative and general functions as RTC employees." (*Mimeo.* at 45.)

D.01-06-077 closed its discussion of the allocation issue by noting that a principal purpose of allocation rules is to "guard[] against cross-subsidy of nonregulated ventures by regulated Services." (*Id.* at 50, [*50] n. 5, quoting *In re Separation of Costs of Regulated Telephone Service from Costs of Nonregulated Activities*, FCC 86-564, 62 Rad. Reg. 2d (P&F) 163, pars. 33, 37.) In this case, in view of the growth in ASUS that can reasonably be expected in the near future, GSWC has not shown that the allocation method it favors would avoid subsidizing ASUS at the expense of GSWC's ratepayers. For that reason, we cannot accept GSWC's proposal, which would allocate nearly 40% of the company's general office costs on the basis of the number of employees.

An additional reason we are rejecting GSWC's proposed approach is that, like Suburban in D.03-05-078, GSWC has skewed the operation of the traditional four-factor methodology -- which it uses to allocate the remaining 60% of its general office costs -- by assuming that ASUS had only 11 customers, one for each of the contracts that ASUS held on September 30, 2005. (See Ex. 47, p. 1.)

This single assumption makes a significant difference in the outcome of the four-factor methodology. Even though -- according to Exhibit 46 -- 91,115 customers received service through the 11 entities with which ASUS held contracts at the [*51] end of 1995, the practical effect of assuming ASUS had only 11 customers is to assign one of the four traditional allocation factors -- the number of an entity's customers -- a value of zero. It is clear from the discussion in D.03-05-078 that we have disapproved of this practice because it results in a serious distortion of the four-factor methodology.

However, we also do not approve of the solution that DRA's witness Aslam used to "correct" this distortion; *viz.*, assuming that 74,270 customers served by the 11 entities with which ASUS had contracts should be considered the equivalent of full GSWC customers. We disapprove for two reasons. First, Aslam could not clearly explain how he arrived at the figure of 74,270. Second, as he was forced to concede during cross-examination, there is considerable variation in the nature of the Services that ASUS provides to its contracting parties, a situation that can make it inequitable to assume that each customer served by an entity with which ASUS has a contract is equivalent to a full GSWC customer.

n14

n14 For example, ASUS provides only after-hours call center service to the Rowland Water District. During cross-examination, Aslam acknowledged that Rowland's customers had placed only 1,800 after-hours calls during the entire 12-month period covered by the cost allocation study. Despite this limited number of calls for the single service ASUS provides, Aslam assumed a customer count of 15,000 for the Rowland Water District in his cost allocation computations. (Tr. 868-872.)

[*52]

In view of the variation in Services that ASUS provides to the entities with which it contracts, there is clearly a need to develop a methodology for determining a "weighted" number of customers for these entities that reasonably reflects the level of service ASUS actually provides. In the next section, we suggest one such method and then apply it to the data in the record.

4.3.5. As an Interim Expedient, GSWC Will Be Required to Use a Three-Factor Formula Based on Total Expenses, Total Labor and a Weighted Number of Customers

Although we are rejecting the allocation formulas proposed by both GSWC and DRA, we are well aware of the need to develop an allocation formula that is acceptable, at least for this general office rate case. Under the rate case plan adopted in D.04-06-018, GSWC was supposed to file a rate case for its general office operations in February 2005. The company did so, but as noted in D.06-01-025, the company and DRA filed a stipulation on August 3, 2005 in which they agreed to (1) defer a decision on the general office rate case for one year, and (2) in the interim, use certain percentages and amounts as the basis for calculating the share of general office [*53] expenses to be allocated to GSWC's Region III ratepayers. The Commission accepted this stipulation. (See, D.06-01-025, *mimeo.* at 66-69 and Appendix B.) In view of the fact that a decision on GSWC's general office expenses has already been deferred once and it will not be filing another general office GRC until July 1, 2008, we do not wish to defer a decision again.

However, the paucity of reasonable allocation proposals offered by the parties raises the issue of how an acceptable allocation formula can be devised for those general office expenses that cannot be directly assigned by GSWC. We have concluded that the most reasonable allocation formula, in view of the likely growth of ASUS's operations and the increased demand on GSWC's general office Services that can be expected as a result, is to use a variant of the three-factor allocation approach that the Commission has recently employed in GRC decisions such as D.03-05-078.

Under this approach, the three factors we will examine for GSWC and its affiliates are (1) total labor costs, (2) total expenses (including, in the case of affiliates, the affiliate's own Operations and Maintenance (O&M) costs as well as costs that are [*54] direct-billed by GSWC), and (3) a weighted average number of customers based upon (a) the number of ultimate customers, ratepayers or connections served by the entity with which the GSWC affiliate has a contract, and (b) the nature of the Services provided by the affiliate.

This approach, which can be implemented using the data in the record plus reasonable approximations based on past SCWC rate cases, will help to ensure that the general office costs allocated to GSWC affiliates -- especially ASUS -- fairly reflect the demands that the operations of these affiliates actually place on GSWC's resources. By examining total labor costs, for example, we are examining the nature and extent of the work actually performed for the entity under consideration. In the case of an affiliate such as ASUS, while the number of employees shown on a formal organization chart may not fairly reflect the full extent of the work performed by the affiliate, measuring total labor costs without regard to whose employee is performing the work should give a more accurate picture of the size of the enterprise. Likewise, measuring total expenses -- including those billed by GSWC -- should help to give a more [*55] accurate measure of the total work undertaken by the affiliate, more illuminating than the affiliate's total revenue or gross plant (which, as noted in D.01-06-077, may only recently have begun to grow.)

The most challenging of the three factors -- both conceptually and computationally -- is the weighted percentage of customers that should be attributed to the affiliate. In the case of CCWC, the computation is easy because it is a full-service utility, and 100% is appropriate. n15 In the case of ASUS, however, the computation is more difficult, because -- as noted above -- ASUS provides varying levels of service to those entities with which it now contracts.

n15 In CCWC's case, the affiliate is also subject to regulation by the Arizona Corporations Commission.

Among the ASUS contracts, the recent ones with military bases are relatively easy to evaluate in terms of the number of "customers", because all of these agreements -- which concern Fort Bliss, Texas; Fort Lee, Virginia; Andrews Air Force Base, Maryland; and [*56] Forts Eustis, Monroe and Story, all of which are also in Maryland -- essentially call for ASUS to provide full water and wastewater Services to these bases. It is therefore appropriate to use 100% of the connections at these bases to determine the appropriate weighted percentage customer count. n16 Based on the data set forth on page 2 of Exhibit 46 (which is GSWC's response to a DRA data request), the combined number of connections for all of these military contracts combined is 12,614. n17

n16 Using these military contracts also avoids the problems in determining the proper weighted number of customers for the ASUS's contracts with WellSpring International, Inc., the City of Chino Hills, and the Goleta water District, all of which expired on various dates in 2005. Rather than try to develop a weighted customer count for these contracts -- none of which will be in effect during the three-year period covered by this rate case -- it makes sense to use the military contracts, all of which were in effect in 2006 and are expected to be in effect for many more years. This is true even though the time period covered by GSWC's cost allocation study, which is the source of much of the data we use here, is the twelve-month period ending September 30, 2005.

[*57]

n17 At pages 4-7 of its August 13, 2007 opening comments, GSWC argues that the PD errs in its discussion of the interim cost allocation methodology insofar as it relates to the number of customers that should be imputed to the ASUS contracts with military bases. With respect to the contract with Fort Bliss, for example, GSWC argues that "the Services in the military base are provided by ASUS's own employees, not GSWC employees," and

that the Fort Bliss contract "does not require any meter reading or billing support, and does not use any GSWC employees to operate the water and wastewater systems." (GSWC Opening Comments, p. 6.) Based on these assertions, GSWC argues that the allocation factor for the contract "should be reduced from 100 percent to 17.9 percent," the percentage applied in the PD to A&G Services only. (*Id.*)

Although the record on this issue is thin, it does appear from GSWC's cost allocation study that at least some of the work at Fort Bliss is being performed by ASUS employees, because GSWC's cost allocation study (Ex. 6, Switzer Schedule B, p. 2) states that seven of ASUS's 14 employees "are under a separate benefit program of Ft. Bliss Water Company, a subsidiary of ASUS."

However, while the work performed by these employees may not consist of all the same Services that would be provided to retail water customers, the work is clearly very substantial, based on the contract that GSWC provided with its February 2006 General Office workpapers. That contract states that ASUS is acquiring the Fort Bliss water and wastewater systems pursuant to 10 U.S.C. § 2688, which empowers the Secretary of a military department to convey "a utility system, or part of a utility system" subject to the Secretary's jurisdiction, to a "municipal, private, regional, district or cooperative utility company or other entity." ASUS is acquiring the Fort Bliss water and wastewater systems over a 50-year period, and many pages of the contract are devoted to its obligations to undertake various kinds of capital improvements. The preamble to the Ft. Bliss contract (at page II) makes clear that ASUS's obligations under it are very broad:

ASUS shall assume ownership, operation and maintenance of the utility infrastructure water and wastewater distribution systems at Fort Bliss, Texas. ASUS shall furnish all necessary labor, management, supervision, permits, equipment, supplies, materials, transportation, and any other incidental Services for the complete ownership, operation, maintenance, repair, upgrades, and improvements to the utility system.

In view of the fact that ASUS is acquiring the water and wastewater systems of this very large military base and has the obligation to run them, it is not unreasonable to assume for purposes of the interim cost allocation methodology that the number of connections at Fort Bliss should be treated as equivalent to retail customers. The same is true for the other ASUS contracts with military bases, which Table 1 to GSWC's opening comments (which table was inadvertently omitted from the comments and belatedly served on August 16, 2007) also asserts should have a smaller number of retail customers attributed to them than the number of connections for these contracts.

[*58]

In cases where ASUS is providing less-than-full utility Services, determining the weighted number of customers is more complex, because the extent of the Services offered to the contracting parties -- most of which are medium- to small-sized municipal utilities -- varies from contract to contract. However, an appropriate discount factor can be developed using the ratios that O&M expenses minus supply costs, Administrative and General (A&G) expenses, amortization and depreciation, and taxes paid by GSWC bear to GSWC's net operating revenues (minus supply costs and cost of capital) in recent rate cases. n18

n18 The PD and alternate decisions that were issued on July 24, 2007 stated that the appropriate factors for comparison were total O&M expenses, total A&G expenses, and supply expenses. Even though neither GSWC nor DRA pointed it out in their comments, when we examined the figures in Table 3 of Attachment B again, it became apparent that supply expenses (which are comprised of purchased water, purchased power and pump taxes) had been counted twice, because they appeared in both the total O&M expense and the supply expense lines. Upon finding the double-counting error, we considered the best way to deal with it. Upon further reflection, we have concluded that it makes sense to eliminate supply costs entirely, because -- as noted in the text -- all of the entities with which ASUS has contracts are responsible for supplying their own water. For example,

paragraph C.3.5 of the ASUS contract concerning Fort Bliss makes it quite clear that the government will be supplying its own water:

Electric, natural gas, and water commodity supply is not included in this contract. The Government retains the right to procure or supply electricity, and/or natural gas, and/or water, that will be transported on the system(s) covered by this contract from any source.

[*59]

We have decided to examine these items because they assure a reasonable degree of comparability between GSWC and the entities with which ASUS contracts. It makes sense to exclude supply costs, for example, because all of the parties with which ASUS has contracts are responsible for supplying their own water. Similarly, even though military bases and municipal utilities may use different accounting terminology, all of them should be putting aside money to replace water-related assets as they wear out over time. Finally, even though municipal utilities and military bases do not pay taxes (or pay smaller amounts of tax than do private utilities such as GSWC), consideration of GSWC's tax burden is required to assure reasonable comparability between the proportion of its total A&G and O&M expenses (less supply costs) and those of the entity with which it is being compared.

Using this approach, if one examines Appendix D to D.06-01-025, which sets forth the summary of earnings for GSWC's Region III for 2006, net operating revenues minus supply expenses and cost of capital) equal \$ 43,666,600. This total is comprised of the following elements: (1) total O&M expenses less supply costs (\$ [*60] 11,383,800), (2) total A&G expenses (\$ 13,304,900), (3) depreciation and amortization (\$ 8,162,500), and (4) total taxes, including property, payroll and income taxes (\$ 10,815,300). Table 3 in Attachment B to this decision sets forth comparable data for Regions I and II of GSWC, and derives appropriate A&G, O&M, amortization/depreciation and tax percentages for the entire company.

The next task is to apply the company-wide A&G and O&M percentages thus derived to particular ASUS contracts. In the case of ASUS's contract with the City of Torrance, for example, ASUS has agreed to provide a full range of A&G support Services (including billing, cash processing and call handling), but it has not agreed to provide any other Services. Since A&G expenses comprise 30.1% of GSWC's net operating revenues less supply expenses and cost of capital for the company's three regions, it therefore makes sense to attribute 30.1% of the 34,000 customers shown for the City of Torrance on Exhibit 46 to the ASUS contract for purposes of the allocation formula we will be using. Using this approach, the appropriate weighted number of customers attributable to the ASUS-Torrance contract amounts to 10,234 ($30.1\% \text{ } [*61] \times 34,000 = 10,234$).

In the case of ASUS's contract with the City of Tustin, on the other hand, ASUS has agreed to provide meter reading, a labor-intensive O&M service, in addition to various A&G Services. In this case, we think it is appropriate to attribute one-third of the percentage that O&M expenses less supply costs comprise on GSWC's system, or 8.2% ($24.6\% / 3 = 8.2\%$), to this O&M service. When added to the 30.1% attributable to the A&G Services that ASUS provides to Tustin, this amounts to 38.3% ($30.1\% + 8.2\% = 38.3\%$). Since the total number of customers shown for the City of Tustin on Exhibit 46 is 15,000, the correct weighted number of customers to attribute to the ASUS-Tustin contract is 5,745 ($38.3\% \times 15,000 = 5,745$). n19 Table 2 in Attachment B to this decision shows the derivation of the weighted number of customers we are attributing to ASUS's contracts with other non-military customers.

n19 In its August 13, 2007 opening comments, GSWC argues that the PD errs in assuming that the ASUS contract with Tustin provides for some A&G Services, because "as shown on page 3 of GSWC [witness] Switzer's testimony, Exhibit 6, the contract . . . is for meter reading **only**." (GSWC Opening Comments, p. 5; emphasis in original.)

While Switzer's testimony does indeed make this assertion, it is contradicted by the terms of the contract itself, which GSWC submitted as part of the workpapers supporting its application. The contract with Tustin (which was apparently entered into by ASWC, GSWC's parent) is included in Volume 4 of the company's February 2006 General Office workpapers. While Paragraph 4.1 of the contract relates to meter reading Services, Para-

graph 4.2 sets forth other customer Services to be provided to the City of Tustin, including meter re-reads, turning meters on and off, hang door tags, shut-off of service to delinquent accounts, and "such other customer Services duties as may be reasonably requested by City." Thus, contrary to GSWC's assertion, the PD did not err in assuming that the Tustin contract provides for some A&G Services in addition to meter reading.

We also wish to point out that during the hearings in this case, the GSWC workpapers containing the ASUS contracts were not marked as exhibits. So that the record is complete concerning these contracts, we are hereby designating Volume 4 of GSWC's February 2006 General Office Workpapers as Exhibit 63 in this proceeding, and Volume 5 of the February 2006 General Office Workpapers as Exhibit 64.

Both of these volumes of workpapers were submitted under seal pursuant to General Order 66-B and Pub. Util. Code § 583. We have added an ordering a paragraph to this decision to grant GSWC's motion to place these workpapers under seal. In keeping with our usual practice, Exhibits 63 and 64 will remain under seal for a period of two years, at which time GSWC will be free to file a motion arguing that the two exhibits should continue to be kept under seal. Except where necessary, we have avoided discussing the most sensitive terms of these contracts (such as the price for Services) in the text.

[*62]

The final step in the process is to average the percentage allocations of customers attributable to GSWC and its affiliates, CCWC and ASUS, with the percentage allocations for the other two factors we are examining for these entities; *i.e.*, total labor costs and total expenses. The total labor costs and total expense figures we use are taken from Exhibit 47, the first page of which was taken from Switzer's own cost allocation study. The averaging process for the three factors, which yields the overall cost allocation factors, is shown on Table 1 of Attachment B. n20 These percentages are as follows:

ENTITY	ALLOCATION PERCENTAGE
Golden State Water Co.	91.5%
Chaparral City Water Co.	2.8%
American States Utility Services	5.6%

n20 In its August 13 opening comments, GSWC has also made other criticisms of the interim cost allocation methodology and urges us to make certain "corrections" that would bring the resulting allocation percentages closer to those advocated in GSWC's own study, which was sponsored by Mr. Switzer.

What GSWC's comments ignore is that the reason the PD found it necessary to develop an interim cost allocation methodology was because of the evident deficiencies in GSWC's own cost allocation study. Not only is the use of single allocation factors (which GSWC says it employed to allocate 48% of general office costs) a method the Commission has generally avoided over the years, but there can be no doubt that in view of D.03-05-078, GSWC distorted the traditional four-factor methodology when it assumed that ASUS had only 11 customers, thereby effectively assigning the customer-count factor a value of zero. While GSWC continues to argue that the use of single allocation factors is appropriate here, it cites no support for this argument beyond the handful of cases that were discussed in the PD itself, and as to D.03-05-078, GSWC's opening comments are completely silent.

While the interim methodology described in the text may not be perfect, it has been applied consistently, and it is preferable to the selective and often confusing approach used in GSWC's own study, which clearly ignored important Commission precedents.

[*63]

However, as Mr. Switzer points out in his direct testimony, once GSWC's overall share of general office costs has been determined, the final step in the process is to assign this share to the company's three water regions and to its small electric company, BVEC, which serves the Big Bear vacation area. (Ex. 6, Switzer, p. 16.)

In his own study, Switzer determined the amount of GSWC general office costs assigned to BVEC, 10.27%, by using the Commission's traditional four-factor allocation methodology, the results of which are shown on Schedule C of his study. (Exhibit 6, Switzer Schedule C.) We have decided this same percentage should be used here because, as we understand it, BVEC is a company GSWC has owned for some time, and it is not growing rapidly. Thus, use of the traditional four-factor methodology to determine BVEC's share of general office costs versus those of GSWC's three water districts does not raise the same questions of subsidization that has caused us to reject the four-factor methodology for determining the share of overall general office costs that should be borne by ASUS.

Similarly, the percentages of general office costs that should be assigned to GSWC's three [*64] water districts, which is shown in column (b) of Schedule D of Switzer's study, represents a reasonable application of the traditional four factor methodology and should be used here. Applying the percentages shown in column (b) of that schedule, the share of general office costs attributable to GSWC's California water operations that should be assigned to the three districts (after first making the proper allocations to ASUS, CCWC, and BVEC) are as follows: Region I, 19.60%; Region II, 40.91%, and Region III, 39.49%. n21

n21 As noted in Section 3 of this decision, P 5.10 of the August 4, 2006 stipulation between GSWC and DRA sets forth an agreement between these parties to allocate certain offices' expenses to the Metropolitan CSA. Because we are concerned that these stipulated allocations may be inconsistent with the cost allocation approach we are using in this decision, we are rejecting the terms of P 5.10.

5. GSWC's Request for a New Customer Information/Customer Relationship Management (CIS/CRM) System is [*65] Reasonable, But the Amount Requested is Unsupported and Will Need To Be Established by a Tier 3 Advice Letter

A substantial part of the increase in ratebase that GSWC has requested for its general office is due to the proposed purchase of a new computer system for handling customer service issues. GSWC has requested \$ 9.1 million for this purpose (exclusive of overheads), and asserts that over three years, this amount is needed to serve customers in its regulated operations. GSWC proposes to spend \$ 2,982,841 in 2006 for the first phase of purchasing and implementing the new system. GSWC refers to the new system as the Customer Information System/Customer Relationship Management System; we will refer to it as the CIS/CRM system. GSWC refers to the old system it currently uses as the Customer Information and Billing System; we will refer to this old system as the CIS system.

The company's witness on the CIS/CRM issue was Yvonne Andres, who has worked with the existing CIS system during her entire career. Since 1997, she has been the supervisor for the system and the staff who operate it. She is well-acquainted with its limitations and lays out a detailed case for replacing it.

While [*66] DRA's testimony does not dispute that a new CIS/CRM will eventually be needed, it opposes the company's request in its present form. In particular, DRA asserts that GSWC's current cost estimates for the system are "too generic and too preliminary," and that it appears a significant portion of the new system may be devoted to GSWC's non-regulated affiliates. In view of this uncertainty, DRA argues:

It would be more prudent to evaluate the cost estimates that will be put forth in a formal [Request for Proposal, or UP] from the Company's CIS consultants. At that time a reasonable evaluation on the capabilities and features of the new CIS System[,] along with the Company's internal, regulated and external, Non-regulated needs could be effectively measured. (Ex. 23, pp. 3-3 to 3-4.)

As set forth below, we have concluded that on this issue, DRA has the better of the argument, and that recovery of costs for the new CIS/ CRM system should await the submission of an advice letter with much more detailed cost information than is set forth in GSWC's testimony.

5.1. GSWC's Rationale for Replacement of the Existing CIS System

In her testimony, Andres lays out a detailed justification [*67] for why the proposed new CIS/CRM system is needed. She begins by noting that the present CIS system has significant limitations with respect to its age, design and

system documentation, and she asserts that "the risks of remaining on the current system are substantial enough to jeopardize normal daily operation of the company." (Ex. 5, Andres Testimony, p. 9.)

With respect to the age of the CIS system and the limitations it creates, Andres states:

GSWC's current system was installed in June 1994, but the system itself was actually developed back in 1977. The system utilizes Report Program Generator (RPG) as its programming language, which originated in the 1960s as a report-building program and evolved into a procedural programming language. Like other languages of its type and age, such as COBOL, it has proven cumbersome and hence costly to modify. It is increasingly difficult for the vendor of the system to hire RPG programmers, as the RPG programming language is considered an obsolete skill. Due to the vendor's difficulty in finding and hiring RPG programmers, system modifications routinely take an excessive amount of time to deliver, sometimes later than promised to and needed [*68] by the company. (*Id.* at 2.)

With respect to the CIS system's design, Andres notes that when it was designed in 1977,

[T]he needs of the utilities [were] . . . very stable and static. [The CIS system] was not designed to easily accommodate the realities faced by the utilities today, such as the need:

To implement changes in business rules and processes such as electric deregulation, Sarbanes-Oxley compliance, and Department of Health Services reporting;

To access and analyze customer and billing information for effective and proactive management decision-making;

For a user-friendly interface to the customer and billing information;

To exchange data to or from other utilities such as meter reading management software, third-party payment vendors, financials software, mobile-computing software, and knowledge-management software;

For customer self-service through telephone Interactive Voice Response (IVR) systems, Internet access to account information, and Electronic Bill Presentment and Payment (EBPP). (*Id.* at 2-3.)

Andres continues that in order to meet modern requirements, GSWC has recently had to increase the budget for programming CIS modifications from [*69] \$ 50,000 to \$ 100,000, and that this latter amount "accommodate[s] only the highest priority requirements." She also asserts that some of GSWC's needs - such as mobile computing, Internet access to account information and knowledge management - "cannot be cost-effectively addressed with the current system." (*Id.* at 3.)

Andres also emphasizes that deficiencies in the documentation for the 1977 CIS system have made it difficult to implement modifications even when they are high-priority:

The vendor's system documentation is unreliable and, in some cases, non-existent. So, programming modifications are time-consuming because the vendor programmers must tediously determine how to program the requested modifications without impacting existing system processes. Programming modifications are also prone to errors due to unreliable and/or non-existent documentation. Erroneous programming modifications have been implemented into production, sometimes resulting in erroneous billing calculations. This is becoming a major issue with regards to internal control and Sarbanes-Oxley compliance. (*Id.*)

Andres concludes her discussion of the CIS system by giving examples of problems that [*70] have recently occurred because of the difficulties in modifying the system. These examples include the following:

-- As identity theft in Social Security Numbers became a major problem, our vendor did not have an enhancement ready for the Company to safeguard the SSNs collected from our customers in the database. GSWC submitted a program modification request to the vendor at the beginning of 2004 and was told that it [would] cost a significant amount of programming time and costs. Our vendor was unwilling to further develop the old system and preferred us to migrate to their 'newer' system. As GSWC insisted that this modification is extremely important and should be treated as the highest priority, the vendor agreed to work on the modification request. This program modification was not delivered until December 2004.

-- Service orders are currently generated at local customer service areas every morning and distributed to Water Distribution Operators. When the Operators complete the jobs, they will manually write up the report and pass the service orders back to the office at the end of the workday. The Customer Service Representatives will then manually input the information [*71] into the system and close the service order. This business practice is proven to be inefficient and input errors happen[] all the time. Service orders are not closed in a timely manner[,] thus increasing customers' dissatisfaction . . . (*Id.* at 4-5) n22

n22 Andres also gives examples of problems involving GSWC's efforts to comply with the Sarbanes-Oxley Act, including (1) the difficulty in assigning security access at the function level, (2) the inability of the CIS system to generate lists of all changes performed by the vendor, and (3) the inability to prevent by electronic means, dollar adjustments from being posted to customer accounts until all required approvals have been obtained. To deal with this last shortcoming, GSWC requires all dollar changes of \$ 500 or more to be manually checked and approvals obtained. (*Id.* at 5-6.)

Andres believes there would be at least 10 general advantages to implementing the new CIS/CRM system she is advocating. These advantages include (1) agility in support of new [*72] business requirements, such as Sarbanes-Oxley, (2) lower training costs (such as cutting the training time for a customer service representative in half), (3) better access to and organization of information, (4) a lower incidence of errors, (5) better control of business rule changes, without the need for vendor intervention, (6) tighter user, application and field security, (7) improved customer service, including self-service through web-based Services, (8) lower vendor support costs, (9) faster response to problems, due to an updated technology platform and tools, and (10) increased availability of skilled technologists who do not need to be proficient in outdated programming languages. (*Id.* at 6-8.)

In her direct testimony, Andres acknowledges that the \$ 9.1 million cost given for the new CIS/CRM system is an estimate, and that precise costs will not be available for some time:

The \$ 9.1 million dollar amount is an estimate of cost for a new CIS/CRM, based on standard high-level pricing models of two vendor-independent consultants. A more accurate dollar amount will be obtained once GSWC completes the full RFP phase for a new CIS/CRM. GSWC has not yet issued formal RFPs [*73] because, once a vendor offers a firm proposal in response to an RFP, the proposal will typically expire in a period of several months . . . GSWC has issued an RFP for a CIS consultant to assist GSWC in evaluating, selecting and implementing a new CIS . . . The consultant will be selected by end of first quarter 2006. With the consultant, GSWC expects to issue the RFP for a new CIS in the third quarter of 2006, finalize contract negotiation by year-end 2006, then begin CIS implementation during first quarter 2007. (*Id.* at 9.)

5.2. DRA's Opposition to Including the Costs of the New CIS/CRM System in this Rate Case

In its report on general office issues, DRA opposes approval of the amounts GSWC has requested for the new CIS/CRM system because (1) GSWC's cost estimates are unreasonably vague, and (2) it appears that a significant portion of the new system's capacity may be devoted to serving the needs of customers of GSWC's non-regulated affiliates. After noting the preliminary nature of GSWC's cost estimates, and the fact that the company has only recently begun the process of hiring a CIS consultant, DRA's report continues:

[T]he Company fully utilizes its Customer Service [*74] Center resources to serve a great number of customers in its Non-regulated businesses. For example, currently the Company is serving approximately 74,270 Non-regulated customers under Customer Service Contracts, and the numbers are growing. The Company constantly pitches its 'state-of-the-art' Customer Service Center to attract more Non-regulated business . . .

* * *

What is the driving force behind the need of replacing existing CIS System? Is it the obsolete software language or the demand that the Non-regulated businesses are putting on the Company? For example, in one of its Non-regulated contracts with [the] City of Torrance, the City puts . . . stringent Customer Service Performance Standards on the Company . . .

* * *

It is therefore evident that replacing the existing CIS System must take the Non-regulated related costs into account. Currently, GSWC based its generic costs only on the number of regulated customers; however, once the new System is installed it will also be used to service the Non-regulated businesses['] needs.

The current cost estimates are too generic and too preliminary, rendering approval of this project at this stage not good sense. It would be more [*75] prudent to evaluate the cost estimates that will be put forth in a formal RFP from the Company's CIS consultants. At that time a reasonable evaluation on the capabilities and features of the new CIS System[,], along with the Company's internal, regulated and external, Non-regulated needs[,], could effectively be measured. (Ex. 23, pp. 3-2 to 3-4.)

5.3. Discussion

Although Ms. Andres has presented a good case for why GSWC needs the new CIS/CRM system, and has sought to rebut a number of the points made in DRA's testimony, we agree with DRA that GSWC's cost estimates are too vague, and that there are too many questions about how much of the new system's capacity will be used for GSWC's non-regulated affiliates, to allow us to approve the CIS/CRM funding request proposed in this application.

Rather than approve the \$ 9.1 million (before overheads) that GSWC is seeking here for the new CIS/CRM system, we have decided to approve only the \$ 2.983 million that the company proposed to spend on the system in 2006. (Ex. 5, Andres, Schedule 1.) In order to recover any additional amount, GSWC will have to submit a detailed Tier 3 advice letter which will be subject to protest by DRA, the [*76] City of Claremont, and any other interested party. Before it can be approved by Commission resolution pursuant to General Rule 7.6.2 of General Order (GO) 96-B, the advice letter will have to demonstrate that (1) the new CIS/CRM system is designed principally to meet the needs of GSWC's customers, and (2) any excess capacity in the system is designed to allow for the growth in the number of GSWC customers (and the applications they may need) that can reasonably be expected during the useful life of the CIS/CRM system. GSWC will also be required to demonstrate in the advice letter that it has developed an adequate methodology for charging directly to GSWC's affiliates, whether regulated or non-regulated, a share of the new CIS/CRM system's costs (including overheads) that is fully proportionate to the demand these various affiliates (and their customers) will place upon the new system while it still has excess capacity. The advice letter must clearly explain this methodology, and must demonstrate that the CIS/CRM costs directly charged to the affiliates will not be aggregated with other costs in a way that renders them less than fully transparent. As with other Tier 3 advice letters, [*77] the Water Division will be free to seek as much additional information from GSWC as it considers necessary to prepare a resolution concerning the advice letter for the Commission's consideration. We will also require, in addition to the other service requirements imposed by GO 96-B, that GSWC serve the Tier 3 advice letter upon the assigned Commissioner and the assigned ALJ for this proceeding.

We have decided upon this treatment because, among other reasons, the cost estimates given by Andres are very vague. Not only are they admittedly general estimates "based on standard high-level pricing models of two vendor-independent consultants," (Ex. 5, Andres, p. 9), but an estimated *total* cost for the CIS/CRM system - including those portions that would serve GSWC's affiliates-is not even presented in the company's testimony.

We have commented in Footnote 12 of this decision on the inadequacy of the discussion in SCWC's affiliate transaction reports for 2000-2003 concerning the amounts the company charged directly to affiliates. Those concerns are especially relevant here, where it seems possible that the clients or customers of ASUS, GSWC's principal unregulated affiliate, will demand [*78] even more detailed billing and other information than the residential and business customers in GSWC's three regions are accustomed to receiving. It seems likely that such information demands will place commensurately greater burdens on the resources of the new CIS/CRM system.

While Andres's rebuttal testimony addresses a number of the specific points raised by DRA, it is significant that she does not deal with the larger issues that DRA raises. Thus, for example, Andres spends a good deal of time rebutting DRA's claim that "the 'driving force' behind replacing the CIS/CRM system is to serve 'a great number of customers in its Non-regulated businesses.'" (Ex. 14, p. 1.) Andres's rebuttal on this point includes a table purporting to show that the number of "Non-regulated customers" - i.e., those served via the ASUS contracts with Brooke Utilities, Inc., the City of Torrance, the City of Bell Gardens, the Goleta Water District and Wellspring International, Inc. - fell from 67,892 in 2002 to 43,913 in 2006. (*Id.* at 2.) She also states:

Furthermore, ASUS growth activities are no longer focused on Customer Service Contracts. This is evident by the lack of new Customer Service Contracts [*79] in the past six years. Rather, ASUS activities are and have been focused on contracts that **would not** benefit from the Company's new CIS System." (*Id.* at 2-3; emphasis in original.) n23

n23 In her rebuttal, Andres also addresses DRA's claim that GSWC is seeking a new CIS/CRM system partly to meet more stringent customer service performance standards contained in the contracts entered into by ASUS. Comparing the standards for the City of Torrance cited in DRA's testimony with the standards used by GSWC and within the water industry, she concludes that "the standards of the Non-regulated businesses are less stringent than the Company's standards." (*Id.* at 3, lines 18-19.)

It is noteworthy, however, that Andres does not deny that the new CIS/CRM system has apparently been sized in part to meet the needs of clients and customers served through GSWC's affiliates. n24 Nor does she attempt to address the obvious questions about what kind of demands, and the magnitude of those demands, that the contracts with [*80] military bases ASUS has won (and in some cases is still pursuing) are likely to place on the new CIS/CRM system. Without clear answers to these questions, we cannot approve the funding for the CIS/ CRM system that GSWC is seeking in this application.

n24 Indeed, Andres's rebuttal seems to concede that the customer needs of GSWC's affiliates have been taken into account in the design of the new system when she states that "Non-Regulated customers consist of less than 20% of the total number of customers *serviced through* GSWC's CIS System." (Ex. 14, p. 2, lines 7-9; emphasis added.)

We view the Tier 3 advice letter process that we wish to use for determining how much funding GSWC should receive for the CIS/CRM system as an updated version of a process that parties in water cases have occasionally used during recent years. In D.05-07-022, for example, we approved a settlement involving the use of advice letters for capital improvements in consolidated rate cases filed by CWS. The decision explained the parties' use [*81] of advice letters as follows:

An important feature of the Settlement is the proposal to exclude many plant additions pending the completion of these additions. Parties propose that as each plant addition is completed and in service, CWS may recover the cost through an advice letter filing. Furthermore, each plant addition will be 'capped,' thus establishing the maximum amount that can be included in each advice letter. Should the recorded

cost exceed the cap for any plant addition, the excess cost will be reviewed for reasonableness in the next GRC for the specific district in which the plant addition is located." (*Mimeo.* at 17; footnote omitted.)
n25

n25 Unlike the situation here, the parties in D.05-07-022 ultimately agreed that since work in certain CWS districts was performed under contract by CWS employees for unregulated enterprises, it was appropriate for CWS's shareholders to pay not only for the expenses connected with this work, but also for a share of the common plant used by the CWS employees in their work for the unregulated companies. (*Mimeo.* at 18.)

[*82]

In this case, we think that the paucity of information that has been furnished about the new CIS/CRM system's costs makes it inappropriate to establish a cap for those costs. However, we caution GSWC that if it fails to make the detailed showing described above in its Tier 3 advice letter, then we may well conclude in the resolution concerning the advice letter that it must be rejected, and that GSWC will have to proceed by application to recover the additional costs of the CIS/CRM system. n26

n26 In its August 13 opening comments, DRA argues that allowing GSWC to use a Tier 3 advice letter to recover the balance of the costs for the CIS/CRM system "would diminish the due process rights of the ratepayers and other interested parties," because, *inter alia*, the Water Division might decline to grant discovery to DRA, the discovery period would be shorter than in the application process, and DRA would not have a clear right to an evidentiary hearing. (DRA Opening Comments, pp. 6-7.)

While we acknowledge that the Tier 3 advice letter process is not the full equivalent of an application, it gives to parties who protest the advice letter many of the same procedural protections that the formal application process provides. In view of the concerns that we have set forth in the text about the issues that GSWC's testimony on the CIS/CRM system fails to address, we fully expect that in the event of a protest, the Water Division will provide protesting parties with ample opportunity for discovery and comment. We also reiterate that if GSWC fails to make the necessary showing, then we expect that the resolution the Water Division will present to the Commission in connection with the advice letter will recommend its rejection, and require that GSWC proceed by application to recovery any additional CIS/CRM costs beyond those allowed in this decision.

[*83]

6. The 20 New General Office Positions GSWC is Requesting for Reasons Other Than Compliance With the Sarbanes-Oxley Act

One of the principal issues between GSWC and DRA concerns 25 new positions that the company is seeking for its general office operations. When added together, the salaries for the disputed positions total approximately \$ 1,850,000 (precise salaries are not stated for a few of the more modestly-paid ones). The positions cover a wide range of levels and functions, ranging from a Senior Vice President for Operations (at an annual salary of \$ 209,000) to three Customer Service Representatives (at an annual salary of \$ 36,349 each). Several of the challenged positions relate to GSWC's information systems, including an Application Support Manager (\$ 113,883) and an Assistant Information Technology Manager (\$ 88,564).

In almost all cases, DRA has challenged the need for these positions on the ground that they would duplicate work other people are now performing within the company. For example, with respect to the Application Support Manager, DRA argues:

It is obvious that a duplication of Application Support functions exist[s] in each major functional area.
The [*84] new Application Support Manager position will not replace the existing functional area ap-

plications support resources. The ratepayers will have to bear unnecessary rate burdens because of GSWC having functions duplicated at the centralized and decentralized levels." (Ex. 23, p. 2-12.)

We conclude below that although DRA's criticisms have merit in a few instances, they are misplaced in a large majority of cases. For example, it is clear from both the testimony on the new positions and from Ms. Andres's testimony advocating the new CIS/CRM system that one reason GSWC is seeking the new information technology positions is to reduce its dependence on outside vendors. To accept DRA's arguments that these positions should not be allowed would amount, in most cases, to being penny-wise and pound-foolish.

GSWC's principal justification for five of the new general office positions it seeks is the need to comply with the Sarbanes-Oxley Act of 2002 (SOX). Those positions raise special issues, and we discuss them separately in the next section of this decision.

Although we are allowing virtually all of the non-SOX-related positions GSWC is seeking for its general office, this does not mean we [*85] condone the manner in which the company handled the submission of its testimony. Although GSWC presented a justification for each of the disputed positions in the direct testimony it submitted in February 2006, the company presented a considerably more extensive justification for the positions - especially those related to SOX - in the rebuttal testimony that GSWC submitted on June 9, 2006. The volume of this rebuttal testimony was so large, and the time to consider it so short, that DRA moved to strike large portions of the testimony in a motion filed on June 28, 2006.

Although we affirm the assigned ALJ's decision not to strike this rebuttal testimony, n27 we also endorse his view that -- since the company had previously been criticized in D.04-03-039 for waiting until rebuttal to offer the principal justification for important proposals -- GSWC's conduct was "not . . . exemplary" and should not be condoned. Accordingly, as explained in the final part of this section, we recommend imposing a \$ 50,000 penalty on GSWC for its conduct.

n27 Administrative Law Judge's Ruling Denying Motion of Division of Ratepayer Advocates to Strike Rebuttal Testimony, filed July 12, 2006 (ALJ Ruling Denying DRA Motion to Strike).

[*86]

6.1. Procedural Background of Motion to Strike

The original justification for the disputed general office positions (including those related to SOX) was set forth in the direct testimony of Jenny Darney-Lane, which was included in Exhibit 5 and filed on February 5, 2006. Darney-Lane's testimony covered new labor expense for both Region II and GSWC's general office; her testimony on the new general office positions totaled 35 pages.

On May 25, 2006, DRA filed its responsive testimony in the form of several reports. The testimony on general office issues was included within Exhibit 23 and was sponsored by DRA witness Mehboob Aslam. His testimony on the disputed general office positions comprised 23 pages.

Pursuant to the procedural schedule the parties had agreed to at the May 2, 2006 PHC, GSWC filed its rebuttal testimony on June 9, 2006. On this round, the company's rebuttal on the general office positions not related to SOX was sponsored by Joel Dickson, GSWC's Senior Vice President for Operations and Administration. Dickson's rebuttal testimony comprised 87 pages plus attached exhibits and was admitted into evidence as Exhibit 11.

As noted above, DRA moved to strike all of Dickson's [*87] rebuttal testimony (as well as a portion of Robert Sprowls's testimony concerning the SOX positions) on June 28, 2006. GSWC filed a reply on July 5, 2006. Although the ALJ found that GSWC's conduct in the matter had "not been exemplary" (especially in view of the admonishment the company had received in D.04-03-039), the ALJ Ruling Denying DRA Motion to Strike also concluded that the prejudice to DRA did not appear to be so great as to justify striking the entirety of Dickson's testimony. Instead, the ruling concluded, the preferable course was to follow the Commission's usual practice of admitting the testimony, but then "afford[ing] it only so much weight as the presiding officer considers appropriate." (Ruling, p. 2.)

6.2. The Testimony of GSWC and DRA Concerning the Disputed General Office Positions Not Related to SOX

As noted above, much of the justification for the 20 disputed general office positions not related to SOX is contained in the rebuttal testimony of Joel Dickson, which comprises 87 pages plus extensive exhibits. This rebuttal testimony is divided into three parts. The first 31 pages are concerned with a discussion of 11 changes in the regulatory landscape that [*88] allegedly support the need for the new positions. The next 31 pages (pp. 31-62) set forth a justification for each of the disputed jobs. In the final portion of his testimony (pp. 63-87), Dickson offers an answer to Aslam's criticisms of GSWC's in-house training program that is known as the EDU, as well as to other DRA claims, including the contention that the company withheld information about some general office positions in the prior GRC on general office issues, A.02-11-007.

6.2.1. The 11 Factors That GSWC Claims Have Significantly Increased the General Office Workload

Because the rebuttal testimony frequently refers to the 11 factors that Dickson claims have changed the regulatory landscape and increased general office workload, even though the number of GSWC's customers has remained about the same, we begin with those 11 factors. First, Dickson argues that the need for infrastructure replacement has increased general office needs. He states that in 1996, GSWC undertook 164 capital projects to replace worn-out water supply and distribution facilities, while in 2006 it planned to undertake 276 such projects. Dickson also states that the size of the company's engineering staff [*89] has not increased during this period; instead, to handle the additional work, the company has had to hire outside engineering firms such as CH2M Hill. Dickson also notes that infrastructure replacement increases the demands on other departments (such as GSWC's purchasing department), and requires more coordination between regional management and the communities where streets are being torn up. (Ex. 11, pp. 6-10.)

Second, Dickson argues that GSWC's practice of applying for low-cost financing for its projects, especially under Proposition 50, would be undermined if DRA's staffing recommendations were to be accepted. According to Dickson, the company's 67 applications under Proposition 50 not only required over 500 hours of engineering department staff time in 2005, but also significant amounts of lobbying in the Legislature by senior executives to ensure that private water companies could be beneficiaries of Proposition 50 funding. (*Id.* at 10-11.)

Third, Dickson argues that the increasingly stringent water quality regulations of the past decade (such as for arsenic) have increased the need for general office staff. GSWC operates 41 water systems in California, and Dickson notes [*90] that the new water quality regulations are more complex than their predecessors and often require increased monitoring and management attention. He notes, for example, that when Unregulated Contaminant Monitoring Rule 1 (UCMR1) took effect in 1999, many companies including GSWC found that their contract laboratories had difficulty in reporting the relevant data directly to the U.S. Environmental Protection Agency, as UCMR 1 required, which led to numerous notices of violation nationwide. Dickson also points out that if a well is found to exceed Maximum Contaminant Levels (MCLs), numerous steps and permits are usually necessary before the well can be put back into service. (*Id.* at 12-15.)

The fourth factor Dickson cites is the increased number of water quality lawsuits and the risks associated with them. The company has been involved in over 20 such lawsuits in the past decade, in many of which parties that are potentially responsible for contamination of groundwater supplies sue water distributors such as GSWC on a variety of theories. Although Dickson asserts that GSWC has done well overall in this litigation, the lawsuits require a great deal of time from senior management and [*91] general office staff. (*Id.* at 16-17.)

Fifth, increased certification requirements for water system operators during the past decade have increased required training time, as well as the workload of the Human Resource Department (which must keep track of the certification process). (*Id.* at 17-19.) Dickson notes that the increased certification requirements have made it more difficult to attract and retain appropriately skilled employees, "especially at the most critical level of distribution system superintendent. This is an industry wide phenomenon that was not anticipated by the regulatory agencies when they adopted the [new] rules." (*Id.* at 19.) Dickson also notes that GSWC's Employee Development University has played a critical role in training and qualifying the company's existing employees for certification. (*Id.*)

The sixth factor cited by Dickson is the increased need for water company security brought about by the attacks of September 11, 2001. These include updating Emergency Preparedness and Response Plans (EPRPs) and ensuring that all affected GSWC employees participate in simulations and training related to the plans. The new requirements also require the [*92] Human Resource Department to conduct more intensive background checks, and also require company employees to be present and conduct inspections when outside vendors of chlorine and other chemicals deliver and install dispensing tanks. (*Id.* at 20-21.)

Seventh, Dickson points to the 2001 legislation sponsored by Senator Kuehl that requires builders to prove there will be enough water to serve their projects. The bill, which requires local agencies such as GSWC to verify that they have enough water to serve new projects of 500 or more homes for 20 years, has increased the company's general office workload in a way not suggested by the normal rate of customer growth. Also contributing to the increased workload, according to Dickson, has been the bill by Senator Costa requiring the submission of comprehensive urban water management plans every five years. (*Id.* at 21.)

The eighth factor cited by Dickson is the need to protect GSWC's water supply through water basin adjudication. Dickson states that GSWC's 41 water systems have approximately 300 wells that pump out of 19 separate groundwater basins. Two of the basins are managed, five have been adjudicated, and 12 basins are still [*93] non-adjudicated. Although Dickson believes GSWC's customers have been well-served by the two adjudications the company commenced, these legal proceedings typically last for several years and require an extensive investment of time by senior management, as well as follow-up by operational personnel who serve on basin management committees. (*Id.* at 21-22.)

Ninth, the procurement and dispatching of electric power needed for GSWC's BVEC, which serves the Big Bear vacation area, has increased the demands on GSWC's Accounting Department since the California energy crisis of 2001. Previously, all of the power for BVEC was purchased under a full requirements contract with Southern California Edison Company. (*Id.* at 22-23.)

Tenth, Dickson argues that compliance with the SOX has significantly increased the time demands on GSWC's senior management and general office staff. While these burdens are described in more detail in the testimony of Robert Sprowls, GSWC's Chief Financial Officer, Senior Vice President of Finance and Secretary, Dickson notes that (1) the requirement under SOX § 302 that the Chief Executive Officer (CEO) and Chief Financial Officer (CFO) certify the company's annual [*94] financial statements, (2) the requirement under SOX § 404 that management prepare an annual "internal control report" describing the internal controls for ensuring the accuracy of financial reports, and (3) the requirement under SOX § 906 that the CEO and CFO make a quarterly certification that the financial reports comply with SEC requirements, have all required significant investments of time by senior management, as well as numerous changes in various company procedures. (*Id.* at 23-25.)

Finally, Dickson asserts that regulatory changes at the Commission have significantly increased the workload in GSWC's Regulatory Affairs Department. The principal cause of these changes is, of course, the Rate Case Plan adopted in D.04-06-018 and D.06-02-010. Since GSWC has three districts, the effect of the mandatory three-year GRC filing cycle set forth in D.04-06-018 is to require GSWC to file a separate rate case every year. In addition, Dickson notes, the rate case schedule set forth in D.04-06-018 and the requirement of early data responses to the Master Data Requests "front loads" the workload for the utility. GSWC also receives many more data requests now than in the past. These requirements [*95] have not only increased the workload of the Regulatory Affairs Department, but also the work of the regional offices, where much of the relevant data is located. (*Id.* at 25-28.)

We turn now to GSWC's and DRA's detailed justifications for their positions on the 20 non-SOX general office positions that are in dispute. Following the description of the parties' positions, we set forth our decision for each position.

6.2.2. Senior Vice President-Operations

6.2.2.1. GSWC's Position

Of the 31 pages Dickson devotes to a detailed discussion of the general office jobs in dispute, eight of them concern this position. Dickson argues in some detail that at least 10 of the major regulatory changes described above have contributed to the need for a Senior Vice President-Operations (SVP-Operations), a position that GSWC created in 2002. (*Id.* at 33, 40.) n28

n28 In her direct testimony, Ms. Darney-Lane notes that prior to the creation of the SVP-Operations position in 2002, GSWC's three regions were given general oversight from a Vice President-Customer Service. Today, the three regional vice presidents report to the SVP-Operations, as does the Vice President-Water Quality. (Ex. 6, Darney-Lane, p. 7.)

[*96]

Dickson takes particular issue with DRA's assertion that the position is not needed because GSWC's operations "have generally remained the same over the years." After pointing out that the increased environmental, water quality and water litigation issues described above have greatly increased the company's workload, Dickson continues that it would be impossible to do all of this work without an SVP-Operations, because "GSWC's operations are more complex than most utilities due simply to the geographical diversity and varied nature of its service areas." (*Id.* at 33.)

Dickson notes, for example, that the SVP-Operations has played a critical role in seven recent situations where wells had to be taken offline because they exceeded applicable MCL standards. In June 2003, for example, Goodyear Well No. 4, which serves the company's Florence-Graham system, had to be taken offline because the MCL for trichloroethylene, a carcinogenic volatile organic compound, had been exceeded. It took until January 2004 to assess the options and then file a new permit application with the California Department of Health Sciences (DHS). The permit was not granted and the well put back in service until [*97] October 2005. Dickson notes that putting this well back into service required the company to undertake all nine of the regulatory steps described in his testimony, in addition to the necessary design, engineering and construction work. (*Id.* at 15, 34) n29

n29 Other situations where the SVP-Operations has had to supervise wells being removed from service and new permits being applied for include Converse Well No. 1 (carbon tetrachloride, 12 months to resolve); Hawaiian Well No. 1 (arsenic, 12 months to resolve); Massinger Well No. 1 (arsenic, 33 months to resolve); Centralia Nos. 3 and 4 (arsenic, 5 months to resolve); Century No. 1 (arsenic, 8 months to resolve). (*Id.* at 34-36.)

In cases where new permits were needed to address the updated arsenic standards, GSWC often filed the permit applications months before the new standards took effect. As a rule, however, the wells were left in service until just before the new arsenic standards took effect on January 23, 2006.

Dickson notes that another reason the [*98] new position is needed is that the SVP-Operations is frequently called upon to coordinate the work of several major company departments. In addition to coordinating the work of the Engineering, Operations and Water Quality departments in the water quality lawsuits he describes, Dickson gives the following example of the need for coordination among departments in connection with new EPA rules:

The Interim Enhanced Surface Water Rule (>10,000 population) and the Long Term 2 Surface Water Treatment Rule (<10,000 population) amended the original Surface Water Treatment Rule. The Long Term 2 Enhanced Surface Water Treatment Rule builds upon earlier rules to address higher risk public water systems for protection measures beyond those required for existing regulations. The LT2ESWTR is being promulgated simultaneously with the Stage 2 Disinfection Byproducts Rule (DBPR) to address concerns about risk tradeoffs between pathogens and DBPs. Both the LT2ESWTR and the Stage 2 DBPR contain initial requirements for extensive and complicated monitoring programs before the rules are in full effect. The initial monitoring and subsequent evaluation of data will determine the full impact of the [*99] rules for each system. Both rules will require significant effort and oversight to manage. Consequently, it is very likely that many utilities -- including GSWC -- will be required to either build new facilities or provide significant modification to treatment facilities located at treatment plants impacted by these rules. The role of the SVP-Operations will be critical because the Engineering, Operations and Water Quality components will need to be balanced and there will be the need for completing new facilities as part of the overall Company Capital Projects program. (*Id.* at 36-37; emphasis supplied.)

In addition to this coordination role, Dickson points out that the SVP-Operations (1) ensures oversight and company-wide consistency in reviewing and practicing the EPRPs and other security measures, (2) provides oversight of the company's capital improvement program, which has grown from \$ 24.4 million in 1995 to over \$ 60 million in 2006, (3) ensures that the new certification requirements for water system operators are adequately communicated to the Human Resource and EDU departments, (4) exercises ultimate responsibility for water supply planning through the Regional Vice [*100] Presidents, who report to him, and (5) has primary responsibility for oversight of the water basin adjudication process, which in the case of the Santa Maria Basin consumed "countless hours" of the time of the SVP-Operations. (*Id.* at 37-39)

Dickson is particularly critical of DRA for failing to recognize the role of the SVP-Operations in SOX compliance. On this issue, Dickson states:

DRA claims that because there were no 'material weaknesses' in GSWC's internal controls, the position of SVP-Operations is not needed . . . What DRA fails to recognize is that the SVP-Operations was in fact in place and part of the process that lead to the findings of 'no material weakness' in the final audit reports. The SVP-Operations position provides a critical review point and control structure for both the regional financial accounting and capital projects accounting processes. (*Id.* at 40.)

Elaborating on this, Dickson notes that all of GSWC's capital spending "occur[s] not in the Accounting Department but in Operations," and that "the SVP-Operations has to ensure that all controls are followed and sign off that such is the case on a quarterly basis." The company's large capital budget [*101] requires the high-level oversight provided by the SVP-Operations, Dickson continues, because "capital construction at the current levels makes it one of the Company's most significant risk factors." (*Id.*) n30

n30 In her direct testimony, Darney-Lane states that "approximately 10% of the SVP-Operations job is related to compliance with Sarbanes-Oxley." (Ex. 6, Darney-Lane, p. 11.)

6.2.2.2. DRA's Position

The basis for DRA's opposition to the SVP-Operations position is that the new job would duplicate functions that are already being performed adequately within the company. DRA's testimony states:

GSWC argues that the current complexity in Water Quality Compliance, Water Quality Litigation, Infrastructure Replacement & Investment, Water Supply Needs, and Sarbanes-Oxley Act, warrant this new position. Furthermore before the creation of this position in 2002, the GSWC service area regions were managed by the Vice President- Customer Service. Now, the GSWC's operations are spread among three regions, each [*102] serving between 55,000 to 100,000 customers and each having a regional vice president who report to the Senior Vice President-Operations.

DRA does not find the justifications for the position compelling. First, GSWC's operations have generally remained the same over the years. The so-called 'Water Quality Compliance' functions are nothing new for a water utility operating in California. GSWC already has a Water Quality Department and a Regulatory Compliance Department, each of which is adequately staffed and has its own vice president. These facts militate against the need to add yet another management layer in the GSWC's organizational structure. (Ex. 23, p. 2-3.)

After describing the water quality staffs that already exist in GSWC's general office and regional staffs, as well as the "elaborate engineering staff" found within each region, DRA concludes:

By requesting [the SVP-Operations] position, GSWC in effect is implementing a 'centralized' approach to its operations. However, GSCW does not show any savings that should result from this centralized structure. In fact, the ratepayers will be burden[ed] with both the decentralized and centralized structure working at the same [*103] time. (*Id.* at 2-4.)

6.2.2.3. Discussion

Although Dickson's testimony does not answer all of the questions one might have about this position, n31 we conclude that on balance, GSWC has made an adequate showing that the growth in the general office's workload makes the SVP-Operations position necessary and appropriate to include in rates. We do not agree with DRA the job is unnecessary because "GSWC's operations have generally remained the same over the years." (Ex. 23, p. 2-3.)

n31 Although the record is not entirely clear on the point, it appears that Dickson is currently serving as GSWC's SVP-Operations. Although Dickson described himself on the stand as GSWC's "senior vice president with operations and administration," he also stated that he is responsible for "all the functions within the company but the financial functions that Mr. Sprowls oversees." (Tr., p. 975.) In his testimony, Sprowls states that his job title is "Chief Financial Officer, Senior Vice President of Finance and Secretary of GSWC." (Ex. 17, p. 1.)

On the other hand, the 2005 and 2006 Annual Reports for GSWC's corporate parent, American States Water Company, lists the following four Senior Vice Presidents and their titles for GSWC: Dickson (Senior Vice President), Sprowls (Chief Financial Officer, Senior Vice President of Finance and Secretary), Denise L. Kruger (Senior Vice President of Operations), and Susan L. Conway (Senior Vice President of Administrative Services). Neither GSWC's briefs nor testimony explain the apparent overlap between the roles of Mr. Dickson and Ms. Kruger, or the duties of Ms. Conway.

[*104]

We begin by pointing out, of course, that the company has had an SVP-Operations since 2002, and it is only because the job was created after the filing of GSWC's last general office rate case, A.02-11-007, that we have not been asked previously to authorize this job.

Dickson's testimony makes a strong case that the position is needed to coordinate GSWC's far-flung operations and provide oversight of its ambitious capital construction program. The energetic debate described in D.00-06-075 and D.04-03-039 about whether region-wide rates should be authorized for GSWC's Region III is strong evidence that the geographically spread-out operations of the company, especially in Region III, present special management challenges. (See D.00-06-075, *mimeo.* at 23-30; D.04-03-039, *mimeo.* at 22-25.)

It is clear from GSWC's testimony that the size and scope of its capital construction program has grown so substantially in the past decade that senior management oversight is needed. As Dickson notes, the capital projects budget grew from \$ 24.4 million to over \$ 60 million between 1996 and 2006, and the number of projects during this period increased from 164 to about 276. Although GSWC [*105] is also seeking authority for a Capital Projects Manager in this GRC, the need for senior management oversight of the capital program seems obvious.

Dickson also makes a persuasive case that coordination from a senior executive will be necessary to ensure that the new water quality rules he cites are properly implemented, and to ensure that the new treatment facilities (or modifications to existing facilities) needed to comply with them are constructed on a timely basis and at reasonable cost. As noted in Dickson's rebuttal testimony, these rules include the Interim Enhanced Surface Water Rule, the Long Term 2 Surface Water Treatment Rule (LT2ESWTR), and the Stage 2 Disinfection Byproducts Rule (DBPR). (Ex. 11, pp. 36-37.) The need for correct and coordinated implementation of the LT2ESWTR and the Stage 2 DBPR seems especially great, because -- as Dickson notes -- these rules are being promulgated simultaneously "to address concerns about risk tradeoffs between pathogens and [disinfection byproducts.]" (*Id.*)

Although Dickson's testimony makes a less compelling case that the SVP-Operations is needed to ensure company-wide consistency in practicing security measures and complying [*106] with new operator certification requirements, he is persuasive when he argues that the SVP-Operations is needed to oversee the company's water supply planning, supervise water basin adjudications, and help ensure that SOX requirements are met at the operational level by providing a "critical review point and control structure" for regional financial accounting and capital projects accounting.

We will authorize the position of SVP-Operations to be included in rates, and we reject DRA's view that the position be disallowed. n32

n32 On page 2-5 of his report for DRA, Aslam states that if the Commission authorizes the new position of SVP-Operations, DRA is not opposed to GSWC's proposal to split the salary for the existing position of Administrative Secretary-Operations between the new SVP-Operations and Vice President-Customer Service for Region I.

6.2.3. Capital Projects Manager-Operations

6.2.3.1. GSWC's Position

Dickson presents three principal justifications for this \$ 124,160 per year position. The first [*107] is that GSWC's capital budget has grown so substantially in the past decade (from \$ 24.4 million to over \$ 60 million) that the decentralized model of construction supervision the company previously used -- which relied on GSWC's three District Engineers for oversight, scheduling and inspection of construction projects -- is no longer feasible. In 1996, according to Dickson, the company undertook about 160 water main replacement and supply projects, permitting for them was relatively straight-forward, and most of the projects could be completed within a year. Today, on the other hand, GSWC must handle about 275 projects per year, many more permits are required, and it is unusual for a project to be completed within 12 months. (Ex. 11, pp. 42-44.) n33

n33 Dickson points out that in 1996, it was unusual for GSWC to have to obtain a Conditional Use Permit (CUP) before beginning construction, and there was no requirement that the company obtain an NPDES discharge permit, submit geotechnical studies or *Traffic Control Plans*, or (usually) undergo a full CEQA review before beginning construction. Today, all of these things are required before construction can commence. (*Id.* at 43.)

[*108]

All of this, Dickson submits, shows that GSWC's existing engineering resources are inadequate to perform the work they are being asked to undertake, which is why the company had to hire an outside firm (CH2M Hill) to provide the 30 full-time equivalent staff needed to do the work on the 2005 construction program. Hiring a full-time Capital Projects Manager is the first step in expanding GSWC's internal resources, since "the position will be tasked with completing all the other steps." (*Id.* at 45) n34

n34 In her direct testimony, Darney-Lane notes that 2004 was the first year in which GSWC tasked someone with the assignment of acting as a capital projects manager. As a result of this trial run, "his help alone contributed to our timely closing of over 300 [General Work Orders] in 2004." (Ex. 6, Darney-Lane, p. 13.)

Dickson also notes that a Capital Projects Manager will be able to provide better coordination and scheduling for all of the work being performed within the three districts. He gives the following explanation: [*109]

With the expanded capital program comes a need to refine the approach to project implementation to ensure the most cost effective methods of project delivery are utilized . . . [The increase in projects from 1996 to 2006] requires different tracking mechanisms, different resource allocation methodologies, different delivery methods and an overall different approach to successful completion . . .

Another key point directing the need to add the Capital Projects Manager is that the types of projects under construction benefit from centralized oversight. GSWC's capital program consists primarily of water main replacement, well replacement, and reservoir replacement . . . With the common nature of the type of work from Region to Region, it only makes sense, then, to look at the program on a company-wide basis. For example . . . GSWC's Region 2 and

Dickson adds that a Capital Projects Manager will enable the company to be more nimble in moving resources around in the event delays are encountered on a particular project, and that the new manager will also be in a better position to draw upon the expertise that particular Regions have acquired on particular projects. (*Id.*)

6.2.3.2. [*110] DRA's Position

Aslam's testimony concerning the Capital Projects Manager's position is a really a general criticism of GSWC's alleged inefficiencies in managing construction projects:

DRA finds GSWC's argument [for centralized control] unpersuasive. Instead, GSWC's proposal reflects a level of inefficiency and lack of planning on behalf of GSWC. As mentioned earlier, GSWC decentralized its Engineering Operations throughout its three Operating Regions, which resulted in an elaborate Engineering staff within each Operating Region. For example, a typical engineering staff at one of the GSWC's regions consists of Engineering and Planning Manager, Senior Civil Engineer, Civil Engineer, Engineer, and several Engineer Technicians and CAD Operators. GSWC's claim that the company's engineering staff in each of its Operating Regions has to compete for the same resources of contractors and outside consultants for their respective projects hold[s] no water. (Ex. 23, pp. 2-5 to 2-6.)

Although he gives no examples, Aslam also argues that other Class A water companies doing business in Southern California must operate with similar constraints, which demonstrates to him that "better planning [*111] and self reliance are necessary in this labor competitive environment." (*Id.* at 2-6.)

6.2.3.3. Discussion

We conclude in this case that GSWC has carried its burden of proof on the need for a Capital Projects Manager for Operations. While managing construction projects from within each Region may have made sense in 1996 - when engineering and permitting requirements were simpler and the company's operations had just been organized into three regions - the growth in the amount of the capital projects budget, the significant increase in the number of projects, and the increasing complexity of permitting and engineering requirements, all lend support to Dickson's argument that there is a need for a senior construction manager who can provide increased coordination in soliciting construction bids, scheduling work, and so forth. In view of the increase in the amount of project design work - a situation that required GSWC to outsource a significant amount of the engineering for its capital projects in 2005 - DRA's criticisms that the company already has an "elaborate engineering staff" within each region, and that the current situation demonstrates "inefficiency and lack of planning," [*112] are not persuasive.

6.2.4. Administrative Support Analyst - Operations

6.2.4.1. Positions of the Parties

In his rebuttal testimony, Dickson argues that this \$ 58, 208 per year position - which would report directly to the Capital Projects Manager - is needed to manage the documentation for the company's ambitious construction program:

With the growth of the capital program comes the increased need for additional analysis and oversight of the capital construction program. As discussed above, complete new delivery methods of construction are needed to improve the efficiency and cost-effectiveness of the construction program. This position is critical in analyzing the status of construction projects and construction contracts for completeness and accuracy and in providing an overall analysis of the program. With over 150 jobs in construction at one time, it is critical to ensure every contract, invoice, change-order and other construction documentation is in order. (Ex. 11, p. 47.)

Dickson notes that the new administrative support analyst would also pull together and analyze statistics necessary to make key decisions in construction resource allocation, construction scheduling, [*113] and the status of contracts and contractors. (*Id.*)

In its testimony, DRA opposes authorizing this position for the same reasons it opposes the Capital Projects Manager position. (Ex. 23, pp. 2-6 to 2-7.)

6.2.4.2. Discussion

In view of the growth of GSWC's capital projects program during the past decade and the need for centralized supervision over it, it is not surprising that the company is requesting an assistant to handle documentation and statistical analysis for the Capital Projects Manager. We think that the company has made an adequate showing to support authorization of this position.

6.2.5. Assistant Application Support Analyst - Operations

6.2.5.1. Positions of the Parties

Like the Administrative Support Analyst, this \$ 50,189 per year position would also report to the Capital Project Manager. In his rebuttal testimony, Dickson argues that this position - which the company currently outsources - is needed to make efficient use of GSWC's new Project Control System (PCS) software:

GSWC has begun to utilize a [PCS] based on PrimaveraTM in conjunction with Microsoft ProjectTM. The PCS was established to track and report on the status of capital projects. [*114] PrimaveraTM is the construction industry standard software used for this purpose, and facilitates project delivery on time and on budget. The PCS allows for tracking and reporting on metrics such as project schedules, milestones, resources, budgets versus costs, cash flow, estimated completion times, project schedule estimated at completion and project cost estimated at completion. The PCS also tracks project issues and resolution of those issues, provides project descriptions and details lessons learned from projects for use on other similar projects. The PCS is also able to track and report at a program level, allowing better management of company-wide resources. Use of this needed tool can only be successful under the direction of an individual skilled in programming and updating the software and its inputs. (Ex. 11, p. 48.)

In addition to the salary savings the company expects to realize by bringing this position in-house, Dickson notes that the position "will allow GSWC to migrate its entire capital program to the PCS platform . . . GSWC currently only has a small number of projects being tracked in the PCS, which severely limits our ability to fully benefit from the value of [*115] the PCS." (*Id.*)

In its testimony, DRA states that, as with the Capital Project Manager position, this job should be disallowed because the company has failed to show a need for reorganizing how it handles construction projects, and has also "failed to show any cost savings that would result from such centralization." (Ex. 23, p. 2-7.)

6.2.5.2. Discussion

It is not surprising that in order to bring about the centralized control over its construction program that the office of Capital Project Manager promises, GSWC would need new software. Moreover, even though the company is apparently spending a significant sum to outsource the programming and updating of this software, it has not yet been able to place its entire capital program on the new PCS system.

We will authorize the requested position so that the promised efficiencies can be realized, but in GSWC's next general office GRC, we will expect to see a persuasive demonstration that the promised construction efficiencies have been realized.

We would also point out that the justification provided for this position in the company's direct testimony - as well as the justification for the Administrative Support Analyst for Operations [*116] - consisted of little more than a job description of the kind that might be posted on a company bulletin board or website. (Ex. 5, Darney-Lane, pp. 15-16.) Such job descriptions are not very informative, and it is not surprising, therefore, that DRA chose to oppose the position. In future GRCs, we expect to see a fully adequate justification for this and other new positions set forth in the company's direct testimony.

6.2.6. General Clerk - Information Technology

6.2.6.1. Positions of the Parties

In his rebuttal testimony, Dickson argues that GSWC needs this \$ 30,000 per year position because GSWC now receives payments in many more varied forms than in the past, a situation that has proven quite labor-intensive to deal with:

Over the past few years more and more customers are now paying their water bills through payment agencies, banks and financial institutions. This type of payment makes it easier for the customer, but often requires much more manual work for GSWC. For example, when payments are received through CheckFree they are entered electronically into our system. However, for most other institutions, includ-

ing EPrinceton.com, the data arrives in a file that we [*117] cannot use electronically or on printed paper forms. We also receive multiple checks from financial institutions with an accompanying printed listing with the customer's name, account number and amount paid. All of this data must be manually entered into our system, the account numbers verified and control balanced along with other payments. There are 500-700 of these manual entries keyed in and verified each day. This requires 5-8 hours of real time, employee activity per day to complete this task. (Ex. 11, p. 49.)

DRA devotes a surprisingly large amount of discussion to its opposition to this position. After noting that the justification given for the position seems to entail more than "processing electronic bill payments from banks and internet service providers," Aslam states:

Currently a staff of 19 is employed within the GSWC's Information System Department in General Office. Five of them are General Clerks. In addition, GSWC regularly hires temporary workers as needed. GSWC did not present any analyses that explained the reasons behind the increased level of activities in [the] mail room. (Ex. 23, p. 2-7.)

Aslam goes on to suggest that customer growth in GSWC's regulated [*118] operations cannot be the reason for the new position, since there have been only about 8,000 new customers during the past five years. Instead, Aslam speculates, the new position is needed to provide service to customers of the entities served by GSWC's non-regulated affiliates, customers who total 74,270 by Aslam's count. (*Id.* at 2-7 to 2-8.)

6.2.6.2. Discussion

As with several of the other new positions GSWC is requesting and DRA is opposing, opposition to this job might have been avoided if GSWC had initially provided a straight-forward explanation of the need for the position along the lines set forth in Dickson's rebuttal testimony. Instead, the company's direct testimony consists of another job description that suggests the key task - data entry of payments in non-check form - only briefly. (Ex. 6, Darney-Lane, pp. 16-17.)

Even though GSWC did not do a good job of justifying this position in its direct testimony, the need for the position (given the limitations of GSWC's current computer system) seems clear. We also think that our resolution of the general office cost allocation issue elsewhere in this decision is adequate to address the cross-subsidy concerns raised [*119] by DRA, to the extent they have merit.

Although we are approving the General Clerk-Information Technology position, we emphasize that we are doing so only for this GRC cycle. It seems to us that if the new CIS/CRM system delivers all of the benefits that Ms. Andres describes in her testimony, the position will become unnecessary once the CIS/CRM system is on-line.

6.2.7. Assistant Information Technology Manager- Information Technology

6.2.7.1. Positions of the Parties

In his rebuttal testimony, Dickson argues that this \$ 88,564 per year position is needed to ensure the security of GSWC's hardware, software, and data bases, and that "there currently isn't an individual within the Company with the expertise" to do this. (Ex. 11, pp. 48-49.) He notes that each of the 11 factors he identifies as having changed the regulatory landscape has contributed to the need for an Information Technology (IT) security officer, as has the increase in the size of GSWC's infrastructure replacement program. (*Id.* at 49.) Dickson also notes that SOX makes having an IT security officer essentially mandatory:

SOX has necessitated that the IT Department develop and review change control systems [*120] for all applications software and operating systems as well as Internet security throughout GSWC in order to comply with Section 404. Approximately 33% of this position's job functions are related to Sarbanes-Oxley compliance. Controls and security have become of paramount importance since the passing of the Sarbanes-Oxley legislation. Conducting reviews and daily monitoring of IT controls, and financial application security records is a time consuming function. These areas require constant monitoring and frequent review and auditing of report and system log records, which is currently putting a strain on internal personnel resources. (*Id.* at 50-51.)

DRA opposes this position mainly on the ground that GSWC's Information System Department already has 19 people, 14 of whom are IT-related staff. (Ex. 23, p. 2-8.) In addition, DRA notes that "GSWC obtains IT[-]related help on [a] regular basis from outside consultants and vendors," and claims to have found no evidence to support the Company's assertion that 33% of the new position's duties are related to SOX compliance. (Id. at 2-9.)

6.2.7.2. Discussion

It is virtually common knowledge that security concerns in IT Departments [*121] the size of GSWC's are rapidly increasing, and that people with the skills necessary to deal with these issues can command a premium. It is also not surprising that GSWC would want to have the necessary expertise in-house, rather than having to rely on outside contractors. Thus, we find DRA's general criticisms of the rationale offered by Dickson for an Assistant IT Manager to be unpersuasive.

We also think it is not unreasonable to assume that one-third of the Assistant IT Manager's time would be devoted to dealing with SOX compliance. As Dickson states in his description of the 11 major factors that have changed the regulatory landscape, SOX § 404(a) requires companies such as GSWC to prepare an annual "internal control report" that "state[s] the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting." Further, SOX § 404(b) requires each "registered public accounting firm" that prepares or issues an audit report for a company like GSWC to "attest to, and report on, the assessment made by the management of the issuer." We do not doubt Dickson when he states that these requirements have increased [*122] the amount of time the company's senior managers must spend interfacing with its auditors. We are also persuaded when Dickson says of SOX § 404(b):

It also requires the Company to continually assess 16 mega accounting processes and document and test about 250 key controls (more than 400 key controls in 2004) to ensure compliance. This requires a continuous monitoring and updating of accounting policies and procedures. (Id. at 25.)

In short, we think that GSWC has met its burden of proving that the position of Assistant IT Manager is necessary, and we will authorize this position to be included in rates.

6.2.8. New System Administrator-Developer - Customer Service

6.2.8.1. Positions of the Parties

Dickson's arguments in favor of this \$ 68,307 per year position complement those set forth in the testimony of Yvonne Andres, the company's principal witness on the need for a new customer service computer system. Dickson states:

The Company is in desperate need of a new CIS/CRM System. This position is needed to assist in report writing, customization and modification of programs for the new CIS/CRM System that is being requested as part of this application. This position [*123] is also in charge of documentation of change management and maintains the integrity of program code. This position will also assist in system administration and upgrade processes. Having a developer in-house will significantly decrease the programming time and cost related to hiring an outside consultant. This position will ensure consistency of implementation without having to pay for outside vendor support. (Ex. 11, p. 51)

In its report, DRA does not question the tasks proposed for this new position, but points out that "the Commission has not yet approved and authorized the CIS/CRM System projects. This requested new position is therefore unnecessary until the CIS/CRM System project[] is authorized by the Commission." (Ex. 23, p. 2-9.)

6.2.8.2. Discussion

As noted in our discussion of Ms. Andres's testimony, we believe she has made a good case for the need for the new CIS/CRM system, and for having an in-house capability to customize and modify the software for it. However, because the company's cost estimates for the CIS/CRM system are so preliminary, we are declining at this time to authorize more than the \$ 2,982,841 (before overheads) that the company has requested for [*124] calendar year 2006 to pay for the new system. As stated in section 5.3 of this decision, in order to recover any greater amount, GSWC will be required to use the new Tier 3 Advice Letter process under General Order 96-B, a process that requires Commission

approval of the advice letter by resolution before it can take effect, and also allows affected parties such as DRA to file protests.

In light of this, there is considerable appeal to DRA's argument that the Commission should not approve the New System Administrator-Developer position at this time. However, we also recognize that in order to begin deployment of the new CIS/CRM system, the Services of the Administrator-Developer are likely to be necessary. Since we expect that a substantial sum for the new CIS/CRM system will ultimately be included in rates (although perhaps not as much as GSWC is requesting in this application), we will authorize the new position.

6.2.9. Three New Customer Service Representatives

6.2.9.1. Positions of the Parties

In both its direct and rebuttal testimony, GSWC requests that it be authorized to increase the number of full-time customer service representatives (CSRs) from 21 to 24, at an annual [*125] cost of \$ 109,047 (without overheads). GSWC argues that although the number of its retail customers has not grown a great deal in recent years, the increase is justified because (1) the average time devoted to each customer service call has increased, (2) the turnover rate among temporary CSRs (of whom the company has three) is high, and (3) it is less expensive to hire permanent CSRs rather than temporaries, due to the high training costs. (Ex. 5, Darney-Lane, pp. 21-22.)

In his report, DRA's Aslam opposes the request because he thinks the real reason GSWC is seeking more CSRs is to deal with calls from the 74,270 retail customers Aslam believes are served through contracts with ASUS, GSWC's non-regulated affiliate. Aslam states:

GSWC historically did not request new CSRs when there were no Non-regulated contracts. For example, in year 1998, GSWC had 16 CSRs that served a total of 241,491 regulated customers. This represented a ratio of one CSR to 15,093 customers. However, in that year, GSWC did not request additional CSRs in it[s] GRC application, thus implying that the ratio of 1:15,093 was working well.

In year 2002 when GSWC was serving 248,776 regulated customers, it [*126] requested 5 additional CSR positions in General Office, raising the total CSR positions to 21, which results in a ratio of one CSR to 11,846 regulated customers when at that time GSWC began serving Non-regulated customers. Therefore, applying a ratio of 1:15,093 for CSRs staffing to the present number of regulated customers, only a total of 18 CSRs would be necessary. (Ex. 23, p. 2-10.)

In his rebuttal, GSWC's Dickson argues that the three additional positions are necessary to meet GSWC's internal standards for call response time:

DRA states the Customer Service Center had 16 representatives to address the customers' needs. In reality, GSWC had had no less than 20 CSRs since 1998. The request for 24 CSRs is not due to an increase in the amount of non-regulated calls; rather it is to address the service level needs of our regulated customers and the increasing call volume.

Eighty percent (80%) of calls are to be answered in forty . . . (40) seconds or less, this is the established service level for GSWC. The industry standard is eighty percent (80%) of calls in thirty seconds or less. The Customer Service Center (CSC) requires an average of 24 representatives to support the [*127] 80/40 standard service level and scheduling needs. (Ex. 11, p. 52.)

6.2.9.2. Discussion

As noted in Section 4.3.5 of this decision, GSWC's non-regulated affiliate, ASUS, does not provide customer call service to all of the retail customers of the entities with which it has contracts. Moreover, we think the equivalent number of full retail customers that can be attributed to ASUS is about 33,370, approximately 45% of the number that Aslam assumes. Thus, we do not find Aslam's analysis of the reasons that GSWC has requested three more CSRs to be persuasive. Instead, we are persuaded by Mr. Dickson that the increase (which is really designed to bring the temporary CSR positions in-house) is needed to maintain the current standard of call response time. We also think Ms. Dar-

ney-Lane is correct in asserting that bringing these positions in-house will serve to reduce turn-over and hence training costs.

Accordingly, we will authorize GSWC to include the three new CSR positions in rates.

6.2.10. Call Center Support Analyst

6.2.10.1. Positions of the Parties

GSWC's testimony notes that this position was created in 2003, in large part to free up the time of the Customer Service [*128] Supervisor so that he or she can focus on training and coaching GSWC's 24 CSRs. In his rebuttal testimony, Dickson states:

The support position of Call Center Support Analyst allows the supervisor to focus effectively on the important tasks of coaching, developing, and training, thus improving service levels. As discussed above, GSWC has a standard of answering 80% of calls within 40 seconds, a goal much lower than the industry standard of 80% of calls within 30 seconds. GSWC has achieved this mark of 80/40 only 112 out of the past 60 months.

The full scope of responsibility for this position includes: payroll entry, attendance/punctuality tracking, scheduling, escalations [i.e., requests to speak to a CSR's supervisor], and informal PUC complaints. By providing support for these tasks, the supervisor's attention can be dedicated to the development of each CSR. This has allowed GSWC to meet its service level goal for seven months in a row starting fourth quarter 2005 into 2006. (Ex. 11, p. 53.)

DRA opposes authorization for the Call Center Support Analyst because it believes the position was "hidden" from DRA in GSWC's last general office GRC, A.02-11-007. On this issue, Aslam [*129] states:

[In A.02-11-007] GSWC did not justify the need for the position. The salary expense for the position was hidden as part of the overall labor expense. DRA protests this sort of evasiveness. GSWC must present and justify all additional expenses clearly and specifically. The Commission's approval of an overall labor expense should not be interpreted as Commission approval for new positions, especially when the new positions are not specifically requested. This elusiveness deprives DRA of fair notice and due process and obstructs the Commission's ratemaking responsibilities. (Ex. 23, pp. 2-11 to 2-12.)

6.2.10.2. Discussion

On the question of whether a Call Center Support Analyst should be authorized, we conclude that GSWC has the better of the issue.

Although DRA vaguely suggests that the GSWC's Call Center is overstaffed, the real source of its opposition to the position seems to be the perception that it was somehow misled about the position in A.02-11-007. In his rebuttal testimony, GSWC's Dickson emphatically denies this, and insists that A.02-11-007 was handled like the company's prior rate cases:

Mr. Aslam claims the positions were hidden in the last [GRC] [*130] and that DRA had no opportunity to review them or rebut the need for them. This is not true. The DRA had every opportunity to examine all costs requested by GSWC and make recommendations. Labor costs in total were examined and cost increases and upward trends in labor expense were closely examined by DRA. The DRA staff assigned to that part of the case chose which costs to challenge and which costs not to challenge . . . There have been many GRCs filed by GSWC over the years where the DRA chose not to challenge various positions. In instances where DRA did challenge the positions[,] detailed justification was always provided upon request. (Ex. 11, p. 76.)

We find this defense of GSWC's conduct in A.02-11-007 persuasive; Aslam has not presented any evidence that in A.02-11-007, DRA asked about the Call Center Support Analyst and received an inadequate or misleading response.

Moreover, GSWC has made a convincing case that the job is needed to free up the time of the Call Center Supervisor to train and coach the staff of 24 CSRs. Accordingly, we will allow this position to be included in rates. n35

n35 Dickson also points out in his rebuttal testimony that GSWC ratepayers are being asked to pay only 69% of the cost of the Call Center Support Analyst position; the rest is charged to the "new business" accounts of GSWC's non-regulated affiliate, ASUS. (Ex. 11, p. 53.) Dickson does not comment on what this may signify about how many of the calls that come into the Call Center are from customers of GSWC versus customers of the entities with which ASUS contracts.

[*131]

6.2.11. Applications Support Manager - Applications Support

6.2.11.1. Positions of the Parties

In her direct testimony, Ms. Darney-Lane states that GSWC's IT department "offers efficiency primarily in the hardware side of the technology." (Ex. 5, p. 24.) The choice of software, on the other hand, has been left up to now in the hands of the company's various "functional areas":

Major application software selections and upgrading are located in [the] respective functional area[s]. For example, the customer service application software was selected and has been maintained by the Customer Service Center; operations select and maintain software such as SCADA for enhancing the data gathering and operating efficiency; [the] Accounting and Finance department provides application supports for accounting/finance, job costs and payroll/human resources related enterprise software." (*Id.*)

Darney-Lane continues that this new \$ 113,883 per year position will offer the following advantages to GSWC:

Provide consistency and documentation for all application implementations and upgrades.

Direct and lead business process analysis for efficiency improvements among all GSWC's divisions.

[*132]

Integrate all application systems to enhance overall performance of the system.

Ensure integrity of system transactions among all applications for internal control purposes.

Direct the development of applications to meet company-wide business process requirements and to eliminate localized developments.

Oversee and review security architecture standards, database integrity and testing procedures for new implementations. (Ex. 5, pp. 24-25.)

In his report for DRA, Aslam recommends this position be disallowed because it will result in a duplication of functions:

It is obvious that a duplication of Application Support functions exist in each major functional area. The new Application Support Manager position will not replace the existing functional area application support resources. The ratepayers will have to bear unnecessary rate burdens because of GSWC having functions duplicated at the centralized and decentralized levels. (Ex. 23, p. 2-12.)

In his rebuttal testimony, Dickson denies that the new position will result in any duplication, n36 and he recites verbatim the list of benefits for the position set forth in Darney-Lane's testimony. (Ex 11, p. 54.)

n36 On this issue, Dickson states:

The DRA assumes that this position will be separated from the application support resources, which reside in the functional areas. This is not the case. The Application Support Manager will manage all of the existing technical support personnel. While the technical support personnel of the functional areas' applications will be moved under the centralized Applications Support Department, the operations and administration personnel of the functional areas' applications will remain in their current department. So, functional resources will not be duplicated, as the DRA suggests. (Ex. 11, p. 54.)

[*133]

6.2.11.2. Discussion

Although GSWC has not made as strong a case for this new position as for several of the others involving information technology, we have decided to approve it nonetheless. It seems reasonable that GSWC may realize benefits and efficiencies from having overall direction of its choice of software applications, and - according to both Darney-Lane and Dickson - that is what this position is intended to provide.

In another portion of Dickson's rebuttal testimony - where he defends positions that GSWC contends were approved in A.02-11-007, but which DRA is now challenging on the ground that no detailed justification was provided - Dickson notes that "currently, GSWC does not have an Applications Support Manager," and that the only position currently dealing directly with this function in the company is the Senior Applications Support Analyst. (*Id.* at 81.) Dickson describes that person's duties as follows:

The Senior Support Applications Support Analyst is responsible for assisting in the analysis, design, development, test and/or implementation of new or revised programs in conjunction with application vendors and department users to meet and support *the* [*134] *needs of a segment of the company.* (*Id.*; emphasis added.)

As noted in testimony of both Dickson and Darney-Lane on this position, one of the principal functions of the new manager will be to provide consistency in software selection *among* GSWC's various departments and functions. We think it is likely enough that efficiencies will result from this consistency that we are willing to approve the position. However, in the company's next general office GRC, we will expect GSWC to present credible evidence that such efficiencies have, in fact, been realized.

6.2.12. Corporate Communications Manager and Communications, Media and Technical Generalist

GSWC is seeking authorization for two positions related to corporate communications. The first is a Corporate Communications Manager, who would receive a salary of \$ 103,417 per year. The second is a Communications, Media and Technical Generalist, who would receive an annual salary of \$ 65,000 per year.

6.2.12.1. Positions of the Parties

The descriptions offered by GSWC of the two positions are quite similar, and the company has not explained very clearly how the duties of the Manager and the Generalist would differ. It appears, [*135] however, that the Generalist's emphasis would be on communicating with customers, whereas the Manager would be more responsible for formulating strategies to communicate better with all of GSWC's constituencies, including regulatory agencies and shareholders.

In their respective prepared testimony, Darney-Lane and Dickson offer the following identical descriptions n37 of the Generalist's duties:

Informing customers on a regular basis about the water they consume is a very important part of earning and building a customer's trust. Educating customers on an ongoing basis about their water supply, rules, regulations, and Company operations that may affect the cost they might pay is even more important. Effectively delivering this information to the customer helps them better understand the quality and cost of providing such a service. Conversely, the Company gains a better understanding of the diversity of the

customer and their values. This important exchange of information will help develop and establish which means of communication best fit our customers. (Ex. 5, Darney-Lane, p. 27; Ex. 11, p. 58.)

n37 It appears that apart from introductory sentences, Dickson's "rebuttal" testimony on both the Manager's and the Generalist's position is identical to the direct testimony of Darney-Lane on these positions. (Compare Ex. 5, Darney-Lane, pp. 27-28, 39-41 with Ex. 11, pp. 57-59, 60-63.)

[*136]

Darney-Lane and Dickson also both note that up to now GSWC has not had a Corporate Communications Manager, and then emphasize that the company needs one so it can explore new methods of communicating more effectively with customers and other constituencies. They suggest, for example, that bill inserts are of doubtful effectiveness because of the negative connotations inserts carry when they arrive with a bill. (Ex. 5, Darney-Lane at 39; Ex. 11 at 61.) After noting that the most appropriate forms of communication may differ depending on whether GSWC is reporting financial results or telling customers about planned repairs or water conservation, Darney-Lane and Dickson continue:

How this [varying] information is communicated is very important. The Company believes in utilizing all methods of communication that are both effective and efficient that also benefit the customers. The Company is interested in methods of communication that help build, strengthen and maintain effective communication. In the past, the Company used traditional communication sources such as individual mailers, newsprint, and spots on radio and television. The Company could not be sure if these traditional [*137] methods were effectively reaching, let alone educating or benefiting[,] our customers. Newer, more specialized methods of communication should be assessed. (Ex. 5, Darney-Lane at 40; Ex. 11 at 61-62.)

In his report for DRA, Aslam argues that neither the Generalist's nor the Manager's position is needed. With respect to the Manager position, Aslam notes that the company already has a CEO, two senior vice presidents, a chief financial officer and two vice presidents, whose total salaries approach \$ 1.4 million. n38 He continues:

In addition, GSWC makes use of every possible method of communication, from simple mail inserts to hi-tech, web-based broadcasts. It is difficult to understand how despite these levels of management and communications capabilities, the GSWC is failing to communicate its objectives, goals, and visions to employees, customers and shareholders. (Ex. 23, p. 2-26.)

n38 Aslam's list of corporate officers is not consistent with the one set forth in the 2006 annual report of American States Water Company, the corporate parent of GSWC. That annual report lists the following officer positions for GSWC: President and CEO; Chief Financial Officer, Senior Vice President, Corporate Secretary and Treasurer; Senior Vice President; Senior Vice President of Operations; Senior Vice President of Administrative Services; Vice Presidents of Customer Service for Regions I, II and III; Vice President, Treasurer and Assistant Secretary; Vice President of Water Quality; and Vice President of Regulatory Affairs.

[*138]

With respect to the Generalist, Aslam argues that the company is already so well-staffed with managers who know how to deal with customers that it does not need one:

Presently, GSWC is adequately staffed in the areas of Water Quality and Customer Service, the two areas that bear directly on both GSWC and its customers. The existing Customer Service Manager could

easily perform the functions of the new position with the occasional help of GSWC's Water Quality resource [including the Water Quality Vice President.] These executives should get involved with corporate communications and conduct public outreach with their customers as a requirement [of] their job function." (*Id.* at 2-18.)

6.2.12.2. Discussion

Of all the new positions GSWC is seeking for its general office, it has done the worst job of justifying these two. As noted above, the direct and rebuttal testimony in favor of the two positions is essentially identical, and the company's justifications as quoted above are almost a parody of a corporate communications manual. testimony in favor of the two positions is essentially identical, and the company's justifications as quoted above are almost a parody of a corporate [*139] communications manual.

However, we think GSWC has made one valid point, which appears in virtually identical form in the direct and rebuttal testimony for both positions. Dickson makes that point as follows with respect to the Generalist position:

Currently, GSWC does not have an employee that is dedicated to this particular job. There are daily situations where a specialized individual in this position would benefit both the Company and the customers. In the past, GSWC has encountered high-profile media situations where an experienced employee in media communications would have greatly helped communications with both the customers and the Company. Informing customers and community leaders about water conservation, low-income programs, and the benefits of proposed capital improvements within their customer service area would be beneficial to all. (Ex. 11, p. 58.)

We agree that having a "Generalist" with broad media experience is likely to pay benefits for both GSWC and its customers, and we do not agree with DRA that adding media responsibilities to the job duties of the customer service and water quality staffs will be sufficient. Thus, we will authorize the Generalist position. [*140]

However, GSWC has clearly not met its burden of proof with respect to the proposed Corporate Communications Manager. It is hard to disagree with DRA's Aslam when he states that in view of the number of GSWC's officers and the many different modes of communications it uses, "it is difficult to understand how . . . GSWC is failing to communicate its objectives, goals, and visions to employees, customers and shareholders." (Ex. 23, p. 2-26.) We suspect the main reason GSWC is seeking the Manager position in addition to the Generalist is that it fears no one below the rank of manager will be taken seriously when he or she offers media advice.

6.2.13. DRA's Attack on the Employee Development University (EDU) and GSWC's Request for Three More EDU Positions

6.2.13.1. Background

Since the mid-1990s, GSWC has maintained an operation within its Human Resources Department that was originally known as the Employee Development Program (EDP) and is now called the EDU. The program grew out of an audit of GSWC's predecessor, SCWC, that was conducted by the Barrington-Wellesley Group, Inc. (BWG) in late 1992. n39 The audit identified employee training as one of the weaknesses in SCWC's management, [*141] and noted that the company had recently hired a Manager of Employee Development and Training (who reported to the Vice President - Administration) to begin rectifying the situation. (Ex. 11, pp. 63-64.)

n39 The Commission has also used the Services of BWG from time to time. See Administrative Law Judge's Ruling Denying Motion of Pacific Gas and Electric Company to Compel Discovery Responses from the California Public Utilities Commission and the Barrington Wellesley Group, Inc., issued March 20, 2001 in A.00-11-038 et al.

In its first GRC following the audit, A.94-06-015, SCWC requested funding for a "comprehensive [EDP] to include personnel salaries, capital costs, and operating expenses needed for effective employee training and development." (*Id.* at 64.) DRA supported the request, finding that the EDP proposal - which relied on in-house training supplemented by some outside training - was a reasonable training program for the utility to undertake. (*Id.* at 65.)

Today, the EDU is accredited and - according [*142] to the executive summary from a 2001 follow-up to the BWG audit included in Dickson's rebuttal testimony - "is well-regarded both within the Company and within the industry." (Ex. 5 to Ex. 11, p. I-2.)

6.2.13.2. DRA's Position on the Value of the EDU

Although it has supported funding for EDU in the past, DRA is not doing so in this application. Not only is DRA opposing GSWC's request for three new EDU positions (an issue we discuss below); DRA is also urging that EDU should be "dissolved" and that two of its employees (the Dean and the Senior Employee Development Specialist) should be moved to the company's Human Resources Department. Noting that GSWC is "the only Class-A water utility in the State of California that has an in-house university," DRA witness Aslam continues:

After carefully analyzing the functionality and claimed benefits of the EDU, DRA finds the EDU in-house training functions are not a core competency of the utility. It is more economical and more efficient to leave such employee training to professional organizations whose core competency is to educate and train a workforce. (Ex. 23, p. 2-13.)

The first reason for DRA's opposition is that, according to [*143] Aslam, a cost-benefit analysis of the EDU demonstrates it is not cost-effective. Aslam summarizes his assessment of the cost-benefit analysis as follows:

In this proceeding, DRA requested GSWC to provide a cost/benefit analysis for its in-house [EDU.] The company responded with a study that considered the last ten years of EDU expenses and capital expenditures but which only showed a savings of merely \$ 94,550 over the past ten years.

However, once DRA analyzed certain cost estimations that GSWC used, it became evident that there were no savings at all. For example, GSWC estimated that for its Customer Service Related training the cost will be \$ 53.06 per hour, whereas DRA believes that after an adjustment of traveling cost the more appropriate cost will be \$ 23.70 per hour. Similarly, GSWC estimated its Management Development and Safety related training costs at \$ 124.69 and \$ 33.78 per hour respectively. However, DRA believe[s] that by becoming a long term partner with the training provider GSWC could make use of membership discounts that would reduce the training costs to \$ 111.88 and \$ 24.75 respectively. These minor changes in the cost estimations resulted in an actual [*144] loss over the last ten years for GSWC's in-house EDU operations. (*Id.* at 2-15.)

Aslam continues that the size of the loss arising from the EDU can be calculated at nearly \$ 4.5 million over the past decade if one takes into account "the value of other existing training programs that run parallel and in addition to" the EDU programs. (*Id.*) Aslam provides the following list of what he considers these other training programs:

Management Initiatives, Succession and Training Cost n40

Corporate membership for the American Water Works Association (AWWA)

Employees membership for AWWA

Corporate membership in the AWWA Research Foundation

Outside consulting

n40 With respect to this item, Aslam asserts that GSWC "currently incurs on average an expense of \$ 318,723 per year under [this program.] This training is above and beyond the Management Development training that

EDU provides in-house. Therefore, ratepayers have to bear the burdens of this duplication of efforts." (*Id.* at 2-16.)

Instead of maintaining [*145] its own costly EDU, Aslam argues that GSWC should rely on the numerous training resources available through the AWWA. Aslam summarizes these resources as follows:

The AWWA, an international non-profit scientific and educational society, is the authoritative resource of training, information, and advocacy to improve the quality and supply of water in North America and beyond. The largest organization of water professionals in the world[,] the AWWA also advances public health, safety, and welfare by coordinating the efforts of the entire water community. This organization also offers a wide range of training on distribution systems, water production and treatment. (*Id.* at 2-16.)

After noting that GSWC spends \$ 22,817 for its corporate membership in the AWWA and another \$ 45,000 for its membership in the AWWA Research Foundation (which provides its members with numerous peer-reviewed papers and reports), Aslam concludes:

It is quite evident that no water utility on its own can develop the extensive water expertise that is available from AWWA. GSWC should focus its limited resources on its core competency, water production and distribution. The task of training should be [*146] left to such professional organizations as the AWWA, which can provide the needed water training more efficiently and cost effectively. (*Id.* at 2-17.)

6.2.13.3. GSWC's Position on the Value of the EDU

In his rebuttal testimony, Dickson strongly disagrees with Aslam's assessment and devotes 12 pages to refuting it. He asserts that Aslam has misunderstood or misstated the facts on virtually every important point concerning the EDU.

As to the argument that GSWC is somehow deficient because it is the only Class A water company in California to operate its own in-house training program, Dickson responds:

Mr. Aslam suggests that GSWC . . . do as other Class A water companies do, but has provided no analysis on what the other companies are doing. He does not show they are more cost effective or offer better training. For all he knows, they may be spending much more than GSWC and he highly inefficient in comparison. (Ex. 11, p. 67.)

Dickson also notes that GSWC decided to establish its own in-house training program rather than rely on outside vendors because in-house training could be more rapid and better-tailored to the needs of the company:

Our Company's management [*147] supported a centralized process for employee development and learning and further believed in staffing the department with skilled personnel who are certificated in water operations, customer service, instructional design, information technology and training background. In so doing, staff can design training programs that are closely linked to our business to benefit both the customers and the Company.

In general terms, the main benefit of centralized learning is the cost savings that result from standardization, central reporting and record keeping and quality control. The advantages of such a system include:

Reduction in number of individual systems required to handle corporate learning.

Immediate population of the central database with course completions and certifications.

Promotion of standardization via reduction in the number of duplicate courses.

Significant cost savings through reduction in number of administrators.

Standardization of content, certifications and competencies.

Ability to easily align employee objectives with corporate objectives.

Simplified reporting (from one system versus many).

Accuracy in reporting (from one system versus many)." ([*148] *Id.* at 67.)

Dickson particularly attacks Aslam's conclusion that the per-hour training costs reported by GSWC could be reduced significantly by using outside vendors. On this question, Dickson states that EDU's total training costs are comprised of four elements, of which Aslam considered only the second:

Mr. Aslam simply made bad assumptions from the data provided to him. The cost of training of \$ 53.06, \$ 124.69, and \$ 33.78 per hour is the total rolled in cost of all training functions performed by EDU[,] not just the in class portion of the training. The four training functions performed by EDU are as follows:

1. Training and Development Needs Assessment: EDU works with management, strategic and business plans, employee development plans and individual intake with employees to assess business and/or career training needs. EDU also uses tools such as surveys, post training evaluations, and others to assess training needs.

2. Training and Development activities: After assessing business needs, EDU then develops (if needed) and provides training courses, workshops, and other activities to meet the business training needs.

3. Application of Training (follow [*149] up): Following training events, EDU staff work with employees to help ensure that the training is being applied in the workplace and that the business needs identified during the assessment stage are being satisfied. EDU staff work with employees and travel to the various work locations in the Company, meet with employees and supervisors and provide individualized coaching where needed.

4. Evaluation of Training: EDU performs evaluation through all stages of the training process to focus on what is working and what is effective in meeting the business training needs of the Company. Evaluation is performed on various levels including:

. Employee reaction - how did they feel about the training [based upon an evaluation form]? . . .

. Learning - did they get it? Measured by pre and post training assessments/exams . . .

. Application - can they do it, use it in their work? ..

. Business Results - was it worth the effort? - look at cost savings, improved performance in the workplace, etc." (*Id.* at 71-72.)

After faulting Aslam for considering only the second of the four cost elements in EDU training, Dickson also points out that very few outside vendors offer [*150] more than one or two courses that would meet GSWC's needs, and that the cost of membership in organizations offering such courses would often exceed any savings that might be realized. In addition, Dickson asserts that greater use of outside vendors would significantly increase travel costs. (*Id.* at 73.)

Dickson then takes aim at Aslam's assertion that when other training programs "that run parallel and in addition to in-house EDU training" are taken into account, the loss during the past decade from maintaining the EDU program approaches \$ 4.5 million. On this issue, Dickson states:

This [assertion] reflects a great deal of misunderstanding by Mr. Aslam. The DRA [claims] that there were duplications of training costs due to requesting data in multiple formats. DRA incorrectly assumed that the \$ 4,481,456 for the items below was a duplicate of EDU training costs:

Management Initiatives, Succession and Training Cost - \$ 3,187,356; DRA incorrectly assumed that this training is a duplication of other programs offered by EDU. This cost is for strategic management consulting and assessments provided directly to the executive leadership of the organization.

Corporate Memberships [*151] for AWWA \$ 149,248

Employees Memberships for AWWA \$ 88,920

Corporate Membership in the AWWA Research Foundation \$ 450,000

Outside Consulting \$ 49,230

Not only is [it] inappropriate and incorrect to apply these costs to the EDU costs over ten years - these costs would be incurred regardless of having EDU and it is significantly misleading to characterize them as training costs in a comparison to the training costs of outside programs.

All the costs included in the \$ 4,481,456 figure above are outside of the function and Services provided by EDU over the ten year historical experience of EDU with the exception of approximately \$ 121,000. (*Id.* at 74.)

Finally, Dickson takes issue with Aslam's assertion that GSWC incurs an average annual expense of \$ 318,723 under its Management Initiatives, Succession and Training (MIS&T) programs, and that these programs duplicate similar courses offered by the EDU:

This [assertion] is untrue and a mischaracterization of the information provided to Mr. Aslam. EDU does succession training programs for rank and file employees in order to have qualified entry level supervision within the Company. The Company conducts separate succession [*152] planning and training for executive management independent of EDU's activities; customers are not charged twice for the same function. (*Id.* at 75.)

6.2.13.4. Discussion of the Value of the EDU

Although supplementary testimony by DRA might have cleared up some of its differences with GSWC, we are sufficiently convinced of the value of the EDU - and of its cost-effectiveness - that we will reject Mr. Aslam's proposal to dissolve the program as it currently exists and transfer EDU's Dean and Senior Employee Development Specialist to GSWC's Human Resources Department.

Based on the record before us, we agree with Dickson that DRA has failed to show EDU is not cost-effective. n41 Aslam concedes that using the data provided by GSWC for EDU's expenses and capital expenditures over the past 10 years, there was a savings during that period of \$ 94,550 over the costs of outside training. (Ex. 23, p. 2-15.) The basis for Aslam's claim of a \$ 4.5 million loss over the 10-year period is his contention that GSWC is not making efficient use of the money it spends for outside consulting and various memberships in AWWA, which - according to Aslam - offers training that frequently duplicates [*153] what is available through the EDU. (*Id.* at 2-15 to 2-16.)

n41 In its August 13, 2007 opening comments on the PD, DRA asserts that this language reflects legal error because it reverses the burden of proof in water rate cases. According to DRA, the Rate Case Plan appended to D.04-06-018 makes clear that water utilities like GSWC have the burden of proof when requesting a rate increase, and that if this requirement is to be given any meaning here, we must deny GSWC's requests for EDU

funding "because their support rests for the most part on vague and unsupported generalizations in GSWC's rebuttal." (DRA Opening Comments, p. 13.)

DRA's argument is without merit, because it confuses the burden of proof with the burden of going forward with evidence, and also ignores the procedural context of this case. As our discussion in the text makes clear at several points, we are well aware that water utility companies bear the burden of proof when requesting a rate increase. However, our decisions also recognize that there is an important distinction between which party in a rate case has the ultimate burden of proof and which party has the burden of producing evidence once a prima facie showing on an issue has been made. *Re Pacific Bell*, D.87-12-067, explained the distinction as follows:

[W]here other parties propose a result different from that asserted by the utility, they have the burden of going forward to produce evidence, distinct from the ultimate burden of proof. The burden of going forward to produce evidence relates to raising a reasonable doubt as to the utility's position and presenting evidence explaining the counterpoint position. Where this counterpoint causes the Commission to entertain a reasonable doubt regarding the utility's position, and the utility does not overcome this doubt, the utility has not met its ultimate burden of proof. (27 CPUC2d 1, 22.)

See also *Universal Studios, Inc. v. Southern California Edison Company*, D.04-04-074, fn. 13, *mimeo.* at 31-32 (where defendant raises a new issue in its direct testimony, complainant has the burden of going forward with evidence concerning the new issue either in rebuttal testimony or on cross-examination.)

In this case, although DRA apparently propounded data requests to GSWC about the EDU expenses and positions the utility had requested, it did not become clear that DRA would be challenging the efficacy of the entire EDU program until DRA submitted its general office report on May 25, 2006. In that report, five pages were devoted to attacking the cost-effectiveness of the EDU. (Ex. 23, pages 2-13 to 2-18.) In view of this substantial attack on a program DRA had previously supported, GSWC had little choice but to devote a substantial portion of its rebuttal testimony to countering DRA's arguments. In his rebuttal testimony, Mr. Dickson did so. (Ex. 11, pp. 63-75.)

Given this procedural posture, the burden of going forward with evidence to rebut Mr. Dickson's arguments clearly rested on DRA. DRA had to choose between meeting this burden by requesting an opportunity to submit surrebuttal testimony, or by cross-examining Mr. Dickson on his rebuttal testimony. Although DRA apparently chose the latter course, little of its cross-examination of Dickson was devoted to the EDU.

The cited pages of Exhibit 23, Dickson's rebuttal, and the parties' briefs comprise the entire record on which the PD had to decide the cost-effectiveness issue. The PD found the arguments presented by Mr. Dickson in support of the EDU more persuasive than those presented by DRA attacking the EDU's cost-effectiveness. Under these circumstances, GSWC met its burden of proof concerning the EDU's cost-effectiveness, and there was no legal error in how the PD handled the matter.

[*154]

Dickson has convincingly argued that the \$ 4.5 million figure is incorrect, and that Aslam has mixed apples and oranges in order to reach it. First, Dickson is credible when he argues that the MIS&T costs of approximately \$ 319,000 per year that GSWC incurs to train its senior management are separate and distinct from the Management Development costs EDU incurs to train qualified entry-level supervisors for the company. (Ex. 11, p. 75.) These MIS&T costs make up over 70% of the alleged \$ 4.5 million loss. (Ex. 23, p. 2-15.)

Second, Dickson is credible when he states that because of GSWC's size and geographic diversity, it would have to incur substantial AWWA costs whether the EDU program existed or not.

Third, we find credible Dickson's argument that Aslam has taken into account only the dollar costs of developing and presenting EDU classes, and has left out of his analysis the presumably significant costs that must be incurred in making needs assessments, following up to be sure that training is properly applied, and evaluating whether particular

training is effective. (Ex. 11, pp. 71-72.) Aslam does not deny that these other steps are part of an adequate training program, yet his [*155] analysis apparently made no attempt to quantify them.

Fourth, we are persuaded by Dickson's argument that turning to outside vendors for GSWC's training needs would not be a very cost-effective option. As Dickson points out, while certain vendors offer some of the courses the company needs, there is no single vendor (or even, apparently, a small group of vendors) which offers all of them. Moreover, if more outside vendors were used for training, it does seem likely that travel costs would increase significantly.

Finally, we agree with GSWC that it is doubtful any outside vendor would be flexible enough to deal with some of the special personnel issues the company faces. Dickson provided one example of such an issue when, in referring to the non-quantifiable benefits of having an EDU, he described the program's special efforts to help a large number of GSWC operators obtain up-to-date certification:

EDU provided a narrative explanation of cost avoidance by its efforts in helping 68 . . . GSWC operators pass the required DHS exams to obtain certification required to keep their jobs and keep the Company from having to replace a large portion of its work force by importing certified [*156] personnel from elsewhere . . . More specifically, much of the Company's service area in Region 2 (with the highest concentration in customers throughout the entire Company) is located in economically disadvantaged inner city neighborhoods. It is the Company's policy to hire from the residents in these areas if at all possible. This policy is consistent with and complimentary to the various diversity initiatives championed by the CPUC. We have found that many . . . employees hired from these areas are readily trainable in the physical water system operations needed to professionally operate a potable water system. However, we also find that many of them are deficient in certain academic skills such as technical writing and basic mathematics needed to pass classroom testing required by the certification requirements. *It is difficult for GSWC to find outside training in these basic academic areas. EDU has developed in house programs to meet these basic needs [that are] unique . . . to GSWC.* (Ex.11 at 70; emphasis supplied.)

In a June 2006 letter to Dickson from the lead consultant on the audit that BWG conducted in 1992, the consultant wrote:

Achieving a culture shift, which [*157] we strongly believed [in the audit] was essential for the future of the Company, required a strong approach. We believed that, at least for a period of time, in-house training was an essential competency necessary within the Company. (Ex. 5 to Ex. 11, p. 2.)

It seems clear from the longevity and growth of the EDU that GSWC continues to find benefits from having a significant in-house training program. DRA has failed to demonstrate that the program is not cost-effective, and it seems clear from the discussion above that the program pays benefits that are significant but sometimes difficult to quantify. Accordingly, we reject DRA's recommendation to dissolve the EDU and transfer its Dean and Senior Employee Development Specialist to the company's Human Resources Department.

6.2.14. New EDU Positions Requested by GSWC

As noted above, DRA's broad attack on justification for having an EDU was originally occasioned by the company's request for three new EDU positions. Dickson does not discuss these positions in his rebuttal testimony, but Darney-Lane set forth a description of the positions and the rationale for them in her direct testimony.

The first position is EDU Facilitator-Instructor, [*158] at an annual salary of \$ 80,001. After noting that few young people at job fairs express any interest in going into utility work, Darney-Lane states:

[T]o attract new workers to water utility operations in order to meet the looming crisis of the water operators worker shortage, it is incumbent upon water operations management personnel to come up with alternatives. [The EDU] is taking a proactive approach by adding to the current EDU team a technical instructor and administrator position equipped with skills in engineering, management, teaching, curriculum design and development, water and waste water, environmental, health and safety. This position will focus on continuing education and training in the technical areas of water operations and management to prepare next-generation upgrades of skilled water operations personnel. (Ex. 5, p. 28.)

The second new EDU position is that of Support Analyst, at an annual salary of \$ 54,241. Darney Lane argues that this position is needed to keep up with the significantly-increased workload of maintaining EDU's data base:

Since the [EDU's] inception in 1992, the department has expanded its administrative activities, to include, managing [*159] a comprehensive database with employee information for mandated safety, annual training activities, tuition reimbursement program, outside vendor training, and most recently, employees' operations certification records for the California [DHS]. In addition, the database is expanded to include training information for [the] Sarbanes-Oxley Act, Security, and Standard Emergency Management Systems. Currently, one staff is assigned 25-percent time to manage the database[,] and the rest of this individual's time is dedicated to other training activities. With the increased workload on the database activities for this staff, much time is spent to maintain the integrity of employees' records[,] resulting in other work duties being deferred to other staff members, thereby stretching staff resources. The person in the Support Analyst position will help to address the workload and allow the rest of the EDU team to spend more time training and coaching frontline employees. Approximately 50% of this position's job function is related to compliance with Sarbanes-Oxley requirements. (*Id.* at 25.)

The third EDU position is that of Senior Employee Development Specialist. [*160] This is already a half-time position, with the other half of the employee's time being devoted to duties in GSWC's Region I. Darney-Lane presents the following justification for making this job a full-time EDU position:

The current responsibilities of [the] American Council on Education (ACE) and the International Association for Continuing Education and Training (IACET) are shared by two staff members who also have responsibilities for mandated safety, emergency management and security, Sarbanes-Oxley, customer service, personal computer, diversity and other compliance training. The expansion of this position from 50-percent to 100-percent will ease the extra hours of current staff and allow one full-time staff to organize, plan and administrate all IACET and ACE records and launch more training authorized through these agencies. All of this position's job functions relate to compliance with the Sarbanes-Oxley act. This will benefit our water operations employees since the [DHS] approved IACET courses for continuing education credits. Also, the fulltime position will allow the staff to allocate more time to develop our current water operators with the looming operators' shortage [*161] in the industry. (*Id.* at 26.)

In his report for DRA, Aslam does not directly take issue with the justifications offered, for these positions. He simply notes that if DRA's recommendation to dissolve the EDU is accepted, the requests for a Facilitator-Instructor and Support Analyst will be rendered moot, and that the Senior Employee Development Specialist should be accounted for in Region I headquarters expenses. (Ex. 23 at 2-17 to 2-18.)

6.2.14.1. Discussion of the Requested New EDU Positions

Although we think GSWC has presented an adequate justification for the Facilitator-Instructor job and the most of the duties of the Support Analyst, we do not think the company has demonstrated how its need to comply with SOX can justify half of the Support Analyst position and all of the Senior Employee Development Specialist's position, as Darney-Lane contends. Although the changes to accounting practices that GSWC has had to make as a result of SOX presumably include some tightening up of how it reports dealings with outside vendors and other training expenses, the description in Darney-Lane's testimony of how these jobs are tied to SOX requirements is [*162] too vague to be persuasive.

Accordingly, even though the Senior Employee Development Specialist position already exists within the company, we will not authorize GSWC to recover half of that job's costs as a general office expense. Instead, the company should present a full justification for its contention that this job is needed due to SOX requirements in GSWC's next general office GRC.

6.2.15. Associate Rate Analyst

In her direct testimony, Darney-Lane notes that due to a retirement and other changes in 2004, GSWC reassessed the needs of and reorganized its Regulatory Affairs Department. Whereas the department had previously had a vice president, three managers and five regulatory analysts, after the 2004 reorganization the department has a vice president, one manager, a senior regulatory supervisor, a senior regulatory specialist, and two associate regulatory analysts (the

last being an entry-level position). In the reorganization, duties performed by some of the managers were reassigned to more junior employees. (Ex. 5, Darney-Lane, pp. 36-38.)

Darney-Lane notes that while the 2004 reorganization increased the size of the Regulatory Affairs Department by one, "the overall labor [*163] expense of the new organization is less than the expense of the currently approved organization." (*Id.* at 38.)

6.2.15.1. Positions of the Parties

The position for which approval is sought here is one of the two associate regulatory analyst positions. Darney-Lane argues that this position is needed principally because of the new filing requirements under the Rate Case Plan:

It was felt that the department was short staffed at the analyst level. Under the new rate case plan, GSWC is required to file a GRC application every January. In addition, under the new rate case plan, water utilities are required to prepare their rate case filings in a shorter period of time and are also required to provide much more information at the time of the filing than was previously required. An additional analyst is required by the Company to work on the rate case team. (*Id.* at 37-38.)

In his report for DRA, Aslam opposes this position on the ground that it cannot be justified merely because the 2004 reorganization slightly decreased the payroll for the Regulatory Affairs Department. Noting that companies like GSWC typically hire [*164] outside consultants to help them prepare rate case filings, and that many people within the company besides those in the Regulatory Affairs Department help to prepare testimony, Aslam argues that GSWC's "current Regulatory Affairs Department is adequately staffed to handle a typical GRC and other regulatory workloads."

In his rebuttal testimony, Dickson points out that the Regulatory Affairs Department today is no larger than it was in 1996, although the workload certainly is. (Ex. 11, p. 60.)

6.2.15.2. Discussion

We will approve the regulatory analyst position that GSWC has requested. Although we recently amended the Rate Case Plan in D.07-05-062 to eliminate the annual GRC filings described by Darney-Lane, there is no doubt that with the increased requirements for information brought about by the Master Data Requests, future rate cases will be more labor intensive for GSWC and other Class A water companies than in the recent past. We also think it is clear from the deficiencies of proof in the company's showing in this rate case that GSWC needs to strengthen its Regulatory Affairs Department overall.

6.2.16. EPRP Coordinator

6.2.16.1. Positions of the Parties

GSWC argues [*165] that the new position of EPRP Coordinator at an annual salary of \$ 79,986 is necessary because of the passage of the Public Health and Bioterrorism Response (PHBR) Act signed by the President in 2002. In her direct testimony, Darney-Lane states:

The requirement for maintaining current Vulnerability Assessments from USEPA and the ongoing requirements to maintain Emergency Response Plans . . . make it critical that this position be maintained. As a Utility serving over one million people in over 40 separate water systems, each of which requires a separate plan, the task of maintaining these plans is an enormous responsibility. With the increasing requirements by state and federal agencies for water utilities to plan and prepare to respond to various emergencies, including natural disasters and as well as potential security or terrorist events in the United States, the Company has identified the need for a position to ensure we are able to do the following minimum activities:

Planning development and coordination of table top exercises as part of the Company's ongoing Emergency Preparedness and Response Plan.

Planning, development, and coordination for the implementation of [*166] water system security programs and related initiatives, in accordance with federal security requirements.

Preparation and maintenance of a comprehensive database on all existing and proposed Federal and State Security Laws, Programs and initiatives that could impact ASWC.

Working with both state and local agencies to ensure the Company's EPRP is in conformance with state standards." (Ex. 5, Darney-Lane, pp. 38-39.)

In his report for DRA, Aslam opposes the EPRP Coordinator position because he believes the job can be performed by the company's existing personnel. Aslam argues that "given the fact that GSWC already has completed the initial vulnerability assessment, the existing Safety Specialist with the help from the Regional Managers, who have first hand knowledge of their respective water systems, can perform the requirements imposed by the [PHBR] Act" (Ex. 23, pp. 2-24 to 2-25.)

6.2.16.2. Discussion

We will approve this new position. We find plausible Dickson's point that DRA's interpretation of the PHBR Act "does not take into account the need to ensure that the Emergency Response Plans . . . remain updated," which includes the need "to provide routine table top training [*167] sessions." (Ex. 11, pp. 59-60.) We are also persuaded by Dickson's points that (1) the Safety Specialist and Regional Managers on whom Aslam would rely "do not possess the time, expertise or capacity" to keep the EPRPs up-to-date, and (2) adopting DRA's position would "place[] the Company at regulatory risk from both the USEPA and DHS." (*Id.*)

6.3. A \$ 50,000 Penalty is Appropriate for GSWC's Failure to Disclose Until Rebuttal Testimony the Rationale for Requesting at Least Half of the 20 New General Office Positions

As noted in the introduction to this section of the decision, a significant controversy developed between GSWC and DRA on the propriety of the scope of the company's rebuttal testimony. DRA claimed it was "sandbagged" by GSWC's decision to serve the Dickson and Sprowls rebuttal testimony - which together totaled over 200 pages - barely two weeks before hearings were scheduled to begin on June 26, 2006. DRA also claimed it was prejudiced when GSWC served a very large volume of responses to DRA's data requests concerning the rebuttal testimony on June 24, just two days before hearings were to begin.

On June 28, 2006, DRA put these objections into concrete form and [*168] filed a motion to strike all of Dickson's rebuttal testimony and portions of the Sprowls rebuttal testimony. In addition to its claims of unfairness, DRA relied on language in D.04-03-039, where the Commission declined to include a \$ 5.4 million software expenditure in the rates for SCWC, GSWC's predecessor, because the company had not provided the basic justification for the expenditure in its direct testimony, and even after DRA noted the deficiencies in SCWC's direct testimony, the company failed to justify the expenditure.ⁿ⁴² In its motion to strike, DRA notes that because it did not receive GSWC's rebuttal testimony until June 9, 2006, DRA was forced to scramble to prepare for cross-examination. On June 16, DRA propounded approximately 92 data requests in connection with the rebuttal testimony. On June 23, GSWC provided partial responses by e-mail. The bulk of the responses came on Saturday, June 24, just two days before hearings were to begin, when GSWC delivered to Aslam's home over 1,000 pages and four CD-ROMs filled with data responses. (DRA Motion to Strike, p. 2.) Had GSWC met its burden by including the justifications for the 20 new positions in its direct testimony, [*169] DRA would have had ample time to review GSWC's data responses in advance of the hearing on these issues.

ⁿ⁴² D.04-03-039 provides in relevant part: "This issue has also raised a concern regarding SCWC's burden in justifying its request. With the application, SCWC submitted testimony, which included a very brief description of the need for this particular project. After ORA recommended the project be rejected for lack of justification, SCWC provided a more detailed justification in rebuttal testimony. A project of this magnitude, which is in excess of \$ 5 million, requires more attention than what was given by the utility in initially justifying its proposed budgets. Providing the basic justification in rebuttal is unfair, since parties are not generally given the opportunity to respond to rebuttal with testimony of their own. In this case, rebuttal was issued on May 1, 2003 and

hearings began on May 12, 2003. The timeframe to conduct discovery on rebuttal, even for the purpose of cross-examination, was limited. When the utility has the evidentiary burden, we caution against the use of rebuttal testimony to provide the basic justification. As a matter of fairness, we must seriously consider either striking such testimony or extending the proceeding, at the utility's risk, to allow for responsive testimony from the other parties." (D.04-03-039, *mimeo.* at 84-85; footnote omitted)

[*170]

GSWC filed a response to DRA's motion to strike at the end of the day on July 5, 2006. In its response, the company argued that the motion to strike should be denied because all of the Dickson and Sprowls testimony was proper rebuttal, in that it responded to contentions made by DRA's Aslam.

Normally, we would have tried to deal with GSWC's conduct by allowing DRA to submit surrebuttal testimony, if requested. However, the fact that GSWC's data responses were received only two days before hearings were scheduled to begin made surrebuttal testimony an impracticable option for DRA and the assigned ALJ, since both needed to prepare for the hearings, and since the submission of surrebuttal testimony would have significantly delayed the hearings beyond the starting date the parties had agreed upon at the May 2, 2006 PHC. The harm caused by GSWC was partially mitigated by deferring the cross examination of the rebuttal witnesses.

On July 7, 2006, assigned ALJ McKenzie issued his ruling on DRA's motion to strike. Although finding that GSWC's conduct had "not been exemplary," the ALJ also concluded that the company's actions did not appear to justify striking the large volume of rebuttal [*171] testimony that DRA had challenged. (AP Ruling Denying DRA Motion to Strike, *mimeo.* at 4.) First, the AP noted that while the justifications for the new general office positions set forth in Darney-Lane's direct testimony were "thin" in comparison with those offered by Dickson and Sprowls, they were "nonetheless sufficient to apprise Mr. Aslam of the basis for the company's request." (*Id.*) Second, the AP observed that the rebuttal testimony had to be prepared very hastily, which likely contributed to its length. (*Id.*) Third, since Aslam acknowledged some familiarity with SOX, the ALJ concluded that DRA's claims of prejudice in connection with the Sprowls rebuttal testimony - which dealt largely with SOX and its implications for GSWC - were exaggerated. (*Id.* at 5.) Finally, the AP noted that the cross-examination of Dickson and Sprowls had been deferred for several days, which appeared to lessen the prejudice to DRA. (*Id.*)

In view of all these factors, the ALJ concluded that he should deny the motion to strike and follow the Commission's "preferred practice" of "admit[ting] the testimony into the record, but then . . . afford[ing] it only so [*172] much weight as the presiding officer considers appropriate." (*Id.* at 2.) While we do not quarrel with the decision of the AP not to strike the rebuttal testimony of Dickson and Sprowls, a decision the AU had to make quickly and appears to have reached with some reluctance, we find it necessary to examine whether we should take further action against GSWC for its conduct on this issue.

In reviewing the record, we find several facts concerning GSWC's conduct troubling. For example, with hearings set to begin on a wide range of issues in less than 48 hours, no attorney or staff member could reasonably be expected to digest the volume of data responses described in DRA's motion, or to work what was learned from these responses into the proposed cross-examination with any comfort. GSWC's conduct is particularly problematic, because at the very least, D.04-03-039 put it on notice that this type of deficiency is unacceptable. We warned SCWC in D.04-03-039 that it had the burden of justifying its case in direct testimony:

Providing the basic justification in rebuttal is unfair, since parties are not generally given the opportunity to respond to rebuttal [*173] with testimony of their own . . . When the utility has the evidentiary burden, we caution against the use of rebuttal testimony to provide the basic justification. As a matter of fairness, we must seriously consider either striking such testimony or extending the proceeding, at the utility's risk, to allow for responsive testimony from the other parties." (D.04-03-039, *mimeo.* at 84-85; footnote omitted.)

Moreover, GSWC should have been aware of the Commission's concern about DRA's claim that the company's ratepayers were being asked to subsidize the activities of ASUS, GSWC's non-regulated affiliate. (D.04-03-039, *mimeo.* at 26-30.) In view of this interest, statements such as Mr. Dickson's that GSWC was seeking to include in rates only 69% of the salary for the proposed new Call Center Support Analyst, and that the rest of this position's salary was allocated to "new business" for ASUS, should have been given more prominence in the company's direct testimony. n43 (Ex. 11,

p. 53.) If it had, DRA might have been able to conduct discovery that would have enabled it to arrive at a better method for allocating call center costs between GSWC and ASUS. (See Ex. 23, pp. 4-2 to 4-3; [*174] DRA Opening Brief, pp. 10-11, 13; Ex. 45.)

n43 In its August 13, 2007 opening comments, GSWC points out that, contrary to the assertion in the PD and alternate PD, a statement that 31% of the salary for the new Call Center Support Analyst position was being charged to ASUS did appear in the company's direct testimony. The statement was reflected in Ms. Darney-Lane's comment that 31% of the new position's salary was being "directly charged to non-regulated cost centers." (GSWC Opening Comments, p. 11; Ex. 5; Darney-Lane, p. 5.)

While we acknowledge that this reference to charging a portion of the new analyst's salary to ASUS did appear in GSWC's direct testimony, it should be noted that the statement was easy to miss. Moreover, the statement concerning the 31% appeared in an introductory discussion by Ms. Darney-Lane of the general methodology she had used to forecast labor expense for the company's Region II and general office operations. No mention of the 31% was made in the actual discussion of the Call Center Support Analyst position, which was very brief. (See, Ex. 5, Darney-Lane, p. 23.) Of note: the data requests attached to GSWC's August 20, 2007 reply comments are associated with GSWC's rebuttal testimony.

[*175]

GSWC's conduct is revealing when one bears in mind that in a general rate case, the burden of proof is on the utility to justify any rate increase. As this Commission stated in denying rate relief less than a decade ago to SCWC for the costs of participating in a project:

A fundamental principle involving public utilities and their regulation by governmental authority is that the burden rests heavily upon a utility to prove that it is entitled to rate relief and not upon the Commission, the Commission staff, or any interested party, or protestant to prove the contrary." (D.99-04-060, 86 CPUC2d 54, 62, quoting Suburban Water Co., 60 CPUC 183, 200 (1962) (; emphasis added).)

Other decisions from this Commission and the Federal Energy Regulatory Commission (FERC) recognize that a corollary of this rule is that a party must place the full justification for a proposal in its written direct testimony, and may not wait until rebuttal to do so. n44 For example, in a ruling striking rebuttal testimony on vertical competition issues offered by Southern California Edison Company (Edison) in the FERC proceeding that considered the proposed [*176] merger between Edison and San Diego Gas & Electric Company, the FERC ALJ said:

"[A]pplicants are required to present all the proof which they intend to offer in support of the issues on which they have the burden of proof and the initial burden of going forward . . . Applicants are not at liberty to hold back affirmative proof at this stage in order to introduce it at a later stage of the trial, and the applicant indulging in such practice must suffer the consequence of this action." (*Southern California Edison Company and San Diego Gas and Electric Company*, FERC Docket No. EC89-5-000, 50 FERC P 63,012, p. 65,065) n45

n44 In D.04-07-022, in commenting upon Edison's failure to include certain capital additions to a Customer Service Business Unit project in its direct testimony, we said:

The Commission has held that it is not permissible for utilities to hold back on the presentation of salient information until the submission of rebuttal testimony. We would be well within our rights

and responsibilities if we were to disallow these capital additions on procedural grounds as advocated by ORA. (Mimeo. at 157.)

However, the capital additions were not disallowed in D.04-07-022 because the Commission expressly found that Edison's failure to include them in its direct showing was inadvertent, and not part of a litigation strategy. (*Id.* at 156-57, 335.)

See also, Pacific Gas and Electric Company, D.87-03-034, 24 CPUC2d 45, 1987 Cal. PUC LEXIS 544 (denying PG&E's petition for modification where the utility alleged that accelerated tax depreciation it had previously taken made it impossible to recover authorized plant investment, where the evidence PG&E had originally offered in the proceeding did not suggest there was a significant difference between the plant's tax basis and its book basis, even though such evidence was apparently available.)

[*177]

n45 In the same ruling, the FERC ALJ noted that trying to deal with the problem of sandbagging by permitting the aggrieved party to submit surrebuttal testimony is often not a good solution:

Allowing such evidence into the record on rebuttal invariably gives rise to the need for the undertaking of additional discovery and for the filing of surrebuttal evidence by the prejudiced party, and thus, at times, interminably delaying the conclusion of the hearings. To paraphrase... another proceeding, if the material was not included in the initial submission due to lack of diligence, or was knowingly withheld, then merely ordering further discovery and surrebuttal would be tantamount to rewarding the slothful and recalcitrant litigant and unduly burdening the more assiduous participants." (*Id.*)

Notwithstanding this general caution, the FERC ALJ did allow some of the intervenors to submit surrebuttal testimony on specific, narrowly-focused issues where Edison had a plausible argument that it could not have included the disputed material in its direct testimony. (*Id.* at pp. 65,067-65,068.)

[*178]

In his rebuttal testimony here, Mr. Dickson suggests that he views the well-established rule that a utility seeking a rate increase bears the burden of proof as a change in how the Commission has traditionally conducted water company GRCs. Dickson notes that as recently as 2002, when GSWC filed its last general office rate case, the company did not offer a detailed breakdown of the new positions it sought. Instead, "labor costs in total were examined and cost increases and upward trends in labor expense were closely examined by DRA." (Ex. 11, p. 76.) Dickson also remarks that "there have been many GRCs filed by GSWC over the years where the DRA chose not to challenge various positions," but that when DRA did challenge the need for a particular position, "detailed justification was always provided upon request." (*Id.*)

We find GSWC's explanation unpersuasive and unacceptable, particularly in view of the warning GSWC received against such conduct in D.04-03-039. We think it is clear that the manner in which GSWC presented its justification for the new positions here, by withholding much of the detailed rationale for them until rebuttal testimony, unfairly handicapped DRA in the preparation [*179] of its report and in its cross-examination of GSWC's witnesses. GSWC's repeated act of providing the principal justification for new general office positions in rebuttal testimony should be addressed beyond giving a stern warning and lecture. Accordingly, because of the prejudice to DRA (and hence to GSWC's ratepayers) our duty to protect our regulatory process, and the need to deter such conduct by GSWC and other utilities in the future, we intend to impose a penalty on GSWC for this conduct.

Our authority to levy a fine against GSWC for its conduct in the proceeding stems from Public Utilities Code Section 2107 (Section 2107):

Any public utility which violates or fails to comply with any provision of the Constitution of this state or of this part, or which fails or neglects to comply with any part or provision of any order, decision, decree, rule, direction, demand, or requirement of the commission, in a case in which a penalty has not otherwise been provided, is subject to a penalty of not less than five hundred dollars (\$ 500), nor more than twenty thousand dollars (\$ 20,000) for each offense. (Pub. Util. Code, § 2107 [*180] .)

Under Public Utilities Code Section 2108, each date on which a continuing violation remains in effect constitutes a separate violation.

We believe that GSWC should be fined for the previously described violations pursuant to our authority under section 2107 because any violation of statutes, Commission decisions, and directives, regardless of the circumstances, is a serious offense that should be subject to fines. Furthermore, as the Commission has previously recognized, "[t]he primary purpose of imposing fines is to prevent future violations by the wrongdoer and to deter others from engaging in similar violations. (D.01-08-058, mimeo. at 80, and D.04-09-062, mimeo. at 62.) We find that GSWC failed to disclose until rebuttal testimony its justification with respect to at least half of the general office positions at issue. Pursuant to Sections 2107 and 2108, each of these ten positions is considered a separate offense, for a total of ten offenses. Therefore, the range of the fine may be from \$ 5,000 to \$ 200,000.

The question we now turn to is what is the appropriate penalty in this case? The Commission's general criteria for determining [*181] the amount of a fine are set forth in D.98-12-075. (84 CPUC2d 155, 188-90.) As stated in that decision, in cases where there has been no physical harm to the public, the relevant criteria in determining the appropriate amount of a fine are as follows:

- Economic harm: The severity of a violation increases with (i) the level of costs imposed on the victims of the violation, and (ii) the unlawful benefits gained by the public utility. Generally, the greater of these two amounts will be used in setting the fine. The fact that economic harm may be hard to quantify does not diminish the severity of the offense or the need for sanctions.
- Harm to the Regulatory Process: A high level of severity will be accorded to violations of statutes or Commission directives.
- Number and Scope of Violations: A single violation is less severe than multiple offenses. A violation that affects many consumers is worse than one that is limited in scope.
- Utility's Action to Prevent a Violation: Utilities are expected to take reasonable steps to comply with applicable laws and regulations. The utility's past record of compliance may be considered in assessing a penalty.
[*182]
- Utility's Action to Detect a Violation: Utilities are expected to diligently monitor their activities. Deliberate, as opposed to inadvertent wrongdoing, is an aggravating factor.
- Utility's Action to Disclose and Rectify a Violation: Steps taken by a utility to promptly report and correct violations may be considered in assessing a penalty.
- Need for Deterrence: Fines should be set at a level that deters future violations. Effective deterrence requires that the size of a fine reflect the financial resources of the utility.
- Degree of Wrongdoing: The Commission will review facts that tend to mitigate the degree of wrongdoing as well as facts that tend to exacerbate the wrongdoing.
- Consistency with Precedent: Any decision that levies a fine should address previous decisions that involve reasonably comparable circumstances and explain any substantial differences in outcome.
- Public Interest: In all cases, the harm will be evaluated from the perspective of the public interest.

Some of the above criteria suggest that only a modest fine is warranted. GSWC is a relatively small water company, and the amount of the fine must reflect its financial resources. Also, it is [*183] unclear whether there has been any economic harm to ratepayers because we do not know whether DRA would have succeeded in securing a different result had GSWC provided the detailed analysis on the new positions in its direct testimony. Of course, D.98-12-075 also states that the fact that economic harm may be hard to quantify does not diminish the severity of the offense or the need for sanctions.

On the other hand, several criteria weigh in favor of a larger fine. GSWC's action harmed our regulatory process and is the type of act that we would want to prevent in future rate cases. In its rebuttal, GSWC made it clear that it does not take its burden to justify its case in direct testimony seriously. In 2004, this Commission found that GSWC conducted similar conduct. Clearly, the message we sent in D.04-03-039 did not have an impact on GSWC. GSWC's failure to comply with D.04-03-039 and its repeated conduct weighs in favor of a higher fine. Moreover, GSWC has not taken any responsibility for its conduct in this case, nor did it take any steps to rectify the harm it caused.

As previously mentioned, in D.04-07-022, a decision concerning Edison's revenue requirement, the Commission declined [*184] to penalize Edison for its failure to provide justification for a non-controversial capital addition in its direct showing. DRA did not dispute the reasonableness of the capital additions, conceded that Edison's omission of its justification was inadvertent, and did not make any claim or showing that it submitted data requests on the justification for capital additions. (D.04-07-022, pp. 156-157.) We concluded, in relevant part, that "SCE obviously made a simple mistake. Its failure to include the justification with the application was not part of a litigation strategy whereby SCE would wait until rebuttal to spring this information on unsuspecting parties." (*Id.*, p. 157.) We further declared, "[n]otwithstanding today's decision, we reserve the right to deny consideration of any 'rebuttal' evidence that could have and should have been included with the utility's direct showing, even where, as here, a simple mistake of omission has been made by the utility." (*Id.*, p. 158.)

In contrast, in this case, DRA disputed the reasonableness of the justifications of the 20 new positions set forth in GSWC's rebuttal testimony. Also, [*185] we do not find, nor does GSWC claim, that it simply made a mistake. While we declined to disallow GSWC's rebuttal testimony for the reasons previously stated, given the totality of the circumstances, including GSWC's repeated conduct, its failure to take responsibility for its actions, and GSWC's financial resources, we believe that a fine of \$ 50,000 is appropriate. By levying a fine against GSWC, we send a strong message to GSWC and other utilities that direct testimony is the time to address and justify its case. In particular, when there is a proposed rate change, new policy proposals or ideas, business changes that could or should influence the treatment of historic data, dramatic regulatory or environmental events and/or significant additions to the employee base or the capital budget, the burden is particularly obvious. Furthermore, as general office expenses are routinely contentious in water cases, it is not unreasonable to expect utilities to be forthcoming in their justifications of these expenses. The integrity of our regulatory process is best served when a utility justifies and addresses the issues in its application in direct testimony.

Therefore, we direct Water Division [*186] to prepare an order to show cause for Commission consideration as to why GSWC should not be fined \$ 50,000 for its conduct in this proceeding. We also direct Water Division to prosecute this Order to Show Cause. Issues considered in the Order to Show Cause shall be considered adjudicatory and thus subject to a ban on *ex parte* communications.

7. General Office Positions Requested by GSWC Due to the Sarbanes-Oxley Act

Among the most contentious issues between DRA and GSWC on the latter's personnel needs has been the number and kind of new positions that should be authorized for general office purposes due to the Sarbanes-Oxley Act of 2002 (SOX). This statute, which was passed in the wake of the Enron and Worldcom corporate accounting scandals, affects public companies like GSWC in three major ways. n46 First, SOX § 302 requires that the CEO and CFO make a certification (under criminal penalties) of the truth of the quarterly financial statements filed with the Securities and Exchange Commission (SEC). Second, SOX § 404 requires that management prepare an annual "internal control report" that describes the company's internal control structure, states whether management believes [*187] these internal controls have been effective, and also states whether the company's outside auditors agree with this assessment. Third, SOX § 906 requires the CEO and CFO to make a quarterly certification to the SEC that the company's financial reports comply with SEC requirements. (Ex. 11, pp. 23-25.)

n46 According to Robert J. Sprowls, the company's Chief Financial Officer, Senior Vice President of Finance and Secretary, GSWC is considered a public company because it issues debt in its own name, even though GSWC is also a wholly-owned subsidiary of American States Water Company. (Tr. 915.)

GSWC is requesting four positions where 50% or more of the new job's time would be devoted to SOX issues and compliance. The four new positions are: (1) Vice President of Finance, Treasurer and Assistant Secretary, (2) Tax Manager, (3) Financial Reporting Supervisor, and (4) Accountant. In addition, GSWC is seeking to add an Internal Auditor, 25% of whose time would be devoted to SOX compliance. As explained below, DRA opposes [*188] funding for all of these new positions except the Financial Reporting Supervisor.

7.1. GSWC's General Stance on New Positions Required for SOX Compliance

Most of the new general office positions GSWC is seeking based on its SOX needs relate to tax issues, because when the company changed its outside auditing firm from Arthur Andersen & Co. to PricewaterhouseCoopers (PWHC) in 2002, GSWC was required to restate its financial results for 2000 and 2001 due to deferred income tax errors.

Although Ms. Darney-Lane offered a justification for the five new positions in her direct testimony (Ex. 5, Darney-Lane, pp. 29-36), an even more substantial justification for the new positions is set forth in the rebuttal testimony of Robert J. Sprowls, GSWC's Chief Financial Officer, Senior Vice President of Finance and Secretary. We discuss each of these new positions below.

7.1.1. Vice President of Finance, Treasurer and Assistant Secretary

Ms. Darney-Lane's testimony states that this job was created in November 2002, too late to be included in the company's last general office GRC, A.02-11-007. According to Darney-Lane, "it is the Vice President of Finance, Treasurer and Assistant Secretary's [*189] primary obligation to oversee the company's day-to-day compliance with the Sarbanes-Oxley Act of 2002." (Ex. 5, Darney-Lane, pp. 32-33.) n47

n47 In the rest of her testimony, Darney-Lane often refers to this position simply as the "Vice President of Finance" or "VP of Finance." For the sake of brevity, we will use these terms as well.

7.1.1.1. Positions of the Parties

In her testimony, Darney-Lane sets forth at considerable length what overseeing GSWC's day-to-day compliance with SOX entails. With respect to SOX § 302, which requires the company's CEO and CFO to certify the company's financial statements, she notes that the company must now spend much more time reviewing and ensuring the accuracy of financial statements, and "while it is the CEO and CFO that must sign off on the certification, the bulk of the additional detailed work is performed by the Vice President of Finance." (*Id.* at 34.)

With respect to SOX § 906, which requires quarterly certification to the SEC by the CEO and CFO that the company's [*190] financial reports comply with certain SEC requirements and fairly represent the financial condition and results of the issuer, Darney-Lane notes that the Vice President of Finance is responsible "to ensure the compliance before the CEO and CFO sign off on the certification." (*Id.* at 33.)

With respect to SOX § 404, which requires GSWC's management to prepare an annual internal control report and state how effective the internal control structure has been in ensuring the accuracy of the company's financial reports (and whether the outside auditors agree with this assessment), Darney-Lane states:

In order to accomplish this, the VP of Finance has the responsibility to continually assess 16 mega accounting processes and document and test about 250 key controls (more than 400 key controls in 2004) to ensure the compliance. This requires a continuous monitoring and updating of accounting policies and procedures. The requirements of doing this are ongoing year after year. GSWC obtained an unqualified opinion in March of 2005 attesting [to] the effectiveness of its internal controls for financial reporting in 2004. (*Id.* at 35.)

In addition to ensuring SOX compliance, Darney-Lane [*191] notes that the VP of Finance is charged with focusing on the company's financing needs, which have grown significantly in the past decade due to the need for infrastructure replacement. Other duties include overseeing tax compliance and the preparation of accounting records, and serving as a liaison between the areas of the company that handle accounting and regulatory affairs. (*Id.* at 35-36.)

In his report for DRA, Aslam opposes funding for the VP of Finance position (which pays \$ 162,500 per year) on the ground that it is "an unnecessary layer within GSWC's organization structure." (Ex. 23, p. 2-22.) Aslam states:

DRA . . . believes that the financial reporting requirements imposed by the various sections of the Sarbanes-Oxley Act directly involve GSWC's CEO and CFO but not the Treasurer. The CFO is paid an annual Salary of \$ 235,000 and CEO an annual salary of \$ 410,000. DRA wonders what these two top executives themselves are contributing, when GSWC is often requesting new additional positions to perform their responsibilities.

As for GSWC's financial reporting responsibilities, they are directly related to the Controller and not the Vice President of Finance. The Controller [*192] should report directly to the CFO and not the Vice President of Finance. (*Id.*)

7.1.1.2. Discussion

We agree with GSWC that the Vice President of Finance position should be authorized. As discussion throughout this decision makes clear, SOX has imposed significant new burdens on public companies, including utilities. Ms. Darney-Lane presented a full justification for the position in her direct testimony, a justification that Robert J. Sprowls - who held the job until the Spring of 2006 - repeated largely verbatim in his rebuttal testimony. n48 As Darney Lane's description of the duties of the job makes clear, the Vice President of Finance cannot reasonably be considered "an unnecessary layer within GSWC's organization structure."

n48 The Vice President of Finance position is now held by Eva Tang. *See* Exhibit 16, p. 1.

For example, there is no dispute within the academic literature that in order to comply with § 404 of SOX by December 31, 2004 - as public companies like GSWC were required to do - the companies [*193] were required to conduct a detailed scrutiny of their accounting procedures and other internal control mechanisms and make changes where necessary. Darney-Lane's statement that the VP of Finance had to review 400 key controls in 2004, and about 250 in 2005 and thereafter, is consistent with a leading study on SOX compliance costs by CRA International that was cited by the Illinois Commerce Commission in a recent decision. n49

n49 The 2006 update to the CRA International study, which is referred to in the Illinois Commission's decision as the "Charles River Associates" study, is entitled *Sarbanes-Oxley Section 404 Costs and Implementation Issues: Spring 2006 Survey Update*. It can be found on the web at www.s-oxinternalcontrolsinfo.com/pdfs/CRAIII.pdf. The Fall 2005 update to this study had found that for "smaller companies" such as GSWC (which are defined as those with market capitalizations between \$ 75 million and \$ 700 million), the number of controls tested in 2005 declined significantly from the number tested in 2004, the first year in which such companies had to be in compliance with SOX § 404. On the question of how many controls are being tested, the Spring 2006 update states:

[T]he Fall 2005 Survey found that an expected decline in the number of key controls tested, reflecting the benefits of experience, and greater reliance on the work of others[,] would also tend to reduce costs. For Smaller Companies, the number of key controls tested by auditors decline more than 21 percent on average from 262 to 206 from year one [2004] to year two [2005] . . .

Both Smaller and Larger Companies' management also reduced their own testing of key controls. (Spring 2006 Update, pp. 4-5.)

[*194]

We also have little doubt that GSWC's financing needs demand a good deal of attention from the Vice President of Finance. As Darney Lane points out, the company's capital projects budget has grown from \$ 16 million in 1995 to more than \$ 60 million today, due largely to GSWC's infrastructure replacement needs. This has increased the need for executive oversight of financing activities:

The four-fold increase in GSWC's capital spending has created the need for increased financing activities. The current level of capital expenditures is about 3 times depreciation, resulting in a need to issue long term financing, debt or equity, nearly every year. These upward pressures on capital spending are driving the need for more executive oversight in the financing area. (Ex. 5, Darney-Lane, p. 35.)

We also have little doubt that the need to oversee in-house accounting and tax compliance (to avoid further restatements) require the attention of a senior executive like the Vice President of Finance.

Finally, we agree with Sprowls that Aslam's suggestion that the duties of the Vice President of Finance overlap with those of GSWC's Chief Financial Officer (CFO) - and therefore the VP of Finance [*195] position is unnecessary - is without merit. In his rebuttal testimony, Sprowls explained the differences between the two positions as follows:

The formal title for the position is Chief Financial Officer, Senior Vice President of Finance and Secretary ('CFO, SVP-Finance & Secretary'). In an effort to save money, GSWC chose to combine the CFO position with the corporate Secretary position. Approximately 40% of the responsibilities of the CFO, SVP-Finance & Secretary position relate to the Secretary function. In addition, GSWC does not have an internal general counsel. The CFO, SVP-Finance & Secretary is also responsible for coordinating much of the work of the external general counsel. (Ex. 17, p. 19.) n50

n50 In his rebuttal, Sprowls also takes issue with Aslam's assertion that GSWC's controller should be reporting to the CFO rather than the Vice President of Finance. (Ex. 23, p. 2-22.) On this question, Sprowls states that having the controller report to the VP of Finance "gives management additional assurance that [accounting] errors will be caught," thus reducing the risk of further financial restatements. (Ex. 11, p. 20.)

[*196]

7.1.2. Tax Manager

GSWC first hired a Tax Manager (who receives an annual salary of \$ 127,000) in 2003, but this is the first time in the rate case cycle the company has sought authorization for this job.

In her direct testimony, Darney-Lane states that the position was created on the recommendation of PWHC, which replaced Arthur Anderson & Co. as GSWC's outside auditors in 2002. As part of the change in auditing firms, GSWC conducted a review of its income tax accounting. The income tax accounting had previously been handled by lower-level staff, and because of errors in their accounting for deferred income taxes, a restatement of the company's financial results for 2000 and 2001 became necessary. Based on this situation, GSWC's management concluded independently and was also advised by PWHC that "qualified tax staff should be added, specifically at the Tax Manager level." (Ex. 5, Darney-Lane, p. 29.)

Ms. Darney-Lane notes that the duties originally envisioned for the Tax Manager have increased since 2002, owing to the complexity of new tax legislation and new requirements of the Financial Accounting Standards Board (FASB). Darney-Lane also notes that "although this position [*197] was not created because of the Sarbanes-Oxley Act, the job has evolved and now is profoundly involved in compliance with the act." (*Id.*)

7.1.2.1. DRA's Position

Consistent with its skepticism about most of the new SOX-related positions GSWC is seeking, DRA opposes authorization for a Tax Manager. In his report for DRA, Aslam states:

First, GSWC did not provide details regarding the nature, source, cause, and the remedial action relating to the so called internal control weakness in tax. DRA understands that utilities sometimes have to revise their financial statements, but GSWC did not show the same or similar problem would likely reoccur in the future. The fact that the GSWC's external auditor verbally made its recommendations for hiring a Tax Manager only validates the concern that the problem may not have been severe.

Further, the increasing complexities of Federal and State tax law are nothing new. Both Federal and State governments constantly revise, amend, and add to tax laws depending upon the current needs and policies of the day.

GSWC currently has one Tax Supervisor and two Tax Specialists in addition to the position of Controller and other Accounting staff. [*198] The existing level of staff handling tax related assignment appears sufficient. There is no need for adding an additional Tax Manager position. (Ex. 23, p. 2-19.)

Aslam also questions the need for a Tax Manager in view of the new tax software GSWC is buying, a purchase DRA does not oppose. (*Id.*)

7.1.2.2. GSWC's Position

In his rebuttal testimony, Mr. Sprowls takes issue with Aslam's assertion that GSWC should be able to deal with its tax problems using a tax supervisor, assisted by two tax specialists. n51 On this question, Sprowls states:

While the specific titles may vary somewhat between public accounting firms and in industry, the general concept of four levels of staff is routinely applied by placement firms to the tax profession: entry-level (inexperienced staff), senior-level staff (experienced staff), manager/director level, and executive level (e.g., Vice President of Tax or Chief Tax Officer). To assert that a public company operating in the complex environment of regulation can support a tax function without adequate leadership (the role assumed at the tax manager level and above), including from a technical perspective, ignores the current accounting environment [*199] in which enterprises operate. (Ex. 11, p. 2.)

n51 On cross-examination, Sprowls stated that the Tax Supervisor who was with the company when the deferred income tax errors were discovered left sometime in 2002 or 2003. He was succeeded by the Tax Manager in August 2003. (Tr. at 903.)

Sprowls also points out that tax law and compliance are usually considered separate disciplines from the work of the controller and other accounting staff:

While a Controller should possess some knowledge of tax-related matters, it has been well recognized in the accounting profession that taxes are a distinct and specialized discipline. For example, separate tax departments are established in accounting firms of significant size and tax professionals have responsibility to audit the tax-related items reported in financial statements. In addition, while a Controller should possess knowledge regarding the GAAP [Generally-Accepted Accounting Principles] accounting of taxes, most Controllers would recognize their limitation with respect [*200] to interpreting and applying tax law and would not venture into practicing outside of their areas of expertise. With respect to [the] 'other Accounting staff' [referred to by Aslam,] none of the staff under the oversight of the Controller function in positions where tax knowledge is a requirement for their position. (Ex. 11, p. 2.)

In addition to arguing that a controller is no substitute for a Tax Manager, Sprowls notes that "a professional functioning in the capacity of a Tax Manager, with the requisite experience and expertise, is a 'given' for a public company such as [GSWC]." (*Id.* at 3.) During cross-examination by the ALJ, Sprowls noted that income taxes are always challenging for a utility, and that when he joined the company in 2004, he was surprised to learn that GSWC had only recently hired a tax manager:

[G]etting your taxes correct for a utility that's got a lot of hard assets - you have timing differences between book and tax depreciation on these hard assets. It's a huge task to get it right. And it's important that you've got very capable people to get it done.

* * *

To be honest, I was very surprised that the company . . . didn't have a tax manager prior [*201] to 2003. It's . . . just a very difficult area. And you've got to have somebody with excellent technical expertise. (Tr. 969-70.)

Sprowls also takes issue with Aslam's assertion that the company's new tax software is an adequate substitute for a tax manager. According to Sprowls, a good tax manager is needed to use the software effectively, because "it is at times of implementing software solutions that the amount of past experience and the extent of technical knowledge come into play the most . . . Software is a tool of professionals, not a reason to justify an absence of staff at levels of higher proficiency." (Ex. 17, pp. 6-7.)

Finally, Sprowls takes strong exception to what he regards as Aslam's "cavalier" attitude toward the possibility of financial restatements, and his suggestion that a tax manager is not justified unless GSWC can show there is some likelihood of further restatements in the future. On these issues, Sprowls states:

Restating financials is an incredibly serious matter. DRA's comment reflects a cavalier, nonchalant attitude towards restatement, and its assertion that 'GSWC did not show the same or similar problem would likely reoccur in the future' indicates [*202] a lack of awareness of developments in a post-SOX accounting world. DRA would have one believe that it would be acceptable to leave a gap in the leadership of the tax function because 'restatements happen' and that unless it can be proven that another restatement or internal control weakness would occur by continuing to have a tax leadership position vacant, it is not necessary to fill it . . . [However,] it is incumbent upon Management to assess risk and act accordingly to prevent a reoccurrence of the internal control weakness in tax, not to continue with the same level of tax competency and hope that a similar problem is not likely to reoccur. (*Id.* at 4-5.)

7.1.2.3. Discussion

In view of the need to restate its 2000 and 2001 financial results and the advice it received from PWHC that the company needed to hire a tax manager, we believe GSWC has provided an adequate justification for this position. Moreover, given the requirements of SOX § 404, we also find plausible Darney-Lane's argument that the duties of the Tax Manager have grown significantly since the position was created in 2002.

As Sprowls testified during cross-examination by the ALJ, the deferred income tax [*203] errors that led to the restatement of GSWC's financial results for 2000 and 2001 were not trivial:

Those amounts were in the neighborhood of \$ 5 million. And in order to make the restatement, it affected the income statement as well as the balance sheet. These are balance sheet items, but to accommodate the restatement, you've got to take them through the income statement. So both the income statements for 2000 and 2001 for both Southern California Water and American States Water and the balance sheets for those two years were restated. (Tr. 961.)

During cross-examination, Sprowls also emphasized that SOX has made the work of the Tax Manager more difficult, because there is less room for error now:

What's happening in the tax area is: it used to be that, you know, you could take a pass on a quarterly basis getting your taxes right, as long as you got it right on an annual basis, because you had [a] cushion - tax cushion to move in and out. And that isn't the case anymore. With Sarbanes-Oxley, it has to be right every quarter. And that's why you're seeing three-, four-, five-fold increase[s] in restatements. (*Id.* at 965.) n52

n52 At another point in the cross-examination, Sprowls noted that "the leading cause of restatements is in the tax area." (*Id.* at 964.)

[*204]

Although Sprowls conceded that GSWC is especially sensitive about restatements because of having to restate its 2000 and 2001 results, (*id.* at 964), we also agree with him that DRA's attitude toward the possibility of further restatements can fairly be characterized as "cavalier." As Sprowls noted, even though GSWC is a wholly-owned subsidiary of American States Water Company, it is nonetheless subject to SOX because it issues public debt. Moreover, the company's need to issue public debt is increasing, due largely to GSWC's ambitious infrastructure replacement program, particularly in Region II. In light of this, we agree with Sprowls that GSWC needs to take all reasonable efforts to maintain investor confidence by avoiding financial restatements, and that having a competent Tax Manager is an important step in that direction.

7.1.3. Financial Reporting Supervisor

In her direct testimony, Darney-Lane offered the following justification for the new position of Financial Reporting Supervisor:

The organization under the Controller at the beginning of 2005 included one accounting supervisor with three staff reporting to this person, and one senior financial reporting analyst [*205] reporting to the Controller with no direct reports. Because of the significant changes over the past couple of years . . . the day-to-day responsibilities have varied depending on the availability of people and skill sets within the department. As work and issues come up, the work was allocated accordingly based primarily on individual skill sets.

* * *

However, this structure was not conducive to an effective department because of the fact we are a regulated entity. The monitoring and analysis of the utility plant area is a full time job and should have GO accounting staff devoted only to this area. This is the Company's biggest area (approx. 80% of total assets) and receives the most amount of attention from the external auditors, tax dept, regulatory affairs, CPUC and others. It was therefore suggested that the accounting department be split into two groups. [The] Controller would have two accounting supervisors as follows:

. Utility Plant Supervisor - in charge of all aspects of Utility Plant. This person would have one full time accountant reporting to them.

. Financial Reporting Supervisor - in-charge of all financial reporting and all other areas (excluding Utility Plant). [*206] This person would have three full time accountants reporting to them." (Ex. 5, Darney-Lane, pp. 30-31.)

In his report for DRA, Aslam accepts this justification and does not oppose the new position, which would pay \$ 79,000 per year.

In light of the justification offered by GSWC and the lack of opposition by DRA, we will authorize this new position.

7.1.4. Accountant

7.1.4.1. Positions of the Parties

In her direct testimony, Darney-Lane states notes that GSWC is requesting one new Accountant, a "junior level" position that pays \$ 68,307 annually, to add to the Financial Reporting Group within the Accounting and Finance Department. She notes that the workload of the Financial Reporting Group has increased significantly in recent years due to the need to monitor the effectiveness of internal controls required by SOX, greater regulatory complexity caused by things such as memorandum accounts, and "increases in nonregulated activities." (Ex. 5, Darney-Lane, p. 31.) Ms. Darney-Lane sums up the duties of the proposed new position as follows:

Currently, the Financial Reporting Group at the general office has one supervisor with two junior accountants reporting to the supervisor. [*207] The new junior accountant position will join this group and will assist with our ongoing compliance with Sarbanes-Oxley's Section 404 requirements and help reduce[] the workload of the other accountants in a fair and equitable manner which, in turn, will improve [the] efficiency and accuracy of the Department. (*Id.*)

In his report for DRA, Aslam opposes this position on the ground that GSWC already has enough staff to deal with the new issues SOX has created. Noting that the Accounting and Finance Department will soon have 26 employees (including the newly-authorized Financial Reporting Supervisor), Aslam argues that this is enough:

As a result [of the recent reorganization,] GSWC's Controller now has two Financial Reporting Supervisors and three junior accountants who assist the two Financial Reporting Supervisors. This arrangement gives the GSWC Controller adequate Financial Reporting staff to handle the increased workload that might have been created by the Sarbanes-Oxley Act. On the other hand, GSWC does have a position of a highly paid Controller who at the most part should be dealing with accounting related issue[s] herself. With this level of increased supporting staff, [*208] the contributions of the GSWC[] Controller itself becomes questionable. (Ex. 23, pp. 2-20 to 2-21.)

7.1.4.2 Discussion

We have decided to authorize this new position. Although, he spends a great deal of his rebuttal testimony disputing various assumptions made by Aslam about the work of GSWC's Controller and its Accounting Department, Mr. Sprowls also offers the following SOX-based justification for the new Accountant position:

One of the main responsibilities of the new Accountant position will be to take over the numerous monthly bank reconciliations to be performed on a timely basis. There are over 20 bank reconciliations that need to be completed every month. This task alone involves significant time and effort and is considered a key control by both the Company and its external auditors from a Sarbanes-Oxley standpoint. In fact, during their quarterly reviews, our external auditors (PWHC) have informed us that the lack of timely bank reconciliations may have to be reported to the Audit Committee of the GSWC Board of Directors. Because of the significant increase in workload over the last couple of years, the preparation of timely bank reconciliations have at times [*209] fallen behind. We have attempted to allocate the completion of bank reconciliations to the existing two junior accountants while still balancing all other increased responsibilities. This has resulted in significant overtime and the use of temporary help. (Ex. 17, pp. 10-11.)

Combined with the rationale offered by Ms. Darney-Lane, we find this justification sufficient for the additional junior-level Accountant position.

7.1.5. Internal Auditor

Although this is a junior-level position paying \$ 71,000 per year, the parties have devoted considerable attention to it because of DRA's assumptions about auditing responsibilities within GSWC.

7.1.5.1. Positions of the Parties

In her direct testimony, Ms. Darney-Lane notes that this position is being sought at the direction of GSWC's Audit Committee:

The increased importance and emphasis on risk management and the monitoring of the effectiveness of internal controls over financial reporting, brought about by Sarbanes-Oxley, warrants this additional headcount. Approximately 25% of this position's job functions are related to our ongoing compliance with Sarbanes-Oxley's Section 404 requirements. The duties performed by this employee [*210] will greatly reduce the fees we currently pay to outside consultants (e.g., Jefferson Wells International, Robert Half, etc.) and should result in a net reduction in cost to the company. (Ex. 5, Darney-Lane, p. 32.)

In his report for DRA, Aslam opposes this position because he believes the auditing is performed for the benefit of GSWC's corporate parent - which he and Sprowls both refer to as "AWR" - rather than the SEC:

GSWC does not report to the [SEC] at the end of the year; it is AWR that is responsible for this financial reporting. GSWC's own organization chart does not depict these positions as having any reporting relations within the Accounting & Finance Department. The Audit Manager directly reports to the Board of Directors instead.

Therefore, DRA recommends disallowing not only the position of Internal Auditor, but also removing all labor expenses related to the other Internal Auditing staff: namely, the Audit Manager and Senior Auditor as well. (Ex. 23, p. 2-21.)

7.1.5.2. Discussion

In his rebuttal testimony, Mr. Sprowls states that all of the assumptions behind Aslam's position on auditing are incorrect. After quoting the Aslam statement above, Sprowls states: [*211]

I disagree with Mr. Aslam's recommendation because his first two observations are incorrect[,] and there is an excellent reason justifying the situation contained in his third observation.

GSWC's internal auditing is not performed for the benefit of AWR, but is performed for the benefit of GSWC and its customers. It has been a standard practice in U.S. business to have an internal audit department long before the U.S. government passed [SOX]. Internal Audit departments have been in place to confirm that the procedures followed by regulated and competitive businesses were both effective and efficient. The requirements of SOX have made the need for an Internal Audit department even more critical. GSWC's Internal Audit Department has played a key role in assisting management in preparing GSWC to be compliant with SOX for 2004, 2005 and in the future . . .

Mr. Aslam is [also] incorrect in his observation that GSWC is not required to file its financial statements and associated disclosures with the SEC. GSWC has issued public debt in the past and many issues are still outstanding. GSWC's customers enjoy the benefit of lower financing costs as a result of public debt issuances. [*212] Since GSWC issues publicly-traded debt, it is required to make quarterly filings of its financial statements with the SEC along with the associated disclosures. GSWC is responsible for its financial reporting with the SEC, not AWR.

Mr. Aslam stated that the fact the Internal Audit Manager reports to the GSWC Board of Directors rather than to the Accounting & Finance Department is a reason for disallowing the expenses of the Internal Audit department. Technically, the Internal Audit Manager reports to the Audit Committee of the GSWC Board of Directors. For an internal audit department to be effective and for its audit reports to have credibility, it is critical that the department maintain its independence. A best practice for competitive and regulated companies is to have the internal audit department report directly to the Audit Committee of the Board of Directors to ensure its independence, which is how it is structured at GSWC. (Ex. 17, pp. 13-14.)

We accept these explanations by Mr. Sprowls. In addition, we note Ms. Darney-Lane's point that by adding a junior-level Internal Auditor, GSWC expects to save money by reducing consultant fees. Mr. Sprowls noted during cross-examination [*213] that when consulting firms provide an employee to a client on a temporary basis, they typically charge the client three times the amount they are paying the temporary employee. (Tr. at 971-72.) Thus, bringing the Internal Auditor position in-house makes sense.

8. DRA's Challenge to General Office Positions At Issue in A.02-11-007

In addition to its challenge to the 25 new general office positions that GSWC is seeking in this rate case, DRA also argues that eight of the general office positions that were approved in the company's last general office GRC, A.02-11-007, should be disallowed.

DRA acknowledges that there is nothing in D.04-03-039, the decision that resolved A.02-11-007, to indicate disapproval of these positions. However, DRA argues that the burden was on GSWC to justify these new positions, and that it failed to meet that burden:

When requesting new positions in the prior GRC, A.02-11-007, GSWC presented no supporting written testimonies; DRA was not informed that GSWC was requesting any new positions. The salary expenses for the new hires were embedded in the GSWC's forecasted labor expense and the positions were inserted into the organizational charts. The [*214] absence of supporting testimony for those new hires was not only deceiving but indicated the lack of justifications for the new positions. DRA now finds out that some of the positions added in this fashion make no practical and economical sense at all. DRA strongly protests this sort of evasiveness. GWC must present and justify all of its requests for additional expenses in a clear and detailed fashion.

The Commission's approval of an overall labor expense does not amount to the Commission approval of new positions that are unjustified and unsupported by specific written testimony. GSWC's elusive presentation deprives DRA of notice and due process and results in an incomplete and less than full record for the Commission's deliberations. (Ex. 23, pp. 2-26 to 2-27.)

8.1. DRA's Position

DRA's report identifies 19 general office positions with annual salaries totaling \$ 1,169,204 that were subject to the allegedly stealthy tactics described above. As noted previously, DRA is challenging eight of these positions as unjustified, and asks that their salaries be disallowed in this GRC. The challenged positions and their respective annual salaries are: (1) System Programmer (\$ 69,956), [*215] Risk Manager (\$ 115,289), (3) Senior HR Specialist (\$ 62,243), (4) CIS Billing Specialist (\$ 51,906), (5) Assistant Applications Support (\$ 53,861), (6) Senior Financial Analyst (\$ 85,365), (7) Financial Analyst (\$ 68,000), and (8) Senior Auditor (\$ 89,666). (*Id.* at 2-27 to 2-30.) The combined annual salaries of the challenged positions total \$ 596,286.

In summary, DRA's reasons for challenging these positions are as follows:

- . System Programmer - DRA argues this position is unnecessary because GSWC already has two Senior System Programmers, who receive regular technical help from outside vendors as well as GSWC's functional areas such as Accounting and Finance.

- . Risk Manager - DRA opposes this position because the Risk Manager "mostly performs liaison Services between GSWC and its outside Brokers and Third-Party Claim[s] Administrator," both of whom are also well-paid. However, DRA does not oppose the subordinate position of Risk Analyst.

- . Senior HR Specialist - DRA opposes this position because it believes GSWC's Human Resources Department is already adequately staffed.

- . CIS Billing Specialist - DRA opposes this position in the department that handles [*216] GSWC's customer billing because there has not been enough customer growth to justify it, and more likely, the

increase in GSWC's Non-regulated Billing Service Contracts [is] the most salient cause for this new position.

. Assistant Applications Support - DRA opposes this position because GSWC already has an Applications Support Manager with an Assistant and other personnel, in addition to receiving support from various vendors for the software installed throughout the company.

. Senior Financial Analyst - DRA opposes this job because GSWC already has one Senior Financial Analyst, in addition to a manager, supervisor, financial analyst and associate financial analyst in its Accounting & Finance Department.

. Financial Analyst - DRA also opposes this position because GSWC already has one Financial Analyst in the Accounting & Finance Department, and in DRA's view does not need another.

. Senior Auditor - Consistent with its position that all of GSWC's auditors ought to be considered employees of GSWC's parent company, AWR, DRA opposes this position.

8.2. GSWC's Position

Although the company's rebuttal testimony does not devote as much attention to the eight [*217] positions described above as to the new general office positions being sought in this GRC, the company argues that DRA is wrong on every job covered by D.04-03-039 that DRA is now challenging.

Four of the eight jobs are addressed in the rebuttal testimony of Robert Sprowls, and the other four in the rebuttal testimony of Joel Dickson. In brief, the company's rationale for the challenged positions is as follows:

. Risk Manager - Sprowls points out that GSWC's Risk Manager has many duties other than performing "liaison Services" with outside insurance brokers and the third-party claims administrator. These duties include (1) using knowledge in the fields of insurance, operations, finance and safety, among others, to reduce risks within the company, (2) managing damage and injury claims brought against the company by persons in its service area, and (3) preparing information for potential insurance carriers, since the company carries large amounts of insurance to cover claims involving its operations and \$ 920 million of gross utility plant (including vehicles), even though GSWC self-insured for workers' compensation. (Ex. 17, pp. 21-22.)

. Senior Financial Analyst and Financial [*218] Analyst - With respect to these positions, Sprowls argues that the duties of the company's Finance section have grown so much since 2002 that it is unreasonable to expect that the staff in place when A.02-11-007 was filed can meet all of these needs. For example, there is more need for help in securing short- and long-term debt, since GSWC's gross utility plant has grown from \$ 731 million in 2002 to over \$ 920 million today. Another example is the increased time that must be devoted to preparing quarterly and annual reports for the SEC since the passage of SOX. (*Id.* at 23-24.)

. Senior Auditor -- Although Sprowls does not specifically address this position, his opposition to DRA's position is implicit from his comments that under sound principles of corporate governance, the internal auditors of GSWC should and do report to the Audit Committee of GSWC's board of directors, rather than to the board of GSWC's corporate parent, AVVR. (*Id.* at 12- 14.)

In his rebuttal testimony, Mr. Dickson offers the following justifications for the following positions:

. System Programmer - Dickson argues that this position is needed to monitor and allocate capacity on GSWC's mainframe [*219] computer, which is "continually being stretched to its limits by the increased workload." In addition to this traffic management function, the System Programmer monitors access to files that GSWC's auditors consider crucial "from a fraud and sabotage perspective" to ensure SOX compliance. (Ex. 11, p. 77.)

. Senior Human Resource Specialist - Many of this position's duties relate to SOX, which has led to a need for more extensive background checks for both new hires and promotions, as well as numerous requests from the auditors during the quarterly audits of the Human Resource Department. There are also annual audits of three benefit plans administered by the department, which also has responsibility for helping with increased certification requirements for operators, and well as compliance with the Health Insurance Portability and Accountability Act (HIPPA). (*Id.* at 78-79.)

. CIS Billing Specialist - In response to DRA's argument that only one such position should be necessary, Dickson notes that one of the CIS Billing Specialists is responsible for generating customer bills on active accounts (including past-due notices), while the other handles closed account and [*220] bad debt collections, including the maintenance of relevant legal documents. (*Id.* at 80.)

. Assistant Applications Support Analyst - Dickson argues that GSWC does not currently have an Applications Support Manager, and that DRA does not understand the duties performed by the company's other personnel who work in applications support. The Applications Support Supervisor supervises the staff that prepares customer bills using the current CIS system, and the Senior Applications Support Analyst helps design, develop and test new systems needed within the company along with outside applications vendors. The Assistant Support Analyst, on the other hand, performs tasks required to administer the CIS system, including transferring customer revenue information, helping with audits, and providing second-level support for CIS trouble-shooting and configuration changes. (*Id.* at 81.)

8.3. Discussion

While we appreciate the clarification provided by Dickson and Sprowls about just what duties the challenged positions do perform, we agree with GSWC that DRA's challenge to these positions amounts to a collateral attack on D.04-03-039, and is therefore improper. As Dickson points [*221] out in his rebuttal testimony, while DRA "closely examined" total labor costs in A.02-11-007, it apparently did not request information about any of the new positions included within this total. In light of this, we agree with Dickson that DRA is improperly attempting to impose the standards that now apply to Class A water GRCs onto a case that was filed more than four and one-half years ago:

[A.02-11-007] was filed in the same manner as many earlier General Office filings. That is how the expectations were set and both the Company and DRA had a somewhat common degree of understanding of those expectations. To impugn purposeful deception with respect to traditional expectations does little to advance the efficient and effective process of rate setting. With the advent of the new Rate Case Plan[,] many of the old expectations have been changing and GSWC is readily adapting to them . . . The mandatory filing requirements, the master data requests, and the process of examining filings for deficiencies has changed the traditional way rate filings were made. In criticizing GSWC's previous filing, DRA is imposing the filing requirements of the new Rate Case Plan onto previous cases [*222] that were submitted and litigated under different rules and filing protocols. It is improper for the DRA to engage in this type of four year retrospective analysis of previous GRC proceedings. (*Id.* at 76-77.)

Accordingly, DRA's challenge to the eight general office positions described above is rejected.

9. Most of the Miscellaneous Disputed Issues Between GSWC and DRA Should Be Resolved in Favor of the Company

As noted in our discussion of the August 4, 2006 settlement stipulation between GSWC and DRA, there are a number of miscellaneous issues these two parties have left for resolution by the Commission, including general office rent, the proper amounts for insurance, and the amount of water usage that should be assumed for commercial customers. In this section, we discuss and resolve these issues.

9.1. Miscellaneous General Office Expenses Including Dues to Trade Organizations

As noted above and in P 5.08 of the settlement stipulation, DRA and GSWC remain about \$ 600,000 apart on the amount of proper miscellaneous expenses for the general office. Although they used different forecasting methodologies, a significant part of the difference between GSWC's position and [*223] DRA's concerns the dues paid to trade

associations such as the National Association of Water Companies (NAWC), the California Foundation on the Environment and Economy (CFEE), and the American Council on Education (ACE). In his report for DRA, Aslam estimates that GSWC pays annual dues to NAWC of \$ 121,857, to CFEE of \$ 15,000, and to ACE of \$ 1385 per year. (Ex. 23, p. 2-47.)

With respect to NAWC, Aslam contends that the dues payment should be excluded because NAWC's "sole purpose is political lobbying in the nation's Capitol." Aslam contends that GSWC's membership in CFEE, which he also characterizes as a lobbying organization, is redundant in view of the fact that the company is a member of the California Water Association, "which provides forums for sharing best practices, and promotes sound, reasonable, and science-based policy making by regulatory agencies," in addition to lobbying. (*Id.*) Finally, Aslam notes that GSWC's membership in ACE will be unnecessary if the Commission accepts DRA's recommendation to dissolve the EDU. (*Id.* at 47-48.)

In its opening brief, GSWC argues that DRA is wrong to argue that NAWC and CFEE engage solely in lobbying, and adds that "these [*224] expenses have been included in prior rate cases, and are allowed for other water utilities." (GSWC Opening Brief, p. 43.)

We agree with GSWC that its methodology for estimating the miscellaneous expenses for the general office is superior to that of DRA, and that all three of the above-noted dues payments should be allowed. n53 Thus, we will allow the \$ 2,009,400 that the company has requested as miscellaneous expenses for the general office in Test Year 2007.

n53 This is consistent with our decision in section 6.2.13.4 of this decision not to dissolve the EDU.

9.2. General Office Rent

On this issue, the parties remain far apart: GSWC seeks \$ 246,300 for general office rent, while DRA would allow \$ 21,700. In its opening brief, GSWC argues:

GSWC currently has a serious shortage of space. In fact, overcrowding in the General Office has forced several employees to telecommute . . . With the addition of the above-described requested positions, new space will be needed even more. GSWC needs the additional space [*225] because the company has grown in ways that simply could not have been anticipated . . . Besides the ordinary expansion of the business, GSWC's technological needs, training requirements, customer service requirements, and benefits and human resources initiative have all changed the Company's need for space. (GSWC Opening Brief, pp. 39-40; citations omitted.)

In its reply brief, DRA argues that the company's pleas for more space are unsupported, and that GSWC has not rebutted DRA's claim that the need for more general office space is really driven by the growth in GSWC's non-regulated businesses, especially ASUS. (DRA Reply Brief, pp. 34-35.)

On this issue, it appears to us that GSWC does indeed need more general office space, but that part of this need is driven - as DRA asserts - by the growth in the company's non-regulated businesses. As noted in our discussion of the new Call Center Support Analyst position the company is seeking, Mr. Dickson testified that GSWC wants to include only 69% of the salary for this position in rates; the rest is to be allocated to ASUS "new business." (Ex. 11, p. 53.) In her direct testimony, Ms. Darney-Lane states that one of the reasons GSWC needs [*226] a new Accountant is an increase in workload in the Financial Accounting Group due to, *inter alia*, "increases in non-regulated activities." (Ex. 5, Darney-Lane, p. 31.) These statements lend some credence to DRA's assertion that the growth in non-regulated businesses is a significant factor driving the need for new space, especially since GSWC's own customer growth is essentially flat.

In view of our conclusion that the need for new office space is driven partly by the growth in GSWC's non-regulated businesses, we will allow the company to include \$ 184,725, or 75% of its rental space request, in rates for general office operations. n54

n54 DRA is also correct when it asserts that GSWC has erred in claiming that "DRA does not dispute, especially if GSWC's requested positions are granted, that additional space is badly needed." (DRA Reply Brief at 35, quoting GSWC Opening Brief at 40.) In fact, what Aslam stated in his DRA report was as follows:

[A]s discussed earlier in this Report, the need for [a] 'fully staffed' Customers Service [Center] is growing due to GSWC's involvement in Non-regulated businesses and not due to increases of its regulated California operations . . . [I]f DRA's recommendations to close the EDU are adopted, more space will become available. Last, if DRA recommendations to reduce the staff level at the General Office are approved, this will also increase the availability of space at the General Office. (Ex. 23, pp. 2-49 to 2-50.)

[*227]

9.3. Business Meals

In its report and opening brief, DRA argues that GSWC should be allowed \$ 66,100 for general office meals, while the company seeks \$ 89,300. Part of the difference relates to different forecasting methodologies; GSWC escalated the last two years of data, whereas DRA looked at 2001-2005 but excluded 2001 and 2005 as unrepresentative. However, another difference between the parties centers on whether ratepayers should be asked to pay for business meals where no travel is involved. (Ex. 23, p. 2-43; GSWC Opening Brief, p. 40; DRA Reply Brief, p. 35.)

On the meal issue, we think the arguments of both sides have some merit. DRA is correct that under the Rate Case Plan set forth in D.04-06-018, the utility is supposed to present (although it is not bound by) five years of data. The average of the five years of general office meal data set forth in DRA's report is \$ 63,445.80. On the other hand, we know from common experience that meal expenses, especially at restaurants, have increased significantly since 2004. We also think that GSWC should not be bound by state government reimbursement rules for meals, under which lunch expense is generally recoverable only in [*228] connection with out-of-town travel. Taking all these factors into account, we will authorize GSWC \$ 82,500 for general office meal expense.

9.4. Injury, Damage and Property Insurance

In their briefs, GSWC and DRA state that they remain far apart on how much should be allowed for the company's insurance needs. Although they have agreed that 79% of insurance costs should be expensed and 21 % should be capitalized, for Test Year 2007 the company is seeking \$ 3,157,000 for injury and damage insurance, while DRA would allow \$ 2,869,000. For property insurance, GSWC requests \$ 456,000, while DRA would allow \$ 382,300 (which includes zero for excess property insurance).

Basically, DRA is seeking a reduction of 11.69% n55 in most insurance categories because of what DRA characterizes as an apples-and-oranges comparison. DRA claims that when it compared the company's actual insurance costs for 2005 with those that had been budgeted, the former amount was 11.69% less. Using an escalation factor, DRA based its recommendation for GSWC's insurance costs in Test Year 2007 on the actual data for 2005.

n55 This is the percentage used by DRA in both its opening and reply briefs, based on corrections Aslam made during the hearing. (See DRA Opening Brief at 42; DRA Reply Brief at 7-8.) However, the settlement stipulation filed on August 4, 2006 states that DRA reduced GSWC's forecasted amount by 12.52%. (1 5.02.) Although it does not matter in view of our resolution of the issue, we assume the 11.69% figure is the correct one.

[*229]

However, in his rebuttal testimony, GSWC's Keith Switzer asserts that DRA has erred, because it ended up comparing the actual insurance costs for GSWC's 2004-2005 *fiscal* year (which ran from October 1, 2004 to September 30, 2005) with the insurance budget for *calendar* year 2005. (Ex. 13, pp. 38-39.) Switzer acknowledges, however, that if DRA had properly compared the amount budgeted for calendar year 2005 with the amount actually spent on insurance in calendar year 2005, the latter would have been about 8% lower. (*Id.* at 39.)

Switzer continues, however, that no reduction in what GSWC has requested is appropriate, because the company's request for Test Year 2007 is based upon a reasonable escalation of its actual insurance expenses for 2005:

Even if you accept DRA's basic premise that the 2005 recorded costs were 12.52 percent less than the 2005 budgeted costs, the Commission should not reduce GSWC's request for future year costs by the same 12.52 percent. The reason is that GSWC's request for year[s] 2006, 2007, and 2008 are not based on the 2005 budget, but rather are tied to the 2005 recorded costs. Thus, GSWC's request already incorporates and reflects the lower [*230] 2005 recorded costs, not the 2005 budget costs.

As shown in Mr. Brewer's testimony [Exhibit 5], the 2005/2006 budget is based on the 2004/2005 actual data plus adjustments for known or projected changes and inflation. Thus, the fact that 2005 recorded costs were less than budgeted has been carried forward into the future test years. A couple of examples will illustrate my point.

General Liability Insurance: As shown in the DRA workpaper [Exhibit 44], the 2005 budget amount for this coverage was \$ 303,000. The 2004/2005 actual cost shown in Mr. Brewer's Prepared Testimony was \$ 242,500. GSWC's budget for the 2006 transition year is \$ 247,000 and for the 2007 Test Year, GSWC requested [\$]255,398.

Umbrella Liability: As shown in the DRA workpaper, the 2005 budget amount for this coverage was \$ 733,000. The 2004/2005 actual costs shown in Mr. Brewer's Prepared Testimony was \$ 561,000. GSWC's budget for the 2006 transition year is \$ 562,000, and for the 2007 Test Year, GSWC requested \$ 581,108.

Fiduciary Liability Insurance: As shown in the DRA workpaper, the 2005 budget amount for this coverage was \$ 25,000. The 2004/2005 actual costs shown in Mr. Brewer's Prepared Testimony was [*231] \$ 10,500. GSWC's budget for the 2006 transition year is \$ 11,000, and for the 2007 Test Year, GSWC requested \$ 11,374. (*Id.* at 40-41.)

We have compared Exhibit 44 with the amounts for 2004/2005 and 2006 shown in Mr. Brewer's testimony (Ex. 5, Brewer, p. 5), and find Mr. Switzer's assertions to be accurate. In view of the fact that the actual results for the 2004/2005 insurance year are the foundation for the injury and damage insurance requests GSWC has made here for Test Year 2007, we agree with Switzer that no reduction is appropriate. Thus, we will allow GSWC the full "stipulated" amounts shown as the company's position for 2007 in P 5.02 of the August 4, 2006 stipulation between GSWC and DRA. n56

n56 As shown in the table that accompanies P 5.02 of the stipulation, GSWC and DRA reached a settlement with respect to the DM&A Administrative Fee, the Brokers Administrative fee paid to Marsh, and the loss reserve for workers compensation. We approve the settlement amounts shown for these items.

With respect [*232] to property insurance, DRA has recommended not only the 11.69% reduction explained above, but also a group of individual adjustments that Mr. Switzer discusses separately in his rebuttal testimony. We agree with Mr. Switzer that none of these individual adjustments are justified, and thus we will allow GSWC the full amounts for Test Year 2007 shown as the company's position in the "proposed" column in the table that accompanies P 5.03 of the August 4, 2006 stipulation.

9.5. Sales per Commercial Class Customer in Region II

Although the parties were able to reach a stipulation as to virtually all issues for Region II, they remain significantly apart on the forecasted usage for Region II commercial customers in Test Year 2007. As the prepared testimony and cross-examination show, the basis for this disagreement is the meaning of certain language in the "New Committee Method" and "Standard Practice No. U-25" and the supplement thereto, which the Rate Case Plan directs be used for such forecasting. GSWC's forecasted water use for commercial customers is 271.1 Ccf n57 per year, while DRA's is

279.9 Ccf per year. According to GSWC, the difference amounts to \$ 1.8 million in total operating [*233] revenues for each year. (GSWC Opening Brief, p. 1.)

n57 "Ccf" stands for 100 cubic feet of water.

In practical terms, the parties have reached these different positions because DRA concluded that under the applicable forecasting authorities, it was appropriate and proper to eliminate the data for two periods: (1) July 2001 to June 2002, which DRA considered to be an abnormally dry year, and (2) July 2004 to June 2005, which DRA considered to be an abnormally wet year.

In its rebuttal testimony (Exhibit 19) and briefs, GSWC argues that what DRA did was an unacceptable deviation from the New Committee Method and Standard Practice No. U-25 (as supplemented), as well as a statistically-improper way to conduct a regression analysis. As to the requirements of the Rate Case Plan, GSWC's opening brief states:

None of the changes DRA made are in keeping with the requirements of the Rate Case Plan. First, DRA removed the July 2001-June 2002 data on the ground that this period was the driest season in Los Angeles' history [*234] . . . However, under the new Rate Case Plan, DRA could only remove data if it occurred during a 'recognized drought period.' Examples in the Rate Case Plan of recognized drought periods are when sales restrictions like rationing are imposed[,] or when the Commission provides the utility with sales adjustment compensation like a drought memorandum account. Importantly, DRA admits that neither sales restrictions nor sales adjustment compensation was implemented during the July 2001-June 2002 period . . .

"Second, DRA removed the July 2004-June 2005 data on the ground that this period was the wettest season in Los Angeles' history . . . However, the Rate Case Plan does not provide for removing data for wet periods. Rather, the New Committee Method provides that rainfall in excess of four inches in a given month should be set at four inches in all the data used in the regression analysis [which GSWC states it did in its own analysis.] In that way, the data is adjusted to eliminate the impact of unusually wet months. Indeed, DRA followed the New Committee Method in all of its regressions and set rainfall at four inches in any month where actual rainfall exceeded that amount . . . (GSWC [*235] Opening Brief, pp. 2-3; citations omitted.)

GSWC also attacks the regression analysis that DRA conducted for replacing the two years of data that DRA removed with zeroes. On this question, GSWC states:

Moreover, the method DRA employed for removing data that it found to be objectionable and replaced that data with zeroes is inconsistent with basic regression analyses. Nowhere does the New Committee Method authorize replacing the data for usage, rainfall and temperature with zeroes in dry or wet years, as DRA has done. Merely replacing data with zeroes implies that the usage was zero, and there was no rain in that time period. Obviously, that makes no sense.

In addition, this technique of zeroing out real observations biased the results of DRA's model. Replacing the dependent and two of the independent variables with zeroes has the effect of artificially increasing the reliability measure of the regression . . . As shown in GSWC witness Adam Rue's rebuttal testimony, Exhibit 9, if GSWC added two years of zeroed data for usage, rain and temperature to its regressions, the resulting R-square value - which is a statistical measure that indicates the level of confidence in the [*236] results of the regression - exceeds the value DRA obtained... (*Id.* at 3-4; citations omitted.)

In its briefs, DRA does not take issue with GSWC's description of what it did in the regression analyses, but asserts that its adjustments are not forbidden under the Rate Case Plan, the New Committee Method, and Standard Practice No. U-25 as supplemented. (DRA Opening Brief, pp. 51-53; DRA Reply Brief, pp. 2-4.)

We agree with GSWC that DRA's approach of eliminating the 2001-2002 and 2004-2005 years, and then replacing the data for those years with zeroes, is not permissible under the approach adopted in the Rate Case Plan, nor is it consistent with correct statistical techniques. During the cross-examination of Victor Moon, DRA's witness, Mr. Moon could only point to his many years of experience as a justification for removing the years he considered abnormally dry and abnormally wet. However, even though experience is valuable, it is not a substitute for proper methodology when the authorities adopted for forecasting purposes in the Rate Case Plan - the New Committee Method and Standard Practice No. U-25 as supplemented - specify what constitutes a "recognized drought year," and also [*237] specify how the data for wet years is to be accounted for.

It is also clear that DRA's decision to replace the data for the omitted years with zeroes biased its regression analysis. Under recognized statistical techniques, DRA should have used only eight years of data to conduct its regression analysis, instead of the eight years of actual observations and two years of zeroes that it did employ.

In view of the errors in DRA's implementation of the forecasting methodology adopted in the Rate Case Plan, we will employ GSWC's forecast of 271.1 Ccf per year as the water usage of Region II commercial customers, rather than DRA's forecast of 279.9 Ccf per year.

9.6. Dividend Equivalent Rights

In P 5.04 of the August 4, 2006 stipulation, GSWC and DRA reached a settlement on most of their differences concerning pension and benefit issues for the general office. However, there are two issues on which the parties require a Commission decision: the propriety of dividend equivalent rights (DERs), and on what GSWC refers to as its Annual Incentive Bonus program.

It is important to note that these compensation programs affect different management levels within the company. According to Joel [*238] Dickson, who presented the company's case on both issues, all those with the title of manager are eligible for the Annual Incentive Bonus program. DERs, on the other hand, are restricted to officers; i.e., those with the title of vice president or above. (Ex. 11, p. 86.) For DERs, the company requests that \$ 406,100 be included in rates, while DRA advocates zero.

In his report for DRA, Aslam gives the following justification for his position:

Currently, the GSWC allows an additional compensation program in the form of Stock Option Compensation for its executives. However, in addition, GSWC also allows its executives to receive dividends while these stocks are not cashed in. GSWC failed to justify the reasonableness of imposing such an extra burden on ratepayers who are already paying for the high executive salaries and their stock options. Therefore, DRA recommends excluding these expenses from ratemaking calculations. The shareholders should bear the burden of these DER programs, which do not benefit the ratepayers. (Ex. 23, p. 2-42.)

In his testimony, Mr. Dickson disagrees with these assertions. He argues that that in order to attract and retain top executives, GSWC must offer [*239] competitive pay packages, and that DERs are part of an executive's total direct compensation. He also contends that according to a study he conducted comparing the total direct compensation of GSWC's five top executives with that of their peers at other, reasonably comparable water utilities, GSWC's compensation packages are just at the level they should be.

The results of Dickson's study are set forth in Exhibit 7 to his rebuttal testimony and are, he says, based upon "the compensation data used by GSWC's Board of Directors in their determination of executive pay." (Ex. 11, p. 83.) Dickson states that he assumed the larger the company, the larger the compensation it pays. He then describes the other assumptions behind his study:

The measurement of compensation I used to test this theory [of size versus compensation] was total direct compensation. Total direct compensation is defined as salary, bonus, and stock ownership through restricted stock or options *including DERs*. This is the most accurate measure of compensation for the peer group[,] as each Company may provide less compensation in the form of salary and more compensation in the form of options. Therefore any measure [*240] of compensation that does not include all direct compensation is a less accurate way of comparing relative compensation. *GSWC's use of DERs as compensation is included in the definition of total direct compensation.* (*Id.*; emphasis supplied.)

Dickson also looked at gross revenues, total assets and market capitalization for the utilities he considered comparable, and discovered that GSWC, which stood third with respect to each measure, was at the 71st percentile. He also ran a regression analysis which confirmed that for the five most highly-paid executives at each company, compensation was closely correlated with company size as measured by these three parameters. Dickson then plotted GSWC's compensation on charts to see where it ranked in relation to its size; i.e., at the 71st percentile. He continues:

If GSWC's total compensation on a position by position comparison were significantly above the 71st percentile, then it could be concluded that that GSWC executive compensation is [unacceptably] 'high'. What I found is that [it] plotted near the 71st percentile. In fact, [Table 4 of Exhibit 7] shows that in total for the five most highly compensated positions[,] GSWC is [*241] exactly at the 71st percentile. The conclusion is that Mr. Aslam is wrong and GSWC executive salaries are not high. The salaries are right in line with its peer group and it can be concluded that GSWC compensation is at market. (*Id.* at 84.)

Since Dickson's analysis was set forth in rebuttal testimony, Aslam did not have an opportunity to submit a written response to it, nor was he cross-examined on his own position. However, DRA's reply brief, while not taking issue with the specifics of Dickson's analysis, argues that he has failed to show "a direct correlation between a drop in compensation below market levels at GSWC has caused the loss[s] of 'key individuals.' The notion that GSWC would have a hard time finding or retaining employees that are already handsomely compensated lacks credibility." (DRA Reply Brief, pp. 36-37.)

After examining Dickson's testimony and the tables set forth in Exhibit 7 to his testimony, we find GSWC's analysis of the DER issue to be persuasive. We agree with Dickson that GSWC needs to offer competitive pay packages to attract and retain talented executives. We also agree with him that total direct compensation is a good measure for comparing compensation [*242] among executives. As Dickson notes, his study includes DERs within this measure. It is also apparent from the tables in Exhibit 7 to Dickson's testimony that among the water utilities with which it is most comparable, GSWC relies more on stock options and DERs and less on base salaries and bonuses to determine total direct compensation. (Ex. 11, Appendix 7, Tables 5-9, 11.) n58

n58 Among the eight companies Dickson surveyed - as measured by market capitalization, total revenues or total assets - GSWC's corporate parent, AWR, ranked third, behind California Water Service Company (Cal Water) and ahead of San Jose Water Company (SJW). It is noteworthy that among the five most highly-paid executives at these three companies, GSWC relies significantly more on stock options (including DERs) and less on salary and bonus than do Cal Water and SJW. Moreover, GSWC's five top executives receive a total of \$ 597,000 in stock options, DERs and restricted stock (which only the CEO receives), while the amount in controversy between GSWC and DRA in this case on the DER issue is \$ 406,100.

[*243]

Accordingly, we agree with Dickson's overall conclusion that the value of DERs included within GSWC's total direct compensation for executives is not unreasonable, does not constitute an "extra burden on ratepayers," and should be allowed in rates.

9.7. Annual Incentive Bonuses

As noted above, persons employed by GSWC who have attained the rank of manager are eligible for the Annual Incentive Bonus program. Under the terms of the August 4, 2006 stipulation between GSWC and DRA, the company would allow \$ 990,000 for this program, while DRA would allow zero.

In his rebuttal testimony, Mr. Dickson notes that managers are eligible for a bonus equal to 12.5% of their salary "if certain measurable outcomes are met." The program specifies eight measurable outcomes, and for each one that is met on a company-wide basis, "the manager can receive 1/8th of 12.5%." (Ex. 11, p. 85.) Dickson describes the eight measurable outcomes as follows:

Establishing a downward trend in the complaint-to-customer ratio for complaints reported to the CPUC or DHS as compared to the previous year;

Achieving the CPUC-adopted return on shareholder investment; Providing on average at least 20 hours of training [*244] per employee per year;

Improving communication and credibility of regional and district management by meeting with community leaders in the communities GSWC serves at least eight times per year for district managers and twice per year for all other regional management;

Maintaining operational and administrative costs no greater than the regulatory authorities' composite inflationary rate;

Maintaining a variance of not greater than 5% of CPUC-authorized operation and maintenance expenses and plant investment;

Pumping all water rights available and adhering to the annual energy resource plan in order to ensure the lowest supply costs possible;

Increasing leadership roles on industry boards, water district boards, AWWA committees and AWWARF research projects to cover basic areas of treatment, distribution, human resources and management, in order to keep abreast of best practices within the industry. (*Id.* at 85-86.)

Dickson argues that under the Annual Incentive Bonus program, "GSWC has provided incentives to its managers to perform in ways that keep costs down for customers. It is this group of managers that are tasked to live within the cost[s] adopted in the rate cases. [*245] Several of the measurable outcomes are tied directly to what comes out of the ratemaking process." (*Id.* at 86.)

In his report for DRA, Aslam opposes the Annual Incentive Bonus program, along with several others, on the ground that it needlessly burdens ratepayers:

GSWC's current salary levels are very competitive and for the most part are toward the higher end of the industry average. DRA already recommends the Discretionary Bonus program. However, any additional complementary compensation program will unfairly burden the ratepayers, and therefore, should be excluded from the ratemaking process. The shareholders [should] bear the burden for these complementary programs if the GSWC believes them useful. (Ex. 23, p. 2-42.)

We conclude that the Annual Incentive Bonus program should be funded only partly by ratepayers. As noted above, Dickson defends the program (which is apparently a new one) on the ground that "GSWC has provided incentives to its managers to perform in ways that keep costs down for customers." However, from an examination of the eight "measurable outcomes" Dickson sets forth, it seems clear that shareholders rather than ratepayers will be the principal beneficiaries [*246] of three of them (Outcome Nos. 2, 5 and 6). Under these circumstances, we believe ratepayers should be asked to fund only five-eighths (5/8) of the \$ 990,000 GSWC has requested for the program, or \$ 618,750.

9.8. DRA Computational Error

On page 16 of the stipulation between DRA and GSWC, in P 5.04, there is a notation that a dispute arose between the parties after hearings concerning the amount that should be allowed for "Management Initiatives, Succession Planning, and Training," which is considered a general office pension and benefits issue. GSWC believes the correct amount for this item should be \$ 353,000, while DRA asserts it should be \$ 247,300.

In GSWC's Opening Brief, the company explains the dispute as follows:

Both parties' forecasts were the result of the separate methodologies they applied to derive each of the 28 line items that comprise Pension and Benefits costs. Upon reviewing DRA's report, GSWC accepted DRA's recommendation for this item and did not submit rebuttal testimony.

Most of these line items have been settled by accepting DRA's estimate. DRA now wants to lower its recommendation . . . to the amount requested by GSWC. But to do so would not make [*247] sense.

DRA's recommended amount of \$ 353,000 was the result of its methodology, and is not believed to be in error. It's that same DRA methodology that produced DRA's recommendation for all the other line items, and the parties have settled by accepting DRA's numbers. DRA's recommendation for this line item should stand. (GSWC Opening Brief, pp. 43-44.)

In its reply brief, DRA urges us to ignore GSWC's argument on the ground this was an issue the ALJ was supposed to resolve at the "true-up" hearing scheduled for September 11-12, 2006. DRA states, however, that its \$ 353,000 recommendation was the result of "Mr. Aslam's proofreading error." (DRA Reply Brief, p. 39.)

For reasons explained in D.06-12-017, the true-up hearing was canceled, so we must now resolve the issue here. (D.06-12-017, *mimeo.* at 5.) For two reasons, we conclude that DRA should be bound by its original estimate of \$ 353,000, even if that estimate was in error. First, GSWC alleges and DRA does not dispute that the company relied on DRA's original forecast in settling most of the Pension and Benefit issues. Second, although it is not entirely clear from their testimony that Messrs. Dickson and Aslam are talking [*248] about the same issue presented here, the annual figure that both of them use for Management Initiatives, Succession Planning and Training in their respective discussions of whether the EDU should be retained - \$ 318,723 per year - is closer to DRA's original forecast here of \$ 353,000 than to the \$ 247,300 DRA is now advocating. (Ex. 23, p. 2-16; Ex. 11, pp. 74-75.) This suggests to us that the higher figure on which GSWC settled is not unreasonable.

In view of the many pension and benefit issues that GSWC settled using DRA's original forecast, we think it would be unreasonable to change now the number on which the parties settled the Management Initiatives, Succession Planning and Training issue.

9.9. When the General Office Case Should Be Filed

In their testimony and briefs, DRA and GSWC differed sharply over when the next general office general rate case (GRC) should be filed. GSWC contended that it would be more efficient to file the general office GRC along with its rate case for Region II, whereas DRA took the position that it made more sense to file the general office GRC along with the rate case for Region III, as specified in the Rate Case Plan. (*See, e.g.*, GSWC Opening [*249] Brief, p. 43; DRA Reply Brief, pp. 38-39.)

In view of the issuance of D.07-05-062, this issue is now moot. Under the Revised Rate Case Plan adopted in that decision, GSWC has been instructed to file its next general office GRC along with its rate cases for Regions II and III on July 1, 2008, and the next general office GRC after that on July 1, 2011. (*See* Appendix A, pp. A-17 to A-18.) n59

n59 At pages 17-24 of its opening comments on the PD, GSWC has raised various concerns relating to the PD's resolution of issues including the Annual Incentive Bonus Program, the recovery of the Low Income Program balance, and general office rent. To the extent they are not addressed in this decision, we find these concerns either to be without merit, or to be covered by provisions of the August 4, 2006 stipulation that are clear and essentially self-executing.

10. Categorization and Need for Hearing

In Resolution ALJ 176-3168, the Commission preliminarily determined the category of this proceeding to be rate-making, and [*250] that a hearing was necessary. In our opinion today, we affirm that categorization. As noted earlier in the text of this decision, hearings in this matter were held on June 26-30 and July 6, 11 and 12, 2006.

11. Comments on Proposed Decision

The proposed decision of the assigned ALJ and the alternate proposed decision of Commissioner Bohn in this matter were mailed to the parties in accordance with Section 311 of the Public Utilities Code and Rule 14.3 of the Commis-

sion's Rules of Practice and Procedure. Opening comments were filed on August 13, 2007, and reply comments were filed on August 20, 2007.

In response to these comments, we have substantially revised section 4.3.5 (dealing with the interim cost allocation methodology) and section 6.3 (which increases the fine to \$ 50,000). Other changes have also been made to the text where appropriate.

12. Assignment of Proceeding

John A. Bohn is the assigned Commissioner and A. Kirk McKenzie is the assigned ALJ in this proceeding.

Findings of Fact

1. On August 4, 2006, DRA and GSWC filed a motion to adopt a joint stipulation that resolves most of the issues between them concerning [*251] GSWC's Region II, and some of the issues between them relating to GSWC's general office operations.

2. The cost of capital set forth in P 10.04 of the August 4, 2006 stipulation, including the 10.1% return on equity, is reasonable and should be adopted.

3. The overhead rates and the methodology for refiguring them that are set forth in PP 2.01, 2.02 and 2.15 of the August 4, 2006 stipulation are reasonable and should be adopted.

4. The agreement between DRA and GSWC as to the general office pension and benefit expenses set forth in P 5.02 of the August 4, 2006 stipulation are reasonable and should be adopted.

5. Apart from the stipulated office expenses described in P 5.10 of the August 4, 2006 joint stipulation between GSWC and DRA (which should be rejected), the other agreements between GSWC and DRA set forth in said stipulation are reasonable and should be adopted.

6. The Commission should not accept DRA's recommendation that GSWC's general office revenue requirement be reduced by \$ 2,957,438 for each of the three years covered by this GRC due to "missed allocations" required by D.98-06-068, because (a) the \$ 101,300 revenue adjustment made by the Commission in D.04-03-039 was [*252] intended to serve as a proxy for the allocations that DRA contends should have occurred, and (b) in addition to this revenue adjustment, D.04-03-039 ordered GSWC to conduct a cost allocation study and present it in this general office GRC.

7. The Commission should not accept DRA's recommendation that 18.21% of GSWC's general office expenses that are not subject to being directly charged should be allocated to GSWC's non-regulated affiliates, because (a) such an approach would result in cost allocations well in excess of the revenues that these non-regulated affiliates generate, and (b) DRA did not consistently follow the four-factor cost allocation methodology the Commission has traditionally used, but instead added and subtracted allocation factors as DRA saw fit.

8. The Commission should not accept GSWC's recommendation to allocate nearly half of the company's costs that cannot be directly charged on the basis of single allocation factors, because, among other reasons, the Commission has rarely sanctioned the use of single allocation factors.

9. As a general rule, the Commission has departed from the traditional four-factor cost allocation methodology only where it is shown that [*253] use of the four-factor methodology would produce unreasonably skewed results in a particular case.

10. In D.03-05-078, the Commission approved the use of three allocation factors rather than four where it was demonstrated that using one of the traditional factors, the number of customers, would tend to shift an unreasonable share of the costs of the corporate parent of a water company onto the water company's ratepayers and away from its non-regulated affiliates.

11. The number of employees, which is the single factor GSWC proposes to use for allocating between itself and its affiliates, representing nearly 40% of the general office costs that cannot be charged directly, would produce skewed results in this case because, while GSWC's unregulated affiliates have few employees now, they are likely to experience significant growth in their operations and number of employees within the next few years.

12. Under the circumstances described in the preceding Finding of Fact (FOF), using the number of employees of GSWC and its affiliates as the sole determinant for allocating 40% of the company's general office costs would not present a fair picture of the demands that GSWC's unregulated [*254] affiliates are likely to place on the company's personnel.

13. In conducting its own cost allocation study, GSWC unreasonably assumed that its affiliate, ASUS, had only 11 customers, an assumption that is inconsistent with the approach the Commission approved in D.03-05-078.

14. In conducting its allocation study, DRA unreasonably assumed that ASUS had 74,270 customers, an assumption that is not justified in view of the wide variability of the Services furnished by ASUS to the entities with which it has contracts.

15. The cost allocation factors that should be used to allocate general office costs between GSWC and its affiliates in this case are (a) total labor costs, (b) total expenses, and (c) a number of customers that is appropriately weighted to reflect the Services that the entity being studied provides to its customers or clients.

16. It is reasonable to use total labor costs as a factor for allocating general office costs between GSWC and its affiliates because total labor costs reflect the nature and extent of the work actually performed for the entity under consideration, whoever the employer of the persons performing the work may be. Thus, using total labor costs gives a [*255] more accurate picture of the size of the enterprise being studied.

17. It is reasonable to use total expenses as a factor for allocating general office costs between GSWC and its affiliates because total expenses give a more accurate picture of the total work undertaken by the entity being studied, more illuminating than the entity's total revenue or gross plant.

18. A proper cost allocation study in this case must include a method for assigning to each of the entities with which GSWC's affiliate ASUS has a service contract, an assumed number of retail customers that is appropriately weighted to reflect the Services ASUS provides under the contract.

19. For contracts where ASUS is providing Services to a military base, it is appropriate to assume that each of the base's connections is equivalent to a full retail customer.

20. With respect to contracts where ASUS provides less-than-full utility Services, an appropriate weighted number of retail customers can be developed using the ratios that O&M expenses minus supply costs, A&G expenses, amortization and depreciation, and taxes paid by GSWC have borne to GSWC's net operating revenues (minus supply costs and costs of capital) in recent [*256] rate cases.

21. Table 3 of Attachment B sets forth appropriate O&M, A&G, Amortization and Depreciation, and Tax percentages to use in determining the appropriate weighted number of retail customers to assume for each non-military ASUS contract.

22. Table 2 of Attachment B sets forth the derivation of the appropriate weighted number of retail customers to assume for each ASUS contract with a non-military customer.

23. Using the three-factor cost allocation methodology described in FOF 15 to 22 above, Table 1 of Attachment B sets forth the percentages of GSWC general office expenses that should be allocated to GSWC and its various affiliates, in cases where a particular general office expense cannot be charged directly.

24. The CIS system that GSWC currently uses has significant limitations in terms of the programming language it uses, the documentation available for the system, the cost of making modifications to the system, and the time necessary for vendors to make such changes.

25. The CIS system that GSWC currently uses cannot be modified to meet modern business needs in a cost-effective manner, such as the need for mobile computing, Internet access to account information, knowledge [*257] management and data exchanges with other utilities.

26. The new CIS/CRM system for which GSWC seeks approval here would not be subject to the above limitations, and would offer advantages such as reducing training time for customer service representatives, lower vendor costs, and better control of business rule changes, including those related to SOX.

27. The \$ 9.1 million that GSWC is seeking here for the new CIS/CRM is only an estimate, based on what GSWC witness Andres describes as "standard high level pricing models of two independent vendor-consultants." More exact costs will not be available until GSWC issues an RFP in connection with the CIS/CRM system.

28. DRA opposes funding for the CIS/CRM system in this rate case because of the vagueness of GSWC's cost estimate, as well as concerns that the system will be used in large part to serve customers in GSWC's non-regulated businesses.

29. Because of the vagueness of GSWC's cost estimates for the proposed new CIS/CRM system, it is appropriate to approve only the \$ 2.983 million (before overheads) that the company proposes to spend in connection with the CIS/CRM system in 2006.

30. In order to recover any additional costs for the [*258] CIS/CRM system, GSWC should be required to file a Tier 3 advice letter that sets forth the additional information concerning use of the CIS/CRM system required by this decision.

31. GSWC contends that 11 factors have changed the regulatory landscape and significantly increased the general office workload in a way not suggested by normal customer growth, including (a) a large increase in infrastructure replacement, (b) the need to apply for low-cost financing under Proposition 50, (c) increasingly stringent and complex water quality standards, (d) an increased number of water quality lawsuits, (e) increased certification requirements for water system operators, which has made it more difficult to retain qualified personnel, (f) increased water company security requirements in the post 9/11 world, (g) new legislation requiring comprehensive urban water management plans and proof of water supplies to serve new housing projects, (h) increased water basin adjudication and management needs, (i) electric power procurement associated with BVEC, (j) new requirements on management and business procedures imposed by SOX, and (k) regulatory changes including the requirements of the Commission's [*259] new Rate Case Plan.

32. The new general office position of Senior Vice President-Operations is necessary due to the need for (a) senior management coordination of GSWC's geographically far-flung operations, (b) senior management oversight of the company's ambitious capital construction program and water supply planning, (c) proper implementation of new water quality rules and timely construction of new treatment facilities, and (d) compliance with SOX requirements by providing a review point and control structure for regional financial and capital projects accounting.

33. The new general office position of Capital Projects Manager-Operations is needed due to the large growth in GSWC's capital projects budget since 1996, and with it the commensurate need for a senior construction manager who can provide increased coordination in soliciting bids, scheduling work on the increased number of projects, and ensuring compliance with more complex engineering and permitting requirements. Regional management of construction projects within GSWC is no longer an optimal model.

34. The new general office position of Administrative Support Analyst-Operations is necessary due to the need to provide [*260] support on documentation and statistical analysis to the Capital Projects Manager.

35. The new general office position of Assistant Application Support Analyst-Operations is necessary due to the need to make efficient use of GSWC's new Project Control System, which includes software that tracks and generates reports on the status of capital projects, including project milestones, resources, budgets, costs, etc. At the present time, GSWC outsources this function.

36. The new general office position of General Clerk-Information Technology is necessary due to the need to process manually payments that GSWC is receiving in more varied forms than in the past, including through payment agencies, banks and financial institutions such as CheckFree and EPrinceton.com. This position may not be needed once the proposed new CIS/CRM system is on-line.

37. The new general office position of Assistant Information Technology Manager-Information Technology is necessary due to the need for an in-house security officer who can ensure the security of GSWC's hardware, software and data bases. At present, GSWC relies on outside contractors to provide these Services.

38. The new general office position [*261] of New System Administrator-Developer-Customer Service is necessary due to the need for an in-house capability to document change management and maintain the integrity of program code in the existing CIS system, and help with deployment of the proposed new CIS/CRM system.

39. Three new CSRs, a general office position, are needed due to the increase in the average amount of time that customer service calls require, the high turnover rate among temporary CSRs, the lower costs of hiring permanent CSRs rather than temporaries, and the need to maintain GSWC's current standard of scall response time.

40. The new general office position of Call Center Support Analyst is needed to free up the time of the Customer Service Supervisor so that he or she can focus on the training and coaching of GSWC's 24 CSRs.

41. The new general office position of Applications Support Manager-Applications Support is necessary due to the need for overall direction of the choice of software among GSWC's various departments and segments. At present, the company only has a Senior Applications Support Analyst, who works with departments to provide the departments with the software they want.

42. The new general office [*262] position of Communications, Media and Technical Generalist is necessary due to the need for an experienced employee in media communications who can help inform customers, communities and employees of GSWC concerning water conservation, low-income programs, and particular capital improvement projects, especially during high-profile media situations.

43. The new general office position of Corporate Communications Manager is not needed because GSWC already has ample experience with and means of communicating with its employees, customers and shareholders.

44. The MIS&T costs that GSWC incurs to train its senior management are separate and distinct from the Management Development costs the company's EDU incurs to train qualified entry-level supervisors for the company.

45. Because of GSWC's company size and geographic diversity, it would incur substantial AWWA costs whether or not the EDU existed.

46. DRA's critique of the EDU's cost-effectiveness takes into account only the costs of developing and presenting classes, and leaves out the costs of making needs assessments, following up to be sure that training is properly applied, and evaluating whether particular training classes are effective. [*263]

47. Turning to outside vendors for training rather than having the EDU would not be cost-effective for GSWC, because no single vendor or group of vendors offers all of the courses that the company needs and EDU provides.

48. It is doubtful that any outside vendor would offer some of the courses that GSWC needs for some of its prospective employees, including courses in basic technical writing and basic mathematics.

49. DRA has failed to demonstrate that the EDU program is not a cost-effective way of providing the training and courses that EDU provides.

50. The new general office position of EDU Facilitator-Instructor is necessary due to the need to provide continuing education and training in the technical areas of water operations and management, which requires skills in engineering, management, teaching and curriculum design and development in addition to substantive technical knowledge on water, environmental, and health and safety issues.

51. The new general office position of EDU Support Analyst is necessary due to the expanded administrative responsibilities within EDU that this position will perform, including management of a comprehensive data base with employee information [*264] concerning safety, annual training, tuition reimbursement, operator certification records with the California DHS, and SOX compliance.

52. GSWC has not demonstrated that the general office position of EDU Senior Employee Development Specialist, which is currently a half-time position, needs to be authorized as a full-time position to comply with SOX requirements. If GSWC still wishes to, make this a full-time position, it should present a full justification for doing so in the company's next general office GRC.

53. The new general office position of Associate Rate Analyst is needed due to the increased filing requirements and milestones for rate cases adopted by the Commission in D.04-06-018, as revised in D.07-05-062. This position will be in GSWC's Regulatory Affairs Department, which has not increased in headcount since 1996.

54. The new general office position of EPRP Coordinator is necessary due to the need under the PHBR Act to keep emergency response plans for water utilities updated and to provide table top training sessions concerning them. GSWC's existing Safety Specialist and Regional Managers do not have the time or training to meet these requirements.

55. The Commission [*265] specifically warned GSWC in D.04-03-039 that it was not permissible to wait until the submission of rebuttal testimony to present the main justification for significant new proposals.

56. The principal justification for many of the new general office positions discussed in FOF 32-54 was not set forth by GSWC until the company submitted its rebuttal testimony on June 9, 2006.

57. DRA propounded 92 data requests to GSWC on June 16, 2006, in connection with the company's rebuttal testimony. Responses to many of these data requests were received on June 24, 2006, two days before hearings were scheduled to begin.

58. No litigation team the size of DRA's in this case could reasonably be expected to digest and work into proposed cross-examination the volume of data responses that GSWC delivered to DRA on June 23-24, 2006.

59. Under the schedule the parties had agreed upon for this rate case, the filing of surrebuttal testimony was not a reasonable option for DRA.

60. DRA was prejudiced in its preparation for cross-examination of GSWC's witnesses by the company's actions in withholding until rebuttal testimony the detailed justification for many of the requested new positions, and by responding [*266] to DRA's data requests such a short time before hearings were scheduled to begin.

61. In view of the prejudice to DRA described above, it is reasonable to conclude that DRA's cross-examination of GSWC's witnesses was not as effective as it might otherwise have been.

62. In a Commission GRC, the burden is on the utility to prove that it is entitled to rate relief, and not upon the Commission, the Commission's staff or interested parties to prove that the utility is not entitled to such relief.

63. In various decisions over the years, the Commission has admonished utilities besides GSWC that it is improper to withhold the principal justification for new proposals until the submission of rebuttal testimony.

64. We are approving some of the positions described in FOFs 32-42, 44-51 and 53-54 despite lingering doubts about the need for some of these positions.

65. In light of the factors set forth in FOFs 55-64, it is appropriate to fine GSWC for the previously described violations pursuant to our authority under Public Utilities Code Sections 2107 and 2108.

66. The new general office position of Vice President [*267] of Finance, Treasurer and Assistant Secretary is needed largely to enable GSWC to comply with the requirements of SOX, including (a) supervision of the detailed work needed to ensure that GSWC's CEO and CFO can certify the company's financial statements as required by SOX § 302, (b) assessing 16 mega accounting processes and 250 key controls so that GSWC's management can certify the effectiveness of its internal controls as required by SOX § 404, and (c) ensuring company compliance with SEC rules so that the CEO and CFO can provide the certification required by SOX § 906. In addition, the Vice President of Finance, Treasurer and Assistant Secretary oversees the company's financing needs and tax compliance and serves as a liaison between the departments that handle GSWC's accounting and regulatory affairs.

67. The new general office position of Tax Manager is needed to facilitate GSWC's compliance with SOX, including the need to avoid having to restate the company's financial results, as GSWC was required to do for the years 2000 and 2001. Public utilities like GSWC normally have Tax Managers, and the company's Controller does not have the necessary tax expertise. Even though the Tax [*268] Manager position was created at GSWC in 2002, before the passage of SOX, it is now needed largely to ensure compliance with SOX and avoid restatements, the vast majority of which are now due to tax errors.

68. The new general office position of Financial Reporting Supervisor is needed due to the reorganization of the Controller's Department, with one supervisor responsible only for utility plant and the other responsible for all other aspects of financial reporting.

69. The new general office position of Accountant, an entry-level position, is needed due to the general increase in workload of GSWC's Financial Reporting Group, and in particular with GSWC's need for more timely monthly bank reconciliations, which are a key internal control for SOX § 404 purposes.

70. The new general office position of Internal Auditor, a junior-level position, is needed due to GSWC's increased emphasis on risk management and the increased workload created by the requirements of SOX § 404. This position will report to the Internal Audit Manager, who in turns reports to the Audit Committee of GSWC's Board of Directors.

71. DRA has not shown that in A.02-11-007, it requested any information concerning [*269] any of the following positions that were included within GSWC's total general office labor costs in that proceeding: System Programmer, Risk Manager, Senior HR Specialist, CIS Billing Specialist, Assistant Applications Support Analyst, Senior Financial Analyst, Financial Analyst, and Senior Auditor.

72. GSWC's methodology for estimating its general office miscellaneous expenses is superior to that of DRA, and the dues GSWC proposes to pay to NAWC, CFEE, and ACE are reasonable.

73. Part of GSWC's need for more office space for general office purposes appears to be attributable to the growth in the company's non-regulated businesses.

74. The increase in restaurant prices in recent years means that using a five-year average of meal expenses to forecast meal expenses for 2007 will understate the reasonable amount of such expenses.

75. GSWC used its actual insurance expenses for the fiscal year running from October 1, 2004 to September 30, 2005, and then escalated these expenses, to arrive at its forecasts of injury, property and damage insurance for Test Year 2007.

76. GSWC's estimates of injury, property and damage insurance for Test Year 2007 are reasonable.

77. DRA's estimate of GSWC's [*270] injury, property and damage insurance expense for Test Year 2007 is unreasonable.

78. Under the New Committee Method and Standard Practice No. U-25 as supplemented, which were adopted in D.04-06-018 for water consumption forecasting purposes, it was not permissible for DRA to remove from the 10 years of data that it studied for estimating the consumption of GSWC's Region II commercial customers, the data for years running from July 2001 to June 2002 and July 2004 to June 2005.

79. Under generally-accepted standards for running regression analyses, it was not acceptable for DRA to replace the data for the two years described in the foregoing FOF with zeroes. Instead, it would have been proper for DRA to have run the regression analysis using only the eight years of data that DRA considered valid.

80. Total direct compensation, which consists of salary, bonus, and stock ownership through restricted stock or stock options that include DERs, are a good measure for comparing executive compensation from one water utility to another.

81. The study conducted by Joel Dickson demonstrates that in determining total direct compensation for its senior executives, GSWC places more reliance on stock [*271] options and DERS and less on salary and bonus than do other comparable water utilities.

82. When measured by market capitalization, gross revenues or total assets, GSWC ranks at the 71st percentile of the water utilities Dickson studied.

83. GSWC's total direct compensation for its senior executives as a group ranks at the 71st percentile of the group of water utilities that Dickson studied

84. The expense for DERs that GSWC included in its estimate of general office pension and benefit expense for Test Year 2007 is reasonable.

85. Only five of the eight criteria that GSWC uses to award bonuses to managers under its proposed Annual Incentive Bonus program directly benefit GSWC's ratepayers; the other three criteria benefit mainly the company's shareholders.

86. GSWC settled most of its contested general office pension and benefit issues with DRA, and chose not to submit rebuttal testimony on these issues, in reliance upon DRA's forecast of the pension and benefit expenses.

87. In D.07-05-062, the Commission revised the Rate Case Plan to provide, among other things, that GSWC should file its next general office GRC along with its GRCs for Regions II and III on July 1, 2008.

Conclusions [*272] of Law

1. Apart from the allocation of expenses set forth in 5.10 of the August 4, 2006 stipulation, the terms of that stipulation are reasonable, consistent with law and in the public interest, and should therefore be adopted.

2. The stipulation concerning certain office expenses set forth in 5.10 of the August 4, 2006 stipulation should be rejected.

3. The percentages set forth in Table 1 of Attachment B should be used to allocate, as between GSWC and its affiliates, general office expenses that cannot be charged directly to a particular entity.

4. In order to recover any additional costs for the CIS/CRM system beyond the \$ 2.983 million authorized in this decision, GSWC should be required to file a Tier 3 advice letter in which it demonstrates that (a) the new system is designed principally to meet the needs of GSWC's customers, (b) any excess capacity in the system is designed to allow for growth in the number of such customers plus any additional applications GSWC's customers may need during the useful life of the new CIS/CRM system, and (c) GSWC has developed an adequate methodology for charging to GSWC's affiliates a share of the CIS/CRM system's total costs (including overheads) [*273] that is fully proportionate to the demands these affiliates place upon the CIS/CRM system while it still has excess capacity to serve these affiliates.

5. The following new general office positions requested by GSWC should be authorized for inclusion in rates: (a) Senior Vice President-Operations, (b) Capital Projects Manager-Operations, (c) Administrative Support Analyst-Operations, (d) Assistant Application Support Analyst-Operations, (e) General Clerk-Information Technology, (f) Assistant Information Technology Manager-Information Technology, (g) New System Administrator-Developer-Customer Service, (h) three Customer Service Representatives, (i) Applications Support Manager-Applications Support, (j) Communications, Media and Technical Generalist, (k) EDU Facilitator-Instructor, (l) EDU Support Analyst, (m) Associate Rate Analyst, (n) EPRP Coordinator, (o) Internal Auditor, (p) Vice President of Finance, Treasurer and Assistant Secretary, (q) Tax Manager, (r) Financial Reporting Supervisor, and (s) Accountant.

6. Sixty-nine percent (69%) of the salary and benefits for the new general office position of Call Center Support Analyst should be authorized for inclusion in rates.

7. GSWC [*274] should not be authorized to include the salary and benefits of the proposed Corporate Communications Manager in rates.

8. DRA's recommendation to dissolve GSWC's EDU and transfer its Dean and Senior Employee Development Specialist to the company's Human Resources Department should be rejected.

9. GSWC should not be authorized to make the EDU Senior Employee Development Specialist, which is currently a half-time general office position for rate purposes, into a full-time general office position.

10. Because DRA did not request any information in A.02-11-007 concerning the following positions included within GSWC's total general office labor costs in that proceeding, DRA's recommendation to disallow these positions in this rate case should be rejected: System Programmer, Risk Manager, Senior HR Specialist, CIS Billing Specialist, Assistant Applications Support Analyst, Senior Financial Analyst, Financial Analyst, and Senior Auditor.

11. GSWC should be authorized to include \$ 2,009,400 in general office rates for miscellaneous expenses in 2007, consistent with the estimate set forth in 5.08 of the August 4, 2006 stipulation between GSWC and DRA.

12. GSWC should be authorized to include [*275] \$ 184,725 in general office rates for general office rental expenses in 2007, which is 75% of the amount shown as GSWC's request in 5.12 of the August 4, 2006 stipulation between GSWC and DRA.

13. In place of the figures set forth in P 5.05 of the August 4, 2006 stipulation between GSWC and DRA, the company should be authorized to include \$ 82,500 in rates as the reasonable cost of general office meal expenses for 2007.

14. DRA's proposed individual adjustments to GSWC's property damage estimate for 2007 are unreasonable and should be rejected.

15. GSWC should be authorized to include in rates its estimates for injury, property and damage insurance for Test Year 2007 shown in 5.02 of the August 4, 2006 stipulation between GSWC and DRA.

16. Because of DRA's unreasonable decision to eliminate two years of data and run its regression analysis with eight years of actual data and two years-worth of zeroes, GSWC's forecast of 271.1 Ccf per year of water usage for commercial customers in Region II should be adopted.

17. GSWC should be authorized to include in rates its estimate of general office DER expense for Test Year 2007.

18. GSWC should be authorized to include \$ 618,750 in rates for [*276] its proposed Annual Incentive Bonus program, which is five-eighths (5/8) of the amount the company proposed and that is set forth in P 5.04 of the August 4, 2006 stipulation between GSWC and DRA.

19. In view of GSWC's reliance upon it and decision to forego the submission of rebuttal testimony based upon it, DRA's original estimate of \$ 353,000 as the pension and benefit expense attributable to GSWC's Management Initiatives, Succession Planning and Training program should be used, even if that estimate was the result of an arithmetic error.

20. In view of the schedule for the Revised Water Rate Case Plan adopted by the Commission in D.07-05-062, the issue between DRA and GSWC as to when the latter should be required to file its general office GRC is now moot.

21. Pursuant to Public Utilities Code Section 2108, GSWC's failure to disclose until rebuttal testimony its justification for at least 10 of the 20 new general office positions is considered a separate offense, for a total of 10 offenses.

22. Pursuant to Public Utilities Code Section 2107, the Commission may fine GSWC anywhere in the range of [*277] \$ 5,000 to \$ 200,000 for its failure to disclose until rebuttal testimony its justification for requesting at least half of the 20 new general office positions.

23. The ALJ Ruling denying DRA Motion to Strike, issued July 12, 2006, should be affirmed.

24. Pursuant to paragraph 9 of the July 26, 2005 stipulation between SCWC and DRA, which stipulation was approved in D.06-01-025 and attached thereto as Appendix B, GSWC should be authorized to include in its Region III rates for Escalation Years 2007 and 2008, the 39.49% share of general office costs attributable to Region III found reasonable in this decision. Such share should be determined after proper allocations of general office costs have first been made to ASUS, CCWC and BVEC in the manner directed by this decision.

25. Pursuant to paragraph 2.15 of the August 4, 2006 stipulation between GSWC and DRA, GSWC should be authorized to develop, in consultation with DRA, a methodology to allocate the balance of the Overhead Pool Account, whether negative or positive, to work orders at the end of each year. The objective of this methodology should be to achieve a zeroing out of the Overhead Pool Account. Such methodology should allocate [*278] the balance on the Overhead Pool Account to jobs in all three of GSWC's regions. The methodology thus developed should not be implemented without the prior approval of DRA, and shall remain in effect only for the three years covered by this rate case cycle.

ORDER

IT IS ORDERED that:

1. The earnings and rates for Test Year 2007 calculated in conformance with this decision, as set forth in Attachment C to this decision, are authorized. Golden State Water Company (GSWC) is authorized to file, in accordance with General Order (GO) 96-B, and to make effective on no less than five days' advance notice, a tariff containing the Test Year 2007 increase as provided in this decision. Consistent with Decision (D.) 06-12-017, these revised rates shall be deemed effective as of January 1, 2007, and shall be adjusted upward or downward to conform with the provisions of D.06-12-017.

2. Subject to pro forma tests after the 2007 increases are effective, GSWC is authorized to file in accordance with GO 96-B, and to make effective on not less than five days' advance notice, a tariff setting rates for years 2008 and 2009, calculated in conformance with this decision. The revised rates shall apply [*279] to service rendered on and after the effective date.

3. Except for the amounts set forth in Paragraph 5.10 thereof, the terms of the Joint Stipulation filed by GSWC and the Division of Ratepayer Advocates (DRA) on August 4, 2006, which stipulation is annexed to this decision as Attachment A, are adopted.

4. The terms of Paragraph 5.10 of the Joint Stipulation filed by GSWC and DRA on August 4, 2006 are rejected.

5. Pursuant to Paragraph 2.15 of the Joint Stipulation filed by GSWC and DRA on August 4, 2006, the following overhead rates for capital budget items should be used instead of the rates set forth in Paragraph 2.01 of said Joint Stipulation: 24.73% in 2006, 26.12% in 2007, and 26.37% in 2008.

6. For the purpose of allocating general office costs that are not susceptible to being directly allocated, GSWC shall use the allocation factors set forth in Table 1 of Attachment B to this decision, as well as the cost allocation methodology set forth in this decision.

7. By this decision, GSWC is authorized to spend no more than \$ 2,982,841.00 (before overheads) for the purpose of beginning the acquisition and implementation of the proposed new Customer Information/Customer Relationship [*280] Management (CIS/CRM) system. In order to recover any additional amounts for the CIS/CRM system, GSWC shall be required to submit a Tier 3 advice letter as set forth in GO 96-B that satisfies the criteria set forth in COL 4.

8. GSWC is authorized to include in rates, the salaries, benefits and related overheads of the new general office positions enumerated in COL 5 and 6 of this decision.

9. GSWC may continue to include in rates the following general office positions, which were part of the general office labor increase approved by the Commission in D.04-03-039: System Programmer, Risk Manager, Senior HR Specialist, CIS Billing Specialist, Assistant Applications Support Analyst, Senior Financial Analyst, Financial Analyst, and Senior Auditor.

10. GSWC is authorized to include in rates, the amounts allowed in COL 11 through 19 of this decision with respect to the miscellaneous issues on which GSWC and DRA were not able to reach a stipulation.

11. We intend to fine GSWC \$ 50,000, payable to the General Fund.

12. We direct Water Division to issue an Order to Show Cause for Commission consideration within 60 days of the effective date of this decision as to why GSWC should not be fined [*281] \$ 50,000 for its conduct in this proceeding.

13. We direct Water Division to prosecute this Order to Show Cause.

14. Issues considered in the Order to Show Cause shall be considered adjudicatory and thus subject to a ban on *ex parte* communications.

15. The Administrative Law Judge's Ruling Denying Motion of Division of Ratepayer Advocates to Strike Rebuttal testimony, issued on July 12, 2006 in this proceeding, is affirmed.

16. Volumes 4 and 5 of the February 2006 General Office workpapers that GSWC submitted along with its application in this proceeding are admitted into the evidence as Exhibits 63 and 64, respectively.

17. Exhibits 63 and 64, which were submitted under seal along with the application as part of GSWC's General Office Workpapers in February 2006, shall remain under seal through December 31, 2009, and during that period shall not be made accessible or disclosed to anyone other than the Commission staff except on further order of the Commission, the assigned Commissioner, the assigned Administrative Law Judge, or the Administrative Law Judge designated as Law and Motion Judge. If GSWC believes that further protection of all or part of the information in Exhibits 63 [*282] and 64 is needed after December 31, 2009, then GSWC shall file a motion stating the justification for further withholding of such material from public inspection, or for such other relief as the Commission's rules may then provide. Such a motion shall explain with specificity why the designated materials still need protection in light of the passage of time involved, and shall attach a clearly-identified copy of the relevant ordering paragraphs of this decision to the motion. Such motion shall be filed no later than 30 days before the expiration of this protective order.

18. In compliance with COL 24 of this decision, GSWC shall include in its Region III rates for Escalation years 2007 and 2008, the 39.49% share of the general office costs for Region III approved in this decision.

19. GSWC shall develop, in a manner consistent with the requirements of COL 25, a methodology for allocating the balance in the Overhead Pool Account among the jobs in GSWC's three regions.

20. Application 06-02-023 is closed.

This order is effective today.

Dated November 16, 2007, at San Francisco, California.

MICHAEL R. PEEVEY

President

DIAN M. GRUENEICH

JOHN A. BOHN

RACHELLE B. CHONG

TIMOTHY ALAN SIMON [*283]

Commissioners

ATTACHMENT A

JOINT MOTION TO ADOPT STIPULATION

The Division of Ratepayer Advocates (DRA) of the California Public Utilities Commission (Commission) and applicant, Golden State Water Company (GSWC) (collectively, the "Parties"), have agreed on a resolution of various issues in this proceeding, as set forth in the, attached Stipulation. The Parties hereby submit the Stipulation for approval and adoption pursuant to Rule 51 *et seq.* of the Commission's Rules of Practice and Procedure.

The Parties represent to the Commission that, pursuant to Rule 51.1(b), prior to entering into the Stipulation, the Parties convened a settlement conference on June 14 and 15, 2006, with notice and opportunity to participate provided to all parties, for the purpose of discussing settlement of the issues in this proceeding. Representatives of DRA and GSWC attended and participated in the settlement conference.

The Parties represent to the Commission that the Stipulation commands the sponsorship of two of the three parties to this proceeding - DRA and GSWC. The City of Claremont is not a party to the Stipulation. The Parties further represent to the Commission that they are fairly [*284] representative of all affected interests in this proceeding, that no term of this Stipulation contravenes any statutory provision or any decision of the Commission, and that the Stipulation, together with the record in this proceeding, conveys to the Commission sufficient information to permit the Commission to discharge its regulatory obligations with respect to the parties and their interests.

The Parties believe that the Stipulation is fair and reasonable in light of the whole record, consistent with applicable law, and in the public interest. For all of the above reasons, the Parties request that the Commission adopt the attached Stipulation in its entirety.

Dated: August 4, 2006

Respectfully submitted,

GOLDEN STATE WATER COMPANY

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Attorneys for Applicant

Golden State Water Company

Dated: August 4, 2006

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STIPULATION

1.00 Introduction

1.01 This Stipulation resolves a portion of the issues in the general rate case (GRC) application of the Golden State Water Company (GSWC) (U133W) for an increase in its general rates for water service in its Region II Service Area and to update its General Office expenses and rate base, A. 06-02-023, pursuant to the description of the issues that are settled as set forth in the Hearing Transcript (Hr'g Tr.), vol 3, 209 et seq., and Exhibits 1 and 2 thereof.

1.02 The Parties to this Stipulation are. GSWC and the Division of Ratepayer Advocates (DRA) of the Commission, collectively referred to as the "Parties."

1.03 DRA reviewed GSWC's GC application, which was formally filed on February 14, 2006; made field tours of the water system, and appeared at Public Participation Hearings held in Placentia and Gardena. On May 25, 2007, DRA filed its "Report on the Results of Operations"; "Report on the General Office and Region II Headquarters", and "Report on the Cost of Capital". On several occasions beginning on June 14, 2007, the [*286] Parties met and conferred. The Parties' stipulations are set forth in following pages:

1.04 Attached are the following appendices:

Appendix A -- Comparative Summary of Earnings

Appendix B -- Region II Capital Budgets

Appendix C -- General Office Capital Budgets

1.05 The Parties agree that neither signatory to this Stipulation nor any employee of DRA or GSWC assumes any personal liability as a result of this Stipulation. The Parties agree that no legal action involving any matter related to this Stipulation may be brought in any state or federal court or in any other legal forum against any individual signatory or employee representing the interests of the Parties, any attorney representing the Parties, or the Parties themselves. Any interpretation of this Stipulation, including all rights and remedies of the Parties, shall be decided by the Commission.

2.00 Plant

2.01 Region II Plant Additions

GSWC and DRA have resolved all of the differences regarding plant additions in GSWC's Region II. It should be noted that the issue of amount of overhead to be applied to the capital budget will not be finally determined until all of the litigated items have been resolved [*287] and the Commission has adopted the Parties' jointly proposed Stipulation. The stipulated capital budgets attached as Appendix 13 reflect the overhead rates that GSWC requested, 21.8% in 2006, 24.9% in 2007 & 22.1% in 2008.

2.02 General Office Plant Additions

GSWC and DRA have resolved 'the following differences regarding plant additions in GSM's General Office. It should be noted that the issue of amount of overhead to be applied to the capital budget will not be finally determined until all of the litigated items have been resolved and the Commission has adopted the Parties' jointly proposed Stipulation. The stipulated items shown in the following table reflect the overhead rates that GSWC requested, 21.8% in 2006, 24.9% in 2007 & 22.1% in 2008:

2006 Plant Additions

Description	Department	GSWC	DRA	Stipulation
Workstations (10) -	ACCT/FINANCE	17,100	11,400	11,400
Replacements w/monitor	ACCT/FINANCE			
New Workstations	ACCT/FINANCE	5,100	0	0
(3) - Financial				
Analyst/Financial				
Mgr/Tax Analyst				
Desktop (6) Printers	ACCT/FINANCE	6,700	2,233	2,233
Replacement and (3) New				
for new employees				
Furniture Replacement	ACCT/FINANCE	6,200	0	0
Ph. 1 - Integrated	CONSERVATION	44,800	0	0
Conservation Database				
Replace PCs (25)	CSC	42,700	17,649	17,649
Ratite & Refixture	INFO. TECH.	58,000	0	0
2 Bathrooms				
Replace Counter Tops in	INFO. TECH.	7,900	0	0
Cafeteria, Mail area				
BancTec Cash Processing	INFO. TECH.	357,900	0	0
Unit w/imaging				
Desk with return and	PREVENTIVE MAINT	3,100	0	2,400
Credenza (1) Manager				
High Back Task	PREVENTIVE MAINT	2,600	0	2,000
Chairs (2)				
PC Workstations	PREVENTIVE MAINT	1,700	0	1,300
Replacement				
w/monitor (1)				
New 5-drawer &	PREVENTIVE MAINT	2,400	0	1,900
2-drawer lateral files				
Table with base	PREVENTIVE MAINT	3,100	0	2,400
and chairs				
Safety and Testing	RISK MANAGEMENT	28,000	5,700	14,000
Equipment				
GPS for Company	SECURITY	217,600	0	72,500
Vehicles				
Furniture Replacement	WATER QLTY.	13,400	0	0
- VP Water Quality				
Auto Replacement -	INFO. TECH.	39,000	0	39,000
2000 Windstar Pool Van				
[*288]				

2007 Plant Additions

Description	Department	GSWC	DRA	Stipulation
Workstations (10) -	ACCT/FINANCE	17,800	11,867	11,867
Replacements w/monitor				
Furniture Replacement	ACCT/FINANCE	4,300	0	0

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2007 Plant Additions

Description	Department	GSWC	DRA	Stipulation
Enterprise One - Additional Web Modules Upgrade	ACCT/FINANCE	68,700	0	34,350
ShowCase Vista - Software upgrade	ACCT/FINANCE	28,500	14,250	14,250
EAM Graphical Interface Enhancement	ACCT/FINANCE	62,500	0	31,250
Ph. 2 - Expansion of Intergrated Conservation Database	CONSERVATION	101,400	0	0
Retile & Refixture 2 Bathrooms	INFO. TECH.	60,500	0	0
Replace Cafeteria Furniture	INFO. TECH.	5,700	0	0
Replace 12 year old Office Furniture	INFO. TECH.	27,100	0	0
Laser Printer/fax/scanner/copier	PREVENTIVE MAINT	5,100	0	0
Safety and Testing Equipment	RISK MANAGEMENT	20,900	5,700	10,450
Compliance Software - Phase 1	WATER QLTY.	27,000	0	27,000
GPS for Company Vehicles	SECURITY	0	0	74,400
Auto Replacement 2002 WS Pool Van	INFO. TECH.	40,700	0	0

2008 Plant Additions

DESCRIPTION	DEPARTMENT	GSWC	DRA	Stipulation
Workstations (10) - Replacements w/monitor	ACCT/FINANCE	17,800	11,867	11,867
Enterprise One - Software Upgrade	ACCT/FINANCE	67,200	33,600	33,600
HR Self Service enhancement	ACCT/FINANCE	61,100	30,550	30,550
Web Server (3) Upgrade	ACCT/FINANCE	30,400	0	15,200
Ph. 3 - Integrated Conservation Database	CONSERVATION	132,200	0	0
Replace 5 Workstations	INFO. TECH.	8,900	0	0
Safety and Testing Equipment	RISK MANAGEMENT	12,500	5,700	6,250
Compliance Software - Phase 2	WATER QLTY.	26,400	0	0
GPS for Company Vehicles	SECURITY	0	0	72,700

[*289]

2.03 General Office Plant Additions Still At Issue -- Parties agree that the need for certain capital projects that are directly related to the General Office labor positions still at issue in this rate case, should be resolved as discussed below.

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2.04 Customer Service Center -- Parties agree that if the Commission approves the addition of three customer service representatives in GSWC's Customer Service Center then the following capital additions and their costs indicated below should also be included in rates:

2006	Office Space for new Workstations	71,600

2.05 Employee Development University -- Parties agree that if the Commission approves the inclusion of the Employee Development University in rates then the following capital additions and their costs indicated below should also be included in rates:

2006	E-Learning Hosted on Internet (Harvard or E-Comell)	39,400
2006	(2) Videoconference Systems (Bear Valley & Santa Maria)	26,700
2006	Develop/Purchase new training modules	26,000
2006	Laptop PC for EDU staff Off-site training replacement	3,600
2006	Adobe Creative Suites for EDU Staff PCs	4,800
2006	25 Classroom chairs replacement (G.O.)	12,700
2006	Staff PC replacements (3)	7,700
2006	Training videos to augment classroom learning (5)	6,400
2006	Database replacement PC	2,600
2007	E-Leaming Hosted on Internet (Harvard or E-Cornell)	41,100
2007	Develop/purchase new training modules	29,400
2007	Online topics (electronic job aids) for field operations	34,500
2007	LCD Projector& Computer (Region II) Replacement	31,700
	PC Lab & Training Room	
2007	Staff PC replacements (3)	8,100
2007	Training Videos (5)	7,400
2007	Printer for PC Lab (Region II)	2,600
2007	Document scanner w/feeder for Dean	2,400
2007	Career Development Online System	69,300
2008	E-learning Hosted on the Internet (Harvard and other vendors)	36,800
2008	Curriculum Development (Purchase/Development costs for Management and Operations Coursework)	59,400
2008	Replacement of EDU Portable LCD Projector for offsite training	6,600
2008	Video capture and editing software package	5,700
2008	Staff PC replacements (3)	8,100
2008	Training videos to augment classroom learning (5)	7,000
2008	Printers for training rooms and EDU common area (3)	3,200
2008	Region III training room tables and chairs replacement	44,200
2008	Handheld digital video camera	2,900
2008	Portable Easels for Classroom (3)	3,400
2008	Ergonomic Chairs for EDU Staff (3)	2,900
2008	Upgrade Videoconference systems for G.O. and Region I	27,800

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2.06 Capital Projects Department -- Parties agree that if the Commission approves the addition of the Capital Projects Department in rates then the following capital additions and their costs as indicated below should also be included in rates:

2006	Digital Overhead Projector	1,900
2006	Four (4) 4-drawer Lateral File Cabinets	4,500

2006	Primavera SureTrak Project Manager Software	22,200
2006	Digital camera	2,100
2006	Task Chairs (2)	1,100
2006	Workstation (1) - Replacement	1,700
2006	Auto Replacement - Replace vehicle # 1100	34,500
2007	Desk with return & credenza - Replacement	3,200
2007	Lateral file cabinets (4)	4,600
2007	Workstation (1)	1,800
2007	Desk & task chair	600
2008	Laptop PCs (2)	6,700

2.07 Human Resources Department -- Parties agree that if the Commission approves the inclusion in rates of the Senior Human Resources Specialist that is at issue in the case then the following capital additions and their costs indicated below should also be included in rates:

2006	Workstations - New (2)	3,400
2006	Office Workstations	10,400

2.08 Internal Audit Department -- Parties agree that if the Commission approves the inclusion of the [*291] Internal Audit Department in rates then the following capital additions and their costs indicated below should also be included in rates:

2006	IBM Laptop PC for Senior Auditor	3,100
2006	Office Furniture Replacement	14,500
2006	Laserjet Printer	500
2008	Replace 2 Laptop Computers	6,400

2.09 Risk Management Department -- Parties agree that if the Commission approves the inclusion of the Risk Manager position in rates then the following capital additions and their costs indicated below should also be in rates:

2006	Workstation with furniture	10,200
2006	PC Workstations Replacement w/monitor (1)	1,700

2.10 Detail of General Office Capital Budgets -- Attached as Appendix C is the detail of the General Office capital budgets, showing projects that are settled and projects that are still at issue and the resolution is to be determined ("TBD") by the Commission.

Advice Letter Treatment

2.11 Advice Letter Protects -- DRA and GSWC agree that GSWC is authorized to file advice letters seeking authorization to include in rate base, upon completion, the actual costs of the plant additions set forth herein and to receive a corresponding rate adjustment [*292] for the additional rate base. Second, the Parties agree to request that the final decision contain an ordering paragraph authorizing each and every advice letter project contained herein. Third, it was agreed upon that these advice letter projects only include the overhead rate that the Commission determines in this proceeding.

Bissell Well # 1 -- GSWC requested approval of \$ 203,500 in 2006 for design and permitting and \$ 2,381,100 for construction of a project to provide treatment of volatile organic compounds (VOC) at Bissell well # 1 and for manganese treatment at Bissell well # 2. DRA recommended \$ 87,656 in 2006 and \$ 1,025,871 to be included in rates at this time for completion of manganese treatment at Bissell Well # 2. GSWC has applied for Proposition 50 funding for the VOC treatment for Bissell Well # 1. Until it is known what funding, if any, GSWC will receive, the parties agree that this portion of the project

for Bissell Well # 1 should not yet be included in rates. Once the level of Proposition. 50 funding for this project is determined, GSWC may file an advice letter to recover its costs, net of outside funding, capped at \$ 1,461,000

WB-01 Emergency Chlorination [*293] Station -- GSWC requested \$ 83,000 in 2006 for design and permitting and \$ 389,500 in 2007 for construction costs to upgrade the existing WB-01 connection with MWD to include an emergency chlorination facility. Due to the uncertainty surrounding the granting of permits related to this project, parties agree that GSWC may file an advice letter, capped at \$ 472,500, once the construction of the project is complete.

2.12 Region II Construction Work in Progress -- GSWC forecasted a Construction Work in Progress (CWIP) to be closed in 2006 of \$ 34,812,900. This amount included monies spent through 12/31/05 on pre-2006 projects and the remaining cost to complete these projects. DRA recommended a CWIP to be closed in 2006 in an amount in 2006 of \$ 19,642,600, based on the five year average of CWIP closed to Utility Plant in Service. In order to allow sufficient funding to complete projects in CWIP and lessen the impact to ratepayers, the Parties agree to include the \$ 34,812,909 in Plant in Service, which will be amortized over the years 2006, 2007 and 2008 as follows:

Year	2006	2007	2008	Total
Amount	14,511,408	10,150,750	10,150,750	\$ 34,812,909

2.13 General [*294] Office Construction Work in Progress -- GSWC forecasted an amount of Construction Work in Progress (CWIP) to be closed in 2006 of \$ 1,509,784. This amount included monies spent through 12/31/05 on pre-2006 projects and the remaining cost to complete these projects. DRA recommended a CWIP to be closed in 2006 in an amount of \$ 428,144. After discussions, the Parties agree that it is reasonable to include \$ 900,000 in CWIP to be closed in 2006.

GSWC agrees with DRA's requests that in future CRC proceedings for CWIP to be closed (recorded plus additional forecast), such requests shall be supported by workpapers and testimony to facilitate DRA's review of the Company's forecast. Explanations will be provided to support the inclusion of abandoned and/or replacement projects.

Other Ratebase Items

2.14 Contingency (General Office & Region II Headquarters) -- GSWC requested a capital budget contingency amount based on 5% of the capital budget excluding the proposed Customer Information System. In the Region II Headquarters GSWC requested a contingency budget based on 10% of the proposed capital budget. DRA recommended a 2.5% contingency for both of these offices. For settlement [*295] purposes Parties agree to a 2.5% contingency. The amount of contingency in the General Office will be calculated when all other outstanding items within the capital budget are resolved and approved in a Commission order.

2.15 Overhead -- GSWC and DRA both calculated the overhead rate to be applied to capital budgets using similar methodologies, with some differences, particularly in relation to the amount of certain expense items to be booked into the overhead pool. After discussions between the GSWC and DRA witnesses the parties agree to the following:

. The Overhead Rates for both General Office and Region II General Rate Cases will be calculated based on the methodology submitted by GSWC witness Eva Tang as part of her prepared written direct testimony in this matter.

. GSWC and DRA agree that the overhead rate to be applied to 2007 and 2008 capital budgets will be determined based on the finalized capital budgets and the capitalized expenses approved by the Commission in the final decision adopting the Parties' Stipulation.

. The (recalculated) rates will then be applied to the finalized capital budget (before overhead loading) to be included in the rate base.

[*296] . It is agreed between GSWC and DRA that at the end of each year, the Overhead Pool Account should be zeroed out. GSWC will develop a methodology that will allocate the balance of Overhead Pool Account (negative or positive) to work orders at the end of each year to achieve this objective. It is also agreed that the balance of the Overhead Pool at the end of each year should be allocated to jobs in all regions.

2.16 Operational Savings Related to Plant Additions -- Parties agree to include a one-time operational savings of \$ 31,380 in 2007 and \$ 3,415 in 2008 as adjustments to expenses in the summary of earnings. Parties agree that these savings are not cumulative and therefore the 2008 summary of earnings should be adjusted to reflect the appropriate operational savings for that year.

2.17 Region II Plant Weighting Factor -- GSWC used a 50% plant weighting factor. DRA used a 5-year average plant weighting factor. GSWC & DRA agree to use DRA's recommended plant weighting factors of 42.97%.

2.18 General Office & Region II Advances (Gross-UP) DRA recommended to exclude from rate base the \$ 3,680,728 included in GSWC's application with respect to income taxes associated [*297] with the gross-up of taxable advances pursuant to D.87-09-026 (Method 5). The reason stated for recommending exclusion of the item was that GSWC had not provided "supporting calculations to vouch for the requested Advances-Gross ups amounts." Similarly, and for the same reason as cited above as well as not having provided a methodological rationale, DRA recommended "disallowing both the charges in General Office, and the [offsetting] credits in Region-II relating to Advances-Gross ups."

In GSWC's rebuttal testimony, calculation workpapers were provided along with methodological information from the Decision. Cross-referencing information was also provided between GSWC's calculation workpapers and the Decision's appendices to support that Method 5 was properly applied. Minor revisions were made to the amounts in the Application and the applicability of offsetting credits, in Region II was made moot by virtue of the methodology reflected in the computational workpapers; consequently, GSWC stated that the credits in Region II would no longer be applicable if the revised figures were to be incorporated in the G.O.

GSWC and DRA have reached agreement that the amounts provided in [*298] GSWC's rebuttal testimony are accurate in view of Method 5 as provided by the Decision. As such GSWC and DRA agree to substitute the amounts in the Application for the G.O. with the following figures:

2006: \$ 3,550,646

2007: \$ 3,399,173

2008: \$ 3,250,726

and to remove the credits in the Application for Region II.

Further, to facilitate the application process, GSWC agrees to provide computational support and a narrative describing the application of Method 5 to GSWC's computational approach in future application filings. GSWC concurs with DRA's recommendation to develop a proposal that will facilitate a transition of the recording of this item from the General Office directly to the operating regions, and will include that proposal in a future rate case.

2.19 Depreciation Accrual Rates

GSWC and DRA utilized the same methodology and depreciation accrual rates to forecast plant depreciation. For Region II, DRA agreed with GSWC's depreciation rates for each of the individual plant categories, but disagreed with the composite accrual rate. DRA recommended a composite accrual rate for Region II of 2.67%, GSWC used a rate of 3.08%. After discussions the Parties agreed that [*299] a composite accrual rate of 2.89% was reasonable. In the General Office, GSWC used a composite accrual rate of 8.04%, which DRA accepted.

2.20 Working Cash Lag days

The difference between DRA's and GSWC's estimates for working cash is due to difference in lag days used for purchased water expense and regulatory commission expense. After discussions between the Parties GSWC and DRA agree to the following lag days in Region II:

Metropolitan	GSWC	DRA	Stipulated
Purchased Water	40.7	55.5	55.5
Expense			
Regulatory Commission	52.8	59.3	59.3
Expense			

3.00 Sales

3.01 Customers (Connections)

GSWC and DRA used the methodology prescribed in the new Rate Case Plan (RCP) to forecast customer growth within each Customer Class. The methodology used by both GSWC and DRA to forecast customer growth was the five year average increase by customer class.

Region II Customer Class	GSWC 2007	DRA 2007	Stipulated 2007
Commercial	98,184	98,184	98,184
Industrial	252	252	252
Public Authority	693	693	693
Irrigation	155	155	155
Resale	0	0	0
Reclaimed Water	39	39	39
Other	14	14	14
Private Fire	1,707	1,707	1,707
Total	101,044	101,044	101,044
[*300]			

Region II Customer Class	GSWC 2008	DRA 2008	Stipulated 2008
Commercial	98,576	98,576	98,576
Industrial	251	251	251
Public Auth.	693	693	693
Irrigation	173	173	173
Resale	0	0	0
Reclaimed Water	40	40	40
Other	15	15	15
Private Fire	1,728	1,728	1,728
Total	101,477	101,477	101,477

3.02 Sales Per Customer

GSWC and DRA used a five year average to forecast usage per customer for all customer classes other than Commercial/Residential. GSWC and DRA differed on methodology for forecasting Commercial/Residential customer usage.

Region II Customer Class	GSWC	DRA	Stipulated
Commercial	271.1	279.9	1/
Industrial	2,994.4	2,994.4	2,994.4
Public Authority	2,310.4	2,310.4	2,310.4
Irrigation	840.0	840.0	840.0
Resale	0	0	0
Reclaimed	9,559.2	9,559.2	9,559.2
Other	353.8	353.8	353.8

1/ disputed issue -- litigated at hearings, will be briefed by parties

3.03 Unaccounted for Water

GSWC and DRA agree to use a five-year average of historical Unaccounted for Water (Water Loss Section of Work Papers) to forecast test year levels.

Region II	GSWC	DRA	Stipulated
Unaccounted For	3.33%	3.33%	3.33%
Used in Operations	2.09%	2.09%	2.09%

[*301]

4.00 Labor

4.01 Region II Labor - GSWC's forecast for total labor was based on its current organizational structure and actual annual salaries, using twelve months' recorded ratios of expense to capital. Added to this base was inflation, overtime, increases for merit, overhead to account for the clearing of miscellaneous tools and stand-by and call-out pay to derive the forecast for the Test Year. DRA recommended a labor expense derived by inflating the 2005 recorded labor expense to 2007. In the Southwest District Office DRA agreed with GSWC's recommended labor expense. After further discussions the Parties agree the following labor expenses are reasonable for the test year 2007.

Metropolitan CSAs	GSWC	DRA	Stipulation
Operations Labor	\$ 3,097,820	\$ 2,991,000	\$ 3,075,800
Maintenance Labor	\$ 884,717	\$ 854,200	\$ 875,600
A&G Labor	\$ 671,776	\$ 648,600	\$ 664,900
Total Labor Expense	\$ 4,654,313	\$ 4,493,800	\$ 4,616,300
Region II Headquarters	GSWC	DRA	Stipulation
Operations Labor	\$ 38,334	\$ 33,100	\$ 33,900
Maintenance Labor	\$ 0	\$ 0	\$ 0
A&G Labor	\$ 648,406	\$ 559,700	\$ 637,400
Total Labor Expense	\$ 686,740	\$ 592,800	\$ 671,300
Central District HQ	GSWC	DM	Stipulation
Operations Labor	\$ 26,474	\$ 25,500	\$ 26,200
Maintenance Labor	\$ 4,263	\$ 4,300	\$ 4,200
A&G Labor	\$ 364,341	\$ 352,000	\$ 360,800
Total Labor Expense	\$ 395,078	\$ 381,800	\$ 391,200

[*302]

Southwest District HQ	GSWC	DRA	Stipulation

Southwest District HQ	GSWC	DRA	Stipulation
Operations Labor	\$ 23,138	\$ 23,138	\$ 23,100
Maintenance Labor	\$ 11,428	\$ 11,428	\$ 11,400
A&G Labor	\$ 234,167	\$ 234,167	\$ 234,200
Total Labor Expense	\$ 268,733	\$ 268,733	\$ 268,700

4.02 Tools Clearing -- GSWC included 1.8% tools clearing expense within its labor expense forecast. DRA recommended discontinuing this practice. The Parties agreed that in future GRC proceedings GSWC will no longer use the tools clearing expense and the cost of small tools will be booked in WUDF account 805.00. Depreciation for general tools and work equipment will no longer be booked to the tools clearing account and will be included in the depreciation expense, WUDF account 503.00.

In order for GSWC to be made whole, GSWC and DRA agree to the following reductions to the clearing account of the General Office and Region II depreciation reserve and a corresponding increase to the depreciation expense.

Location	Adjustment
General Office	\$ 21,661
Metropolitan	\$ 121,361

4.03 General Office Labor -- GSWC and DRA used the same methodology to forecast General Office Labor expense, however there were some differences [*303] within the components of the methodology where DRA disagreed with GSWC's forecast.

The most significant difference between DRA and GSWC is DRA's exclusion of 36.5 positions that GSWC had included in its forecast. The issue of these positions remains unresolved between the Parties. All other differences between the Parties' positions have been resolved as follows.

4.04 General Office Tools Clearing -- GSWC included 1.8% tools clearing expense within its labor expense forecast. DRA recommended discontinuing this practice. The Parties agreed that in the future GSWC will no longer use the tools clearing expense and the cost of small tools will be booked in WUDF account 805.00. Depreciation for general tools and work equipment will no longer be booked to the tools clearing account and will be included in the depreciation expense, WUDF 503.00. In order for GSWC to be made whole, GSWC and DRA agree to transfer \$ 21,661 from the accrual charged to the clearing account to the depreciation expense of the General Office depreciation reserve.

4.05 Common Customer Account -- GSWC included a portion of the labor expense for supervisors in its customer service center (CSC) in the [*304] Common Customer Account expense, WUDF 773.00. DRA recommended that all of the labor expense for the CSC supervisors' labor should be included in Operations Labor expense, WUDF 780.00 in this case and going forward. GSWC agrees with DRA's recommendation.

4.06 General Office Overtime -- GSWC proposed an overtime rate of 2.0%, which was the recorded overtime rate for the twelve months ended September 2005. DRA recommended an overtime rate of 1.08%, the average of 2001, 2002 and 2005. The parties have agreed to an overtime rate of 1.185% for the test year.

4.07 General Office Vacancies -- GSWC made no adjustments in its forecasted labor expense for possible vacancies during the test year. DRA proposed a vacancy adjustment of \$ 563,627 to the 2005 labor base, which erroneously included some vacant positions that were not part of the General Office. The parties agree that an adjustment of \$ 474,428 to the 2005 labor base is reasonable.

4.08 General Office Equity Adjustment -- GSWC included a 1.28% performance based merit adjustment in its labor expense forecast. DRA did not include any equity adjustment in its recommendation. Upon further discussions between GSWC and [*305] DRA, the Parties agree that it is appropriate to include an equity, or merit, adjustment of 0.7% to derive the General Office labor expense for the test year.

5.00 Administrative and General Expenses

5.01 Office Supplies - To forecast Office Supplies expenses, GSWC mainly based their estimate on inflating the recorded data. In addition, GSWC requested funds to cover some of the anticipated future cost in Region II- I-IO and General Office, while. DRA used various methodologies at the sub-categories level in the General Office; trending the -recorded expenses in Metropolitan CSA; inflating 5 years average in Region II-HO and inflating 2 years average in Central District HQ. DRA accepted GSWC's estimate in Southwest District-HQ

After discussions, the Parties agree to the following estimates for Office Supplies in 2007:

2007	CSA	GSWC	DRA	Stipulated
General Office		2,380,700	1,727,400	2,054,600
Region II -- HQ		260,100	176,900	244,400
Central District HQ		111,800	96,200	105,200
Southwest District HQ		136,300	136,300	136,300
Metropolitan CSA		338,400	315,000	326,000

5.02 Injuries and Damages -- GSWC evaluated the insurance market and the [*306] anticipated economic development to estimate expenditures for Injuries and Damages in General Office. DRA reduced GSWC's forecasted amount for Injuries and Damages by 12.52% to forecast DRA's Injuries & Damages expense level. Other than Brokers fee, DM&A fee and Worker Comp (Loss Reserve) which are components of Injuries and Damages expense, the total level of Injuries and Damages cost for General Office is still a disputed issue.

2007	Proposed		Stipulated		
	GSWC	DRA	GSWC	DRA	
ITEM	In Thousands		In Thousands		
Gen. Liability Insurance	255.4	221.5	255.4	221.5	1/
Auto Liability Insurance	226.4	187.6	226.4	187.6	1/
Reserve AL & General Liability					1/
Loss Reserve	517.0	448.3	517.0	448.3	
Excess Workers Comp	222.3	201.2	222.3	201.2	1/
Umbrella Liability	581.1	503.9	581.1	503.9	1/
D & O Insurance	222.3	192.9	222.3	192.9	1/
Fiduciary Liability Insurance	11.4	9.9	11.4	9.9	1/
Crime Insurance	6.2	5.4	6.2	5.4	1/
EPL Insurance	56.9	49.3	56.9	49.3	1/
DM&A Adm Fee	111.7	55.7	55.7	55.7	Settled
Broker (Marsh) Adm Fee	249.2	205.5	205.5	205.5	Settled
L/C for Auto	6.2	5.4	6.2	5.4	1/

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ITEM	Proposed		Stipulated		
	GSWC	DRA	GSWC	DRA	
		In Thousands		In Thousands	
Workers Comp (Loss Reserve)	723.8	654.9	723.8	723.8	Settled
Claims Management Services	54.3	47.1	54.3	47.1	1/
Workers Comp (Security Deposit)	12.4	12.0	12.4	12.0	1/
Total Injuries and Damages	2,800	3,157	2,869		
Net Expensed [*307]	2,573	2,222	2,494	2,267	

1/ disputed expense - litigated at hearings, will be briefed by parties

As part of determining the overhead rate, the Parties stipulated to capitalize 21% of the total cost of Injuries and Damages and 79% will be expensed and booked into General Office Summary of Earning.

5.03 Property Insurance -- There are two components for this line item: Property Insurance and Excess Property Insurance. GSWC evaluated the insurance market and the anticipated economic development to estimate both components in General Office. DRA inflated 2005 recorded of Property Insurance and set Excess Property Insurance to zero noting that the value of Excess Property Insurance is already embedded into the value of Property Insurance.

As part of determining the overhead rate, the Parties stipulated to capitalize 21 % of the total cost of Property insurance and 79% will be expensed and booked into General Office Summary of Earning.

The level of Property Insurance expense for General Office is still a disputed issue.

2007

ITEM	Proposed		Stipulated	
	GSWC	DRA	GSWC	DRA
		In Thousands		In Thousands
Property Insurance & Excess Property Ins	422.9	382.3		1/
Excess Property Insurance	33.1			1/
Total Property Insurance	456.0	382.3		
Net Expensed [*308]	360.9	282.9		

1/ disputed expense -- litigated at hearings, will be briefed by parties

5.04 Pensions and Benefits -- GSWC's estimate in the General Office for the Pension Plan is calculated in accordance with the accounting requirements of Financial Accounting Standards Board Standard No. 87, "Employers' Accounting for Pensions". As such, the annual expense for the Pension Plan is actuarially determined based on calculations performed by the Pension Plan's actuary. DRA estimate was based on adjusting GSWC's estimate downward incorporating the reduction in annual increase and number of employees in General Office. The table below illustrates the partially stipulated Pension & Benefits expense in the General Office

2007

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G.O. Pension & Benefits	Proposed		Stipulated		
	GSWC (\$ 000)	DRA	GSWC (\$ 000)	DRA	
401-k Plan Contribution	1,412.0	1,146.1	1,412.0	1,210.0	2/
VEBA Costs (FASH 106)	1,049.0	924.6	1,049.0	1,049.0	
Pension Plan Costs (FASB 87)	5,710.0	5,069.5	5,710.0	5,352.2	2/
Legal Expenses Pension & 401k Plan	21.0	2.1	2.1	2.1	
Audit Expenses - 401k	36.0	34.9	35.9	35.9	
Actuary Costs Pension Plan (Mercer)	66.0	64.6	64.6	64.6	
Actuary Expenses : Special Projects	62.7	61.5	61.5	61.5	
Trustee Cost for 401K Plan (Wells Fargo)	41.1	42.1	41.1	41.1	
Pension Restoration Fund (SERF)	637.6	402.7	637.6	433.1	2/
Transition Obligation for [*309]	61.8	55.3	55.3	55.3	
G.O. Pension & Benefits	Proposed		Stipulated		
	GSWC (\$ 000)	DRA	GSWC (\$ 000)	DRA	
FASB 106 Stock Option Compensation (FASB 123)	1,083.0	664.9	950.0	950.0	
Group Health Insurance	6,251.0	4,471.2	5,234.6	5,234.6	
Executive Physicals	2.1	0.0	0.0	0.0	
Discretionary Bonus	151.6	78.9	78.9	78.9	
Dividend Equivalent Rights	406.1	0.0	406.1	0.0	1/
Annual Incentive Bonus	990.0	0.0	990.0	0.0	1/
Albert Printing for employee related matters	15.0	0.0	0.0	0.0	
Employment Advertising	100.0	63.9	63.9	63.9	
Pre-Employment Physical Examinations	18.8	8.7	8.7	8.7	
DMV & Background check	24.6	0.0	0.0	0.0	
Flowers	2.8	0.0	0.0	0.0	
Service Awards	63.8	0.0	0.0	0.0	
Tuition Reimbursement	60.0	40.5	40.5	40.5	
Company Sponsored Picnic	60.0	0.0	0.0	0.0	
Holiday Events Employee					

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G.O. Pension & Benefits	Proposed		Stipulated	
	GSWC (\$ 000)	DRA	GSWC (\$ 000)	DRA
Activity	120.0	0.0	0.0	0.0
DOT Drug Test Program	3.3	2.8	2.8	2.8
Workers' Comp fee to CMS	0.0	45.7	0.0	0.0
Sub-totals	18,449.3	13,180.0	16,844.6	14,684.2
Capital Allocation @	-3,874.4	-3,426.8	-3,537.4	-3,083.7
Sub-Total Net For Expense	14,574.9	9,753.2	13,307.2	11,600.5
Management initiatives, Succession planning, and training	247.3	353.0	353.0	247.3 3/
Total Net For Expense [*310]	14,822.2	10,106.2	13,660.2	11,847.8

1/ disputed expense -- litigated at hearings, will be briefed by parties

2/ partially stipulated - to be adjusted upward for employee count increase which is subject to Commission approval

3/ unresolved -- dispute arose after hearings, to be resolved pending ALJ review

The Parties agree that if the Commission approves the inclusion of the DRA's disallowed positions in the General Office, 401K Plan Contribution, Pension Plan and Pension Restoration Fund (SERP) will be accordingly adjusted upward.

As part of determining the overhead rate, the Parties stipulated to capitalize 21% of the total cost of Pension & Benefit, and 79% will be expensed and booked into General Office Summary of Earning.

In Region II, GSWC mainly based their estimate on inflating the recorded data. In addition, GSWC requested funds to cover the cost of water quality training in Region II-HQ, Central District HQ and Metropolitan CSA. DRA applied several methodologies based on recorded data. Upon further discussions, the Parties stipulated to the following amounts for Pension & Benefits in Region II.

2007

CSA	GSWC	DRA	Stipulated
Region II - HQ	70,900	43,000	55,000
Central District-HQ	28,200	21,200	21,200
Southwest District-HQ	28,900	28,900	28,900
Metropolitan CSA	65,300	47,900	57,900

[*311]

5.05 Business Meals -- To estimate expenditures for Business Meals, GSWC inflated the latest recorded to 2007 level. In Region II, DRA used five year average inflated to 2007 level and in the General Office, DRA based its estimate on three year average inflated to 2007 expense level, then adjusted it downward by 10%.

The Parties stipulated to Business Meals amounts except in the General Office which is still disputed.

The Parties agree to the following estimates for 2007 in Region II:

2007

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CSA	GSWC	DRA	Stipulated
General Office	89,300	66,100	1/
Region II- HQ	10,700	7,000	7,100
Central District-HQ	3,300	2,800	2,800
Southwest District-HQ	2,500	2,500	2,500
Metropolitan CSA	4,100	2,700	2,700

1/ disputed expense - litigated at hearings, will be briefed by parties

5.06 Regulatory Commission Expense -- GSWC based its estimate for Region II - Regulatory Commission Expense on a comparable cost for another rate case, while DRA's estimate is a combination of Region II recorded data and components of GSW's estimates. In the General Office, GSWC utilized the four-year average and DRA utilized the three-year average, inflated to 2007 expense level. [*312] After discussions between the Parties

GSWC and DRA agree to the following:

2007

CSA	GSWC	DRA	Stipulated
General Office	50,300	35,800	35,800
Region II - HQ	0	0	0
Central District-HQ	0	0	0
Southwest District-HQ	0	0	0
Metropolitan CSA	224,500	201,100	224,500

5.07 Outside Services -- GSWC based its forecast for Outside Services in Region II on the recorded data. Additional funds were requested to cover anticipated future cost in Region II-HQ. DRA accepted GSW's estimate in Metropolitan CSA and Southwest District HQ.

In Central District HQ, GSWC requested funds of \$ 500,000 in legal cost to secure amendment of the court judgments which governs the rights of the Parties in Central and West Basin. DRA recommendation is to continue recording these legal costs in the memorandum account, that was established in D.04-08-053 and recovering it through an advice letter process. The memorandum account and advice letter process was described in D.04-08-053, Attachment A, Stipulation and Settlement. GSWC do not oppose DRA's recommendation to extend the memorandum account treatment that was established in D.04-08-053 to record the legal cost in Central District [*313] for Test year 2007 and Escalation Year 2008 and recover it through advice letter filing.

In the General Office, GSWC inflated 2005 Outside Service recorded to 2007 expense level, while DRA applied several forecasting methodologies at the vendor level.

After several discussions, GSWC and DRA stipulate to the following estimates for 2007:

2007

CSA	GSWC	DRA	Stipulated	Memo Acct
General Office	6,740,900	3,323,400	5,698,000	
Region II - HQ	195,700	58,500	161,400	
Central District-HQ	527,300	27,300	27,300	
		500,000	500,000	500,000

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CSA	GSWC	DRA	Stipulated	Memo Acct
Southwest District-HQ	38,700	38,700	38,700	
Metropolitan CSA	121,900	121,900	121,900	

5.08 Miscellaneous -- To estimate expenditures for Miscellaneous Expenses in Region II, GSWC used 2005 recorded expenses and applied composite inflation factor to forecast 2007 expense level. DRA accepted GSWC's estimate for Miscellaneous Expenses in Region II.

In the General Office, GSWC estimate is a combination of inflating the recorded data and requesting additional funds to cover the anticipated future higher cost in this category. DRA's estimate is based on inflating three-year average, and then adjusted it downward to exclude [*314] several organizations dues such as National Association of Water Companies (NAWC), California Foundation on the Environment and Economy (CFEE) and American Council on Education (ACE).

The Parties reached to a stipulated Miscellaneous amounts except in the General Office which is still considered a disputed issue. The following is stipulated amounts in Region II for 2007.

2007

CSA	GSWC	DRA	Stipulated
General Office	2,009,400	1,415,600	1/
Region II - HQ	4,600	4,600	4,600
Central District HQ	34,100	34,100	34,100
Southwest District HQ	12,400	12,400	12,400
Metropolitan CSA	6,400	6,400	6,400

1/ disputed expense - litigated at hearings, will be briefed by parties

5.09 Allocated Expense of General Office. Common Customer Accounts, GSWC allocated the General Office Expenses and Common Customer Accounts expenses to Metropolitan CSA based on GSWC's General Office Allocation Study, which is part of this proceeding, and subject to the Commission approval. DRA allocated the General Office Expenses and Common Customer Accounts to Metropolitan CSA based on DRA's General Office Allocation Study.

Since the General Office Cost Allocation methodology and [*315] some of the General Office expenses are disputed issues, the General Office Expenses and Common Customer Accounts allocated to Metropolitan CSA (Accounts 77300 and 79910) are still disputed issues.

2007

	GSWC	DRA	Stipulated
Metropolitan			
77300 Common Customer Acct	1,273,500	766,600	1/
79910 Alloc General Office	13,375,200	7,125,100	1/

1/ disputed expense -- litigated at hearings, will be briefed by parties

5.10 Allocated Expense of, Region and District Offices -- GSWC allocated the General Region II-HQ, Central and Southwest District Offices to Metropolitan GSA based on the updated "Revised Four-Factor."

GSWC and ORA agree to the following estimates of the allocated Region II-HQ, Central and Southwest District Offices to Metropolitan CSA for 2007.

2007

GSA	GSWC	DRA	Stipulated
Allocated Region Office	1,423,400	1,050,600	1,327,400
Allocated District Offices	2,036,500	1,499,000	1,518,100

5.11 Other Maintenance of General Plant -- GSWC inflated the five-year average in Region II and inflated the four-year average in the General Office to estimate 2007 expenditures for Other Maintenance of General Plant

DRA accepted GSWC's [*316] estimate for Other Maintenance of General Plant in Region II and used two-year average in the General Office. The following table is the stipulated amounts for Other Maintenance of General Plant

2007

CSA	GSWC	DRA	Stipulated
General Office	793,300	723,000	765,000
Region II - HQ	13,700	13,700	13,700
Central District - HQ	8,600	8,600	8,600
Southwest District -HQ	8,200	8,200	8,200
Metropolitan CSA	17,200	17,200	17,200

5.12 Rent -- In Region II, GSWC estimate for Rent was based on actual lease contracts; and in the General Office, GSWC requested additional funds to cover the cost of renting additional space due to overcrowding in the existing building.

The Parties reached to a stipulated Rent amounts except in the General Office which is still a disputed issue.

2007

CSA	GSWC	DRA	Stipulated
General Office	246,300	21,700	1/
Region II - HQ	\$ 177,200	\$ 177,200	\$ 177,200
Central District	\$ 118,700	\$ 118,700	\$ 118,700
Southwest District	\$ 0	\$ 0	\$ 0
Metropolitan	\$ 359,200	\$ 359,200	\$ 359,200

1/ disputed item - litigated at hearings, will be briefed by parties

5.13 A&G Expense Capitalized -- In Region II Headquarters, [*317] GSWC applied a credit of 21% to Office Supplies, Outside Services and Corporate Expenses, while DRA used two ratios: 21% and 5%. After further discussions, DRA stipulated to GSWC's capitalized ratio of 21%.

The Parties accept the A&G Expense Capitalized forecast as set forth below:

2007

	GSWC	DRA	Stipulated
Region 2 HQ	-\$ 308,200	-\$ 308,200	-\$ 298,900

6.00 Operations and Maintenance

6.01 Common Customer Accounts -- In the General Office, Common Customer Account is comprised of three components: Customer Service Labor, Equipment Rental and Billing Supply. GSWC

GSWC included a portion of the labor expense for supervisors in its customer service center (CSC) in the Common Customer Account expense, WUDF 773.00. DRA recommended that all of the labor expense for the CSC supervisors' labor should be included in Operations Labor expense, WUDF 780.00. GSWC agrees with DRA's recommendation.

Equipment Rental -- GSWC annualized the latest recorded equipment lease costs and inflated it to the 2007 level. DRA only utilized the latest recorded of equipment lease costs without including any inflationary increase for the future test year.

Billing Supply [*318] -- GSWC and DRA used two year average recorded and inflated to 2007 level.

After several discussions, the Parties agree to the following estimate for Common Customer Account

2007

	GSWC	DRA	Stipulated
General Office	671,400	371,100	396,800

6.02 Postage - GSWC and DRA based their estimate on the estimated unit cost of postage multiplied by the total number of customer, however. DRA didn't inflate the estimated cost for 2007 level, noting that an increase in number of customers in 2007 is already taken into account.

After several discussions, the Parties stipulated to the following estimate for Postage

2007

CSA	GSWC	DRA	Stipulated
General Office	769,000	751,400	751,400

6.03 Uncollectibles -- GSWC based its forecast for uncollectibles on the 5- year average of write-offs less recoveries as a percentage of gross revenues. DRA accepted GSWC's estimates. GSWC and DRA agree to the following uncollectible percentage, to be used for the test years:

CSA	GSWC	DRA	Stipulated
Metropolitan CSA	0.287%	0.287%	0287%

6.04 All Other Operations --GSWC estimate in Region II and General Office for Other Operations Expense [*319] was based on inflating five-year average of recorded data to 2007 expense level. In addition GSWC requested funds to cover some of the anticipated higher future cost in Region II HQ and Metropolitan CSA.

In the General Office, DRA applied several methodologies at the sub-account level. In Region II-HQ, DRA inflated five-year average and accepted GSWC's estimate in Central and Southwest District Offices.

GSWC requested funds for Conservation programs as part of capital addition. DRA recommended \$ 1,545,900 to fund the best management programs and be included as a component of Other Operation Expenses GSWC doesn't oppose DRA's recommendations. Since some of the cost for best management programs is covered in various types of expenses, the Parties stipulated to an amount of \$ 458,700.

After further discussions between the Parties, GSWC and DRA stipulated to the following estimates for 2007 expense:

2007				
CSA	GSWC	DRA	Stipulated	
General Office	287,700	154,700	241,600	
Region II - HQ	39,800	20,600	20,600	
Central District HQ	24,600	24,600	24,600	
Southwest District HQ	24,700	24,700	24,700	
Metropolitan CSA	1,769,700	1,554,800	1,725,200	
Conservation				
Capital	458,700	0	0	
Expense		1,545,900	458,700	

[*320]

6.06 All Other Maintenance -- GSWC estimate in Region II for Other Maintenance Expense was based on inflating four-year average of recorded data to 2007 expense level. In addition GSWC requested funds to cover some of the anticipated higher future cost in Metropolitan CSA.

After several discussions, GSWC and DRA stipulated to the following estimates for 2007 expense:

2007				
CSA	GSWC	DRA	Stipulated	
Region II - HQ	0	0	0	
Central District HQ	5,000	5,000	5,000	
Southwest District HQ	1,200	1,200	1,200	
Metropolitan CSA	3,865,500	3,406,100	3,754,100	

7.00 Taxes Other Income

7.01 Property Taxes -- GSWC and DRA used a five-year average of property tax expenses divided by the five-year average of utility plant in service to derive the property tax rates. GSWC and DRA agree to the following property tax rate for use in the test years:

CSA	GSWC	DRA	Stipulated

CSA	GSWC	DRA	Stipulated
Metropolitan	0.84%	0.84%	0.84%

7.02 Payroll Taxes -- GSWC and DRA agree to apply a rate of 8.10% to all labor expenses, as calculated in GSWC's zero-based forecast.

7.03 Local Taxes -- GSWC and DRA agree to apply the 5-year average recorded rate of 1.172% to all [*321] gross revenues.

8.00 Supply

8.01 Sources -- A combination of historical usage, expected developments, and constraints on systems were analyzed to determine the level of production from wells and purchased water. The difference in supply volume is attributable to differences in the Parties' projection of sales (usage per commercial class customer), which is addressed in paragraph 3.02.

CSA	GSWC Ccf	DRA Ccf
Metropolitan GSA	31,174,573	32,083,534

8.02 Supply Cost -- The Parties agree to use GSWC's methodology to forecast purchased water, purchased power, and pump taxes costs. The difference in supply cost is attributable to the differences in the Parties' projection of sales, which is addressed in paragraph 3.02. The latest available rates prior to producing the final decision tables should be used as referenced in paragraph 8.03.

9.00 Common Issues

9.01 Inflation -- The Parties adopt the inflation factors stated in the February 28, 2006 Memo attached to DRA's Results of Operations Report.

9.02 Established Inflation Factors -- The Parties agree that the Established Factors should be as set forth in the Commission's New Rate Case Plan [*322] guidelines, D.04-06-018.

9.03 Rates Charged for Purchased Water. Purchased Power and Puny Tax -- The Parties agree for 2007 that the latest available rates prior to developing the decision tables should be used to calculate supply expenses in the final decision.

10.00 Cost of Capital

10.01 Return on Equity -- GSWC requested a return on equity of 11.2%. DRA recommended a return on equity of 9.68%. Following discussions between the parties it was agreed that a return on equity on 10.1% was reasonable.

10.02 Cost of Debt -- GSWC requested a cost of debt of 7.46%. DRA concurred with this rate.

10.03 Capital Structure -- GSWC requested a capital structure of 49.2% debt and 50.8% equity. DRA accepted GSWC request.

10.04 Return on Ratebase -- The agreements described in paragraphs 10.01 to 10.03 result in, a return on ratebase of 8.80%

11.00 Other Issues

11.01 Low Income Program (CARW) -- GSWC requested recovery of the accumulated balance of the cost of its low income program in Region II through a rate surcharge. As of December 31, 2005 the balance was \$ 1,310,645. DRA did

not address this item in their report, but following discussions between [*323] the parties it was agreed that when the balance reaches 2% of adopted Region II revenues GSWC is permitted to file an advice letter to recover the accumulated balance through a surcharge.

Dated: August , 2006

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Dated: August 4, 2006

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APPENDIX A

RECONCILIATION EXHIBIT

GOLDEN STATE WATER COMPANY

Region 2 - Metropolitan A.06-02-023

TEST YEAR 2007

SUMMARY OF EARNINGS	GSWC	Change	GSWC
AT PRESENT RATES:			Stipulation

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation
Operating Revenues	94,513.5	2.8	94,516.3
Oper. & Maint. Expenses			
Purchased Water	24,138.0	2.5	24,140.5
Purchased Power	2,041.1	0.0	2,041.1
Pump Taxes	3,802.1	0.0	3,802.1
chemicals	453.0	0.0	453.0
Common Gust. Acct. (G	1,273.5	(146.6)	1,126.9
Common Cust. Acct. (R	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0
Postage	0.0	0.0	0.0
Uncollectibles	271.7	0.0	271.7
Oper-Labor	3,097.8	(32.0)	3,065.8
Oper-Others	1,789.7	414.2	2,183.9
Maint-Labor	884.7	(9.1)	875.6
Maint-Others	3,865.5	(111.5)	3,754.1
A&G Expenses			
Office Supplies	338.4	(12.4)	326.0
Insurance	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0
Pension & Benefits	85.3	(7.4)	57.9
Business Meals	4.1	(1.4)	2.7
Regulatory Comm	224.5	0.0	224.5
Outride Services	121.9	0.0	121.9
Misc	6.4	(0.0)	6.4
Alloc Gen Office	13,375.2	(1,035.6)	12,339.6
Alloc Region Office	1,423.4	(96.0)	1,327.4
Alloc District Office	2,036.5	(518.4)	1,518.1
Maintenance	17.2	(0.0)	17.2
Rent	359.2	0.0	359.2
A & G Exp. Capitalized	0.0	0.0	0.0
A&G Labor	671.8	(6.9)	664.9
Depreciation	9,578.2	(1,169.4)	8,406.8
Other Taxes			
Property Taxes	2,860.9	(198.1)	2,662.9
Peyrol Taxes	376.8	(3.9)	373.0
Local Taxes	1,107.6	0.0	1,107.6
Income Taxes	5,429.9	1,431.4	6,861.3
Adjustment of GO Capitalized Exp	0.0	0.0	0.0
Total Expenses After Taxes	79,592.5	(1,500.4)	78,092.1
Net Operating Revenues	14,921.0	1,503.2	16,424.2
Rate Base	246,042.7	(26,361.0)	219,681.7
Rated Return	6.06%		7.48%
AT PROPOSED RATES:			
Operating Reveilles	109,166.0	(9,395.0)	99,771.0
Uncollectibles	313.8	(27.0)	286.8
Local Taxes	1,279.3	(110.1)	1,169.2

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SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation
Income Taxes	11,759.9	(2,628.7)	9,131.2
Adjustment to match DRA report			
Total Expenses After Taxes	86,138.3	(5,697.6)	80,438.7
Net Operating Revenues	23,029.7	(3,697.4)	19,332.3
Rate Base	246,042.7	(28,361.0)	219,681.7
Rate of Return [*324]	9.36%		8.80%
SUMMARY OF EARNINGS AT PRESENT RATES:	Difference	DRA Stipulation	Change
Operating Revenues	(1,801.4)	96,317.7	0.8
Oper. & Maint. Expenses			
Purchased Water	(1,146.6)	25,287.1	0.0
Purchased Power	(3.8)	2,044.9	0.0
Pump Taxes	0.0	3,802.1	0.0
chemicals	44.6	408.3	0.0
Common Cust. Acct. (G	359.1	767.8	1.1
Common Cust. Acct. (R	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0
Postage	0.0	0.0	0.0
Uncollectibles	(5.2)	276.9	11.0
Oper-Labor	0.0	3,065.8	74.8
Oper-Others	0.0	2,183.9	(916.8)
Maint-Labor	0.0	875.6	21.4
Maint-Others	0.0	3,754.1	348.0
A&G Expenses			
Office Supplies	0.0	326.0	11.0
Insurance	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0
Pension & Benefits	0.0	57.9	10.0
Business Meals	0.0	2.7	(0.0)
Regulatory Comm	0.0	224.5	23.3
Outride Services	0.0	121.9	0.0
Misc	0.0	6.4	(0.0)
Alloc Gen Office	4,563.0	7,778.6	651.6
Alloc Region Office	0.0	1,327.4	276.8
Alloc District Office	0.0	1,518.1	19.2
Maintenance	0.0	17.2	(0.0)
Rent	0.0	359.2	0.0
A & G Exp. Capitalized	0.0	0.0	0.0
A&G Labor	0.0	664.9	16.2
Depreciation	0.0	8,406.8	910.8
Other Taxes			
Property Taxes	0.0	2,662.9	50.1
Peyrol Taxes	0.0	373.0	9.1
Local Taxes	(21.1)	1,128.7	43.1
Income Taxes	(2,184.6)	9,045.9	(330.9)
Adjustment of GO Capitalized Exp	0.0	0.0	(1,757.6)

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	Difference	DRA Stipulation	Change
Total Expenses After Taxes	1,605.5	76,488.6	(527.8)
		67,440.7	(196.9)
Net Operating Revenues	(3,406.9)	19,831.1	528.4
Rate Base	3,919.8	215,761.9	19,053.7
Rated Return		9.19%	

AT PROPOSED RATES:

Operating Reveilles	4,978.5	94,792.5	2,162.5
Uncollectibles	14.3	272.5	6.2
Local Taxes	58.3	1,110.9	25.3
Income Taxes	744.1	8,387.1	512.7
Adjustment to match DRA report			
Total Expenses After Taxes	4,633.1	75,805.5	72.0
Net Operating Revenues	345.4	18,986.9	2,090.5
Rate Base	3,919.8	215,761.9	19,053.7
Rate of Return			
[*325]			

SUMMARY OF EARNINGS
AT PRESENT RATES:

	DRA
Operating Revenues	96,317.1
Oper. & Maint. Expenses	
Purchased Water	25,287.1
Purchased Power	2,044.9
Pump Taxes	3,802.1
chemicals	408.3
Common Cust. Acct. (G	766.6
Common Cust. Acct. (R	0.0
Common Cust. Acct. (D	0.0
Postage	0.0
Uncollectibles	265.8
Oper-Labor	2,991.0
Opel-Others	3,100.7
Maint-Labor	854.2
Maint-Others	3,406.1
A&G Expenses	
Office Supplies	315.0
Insurance	0.0
Injuries & Damages	0.0
Pension & Benefits	47.9
Business Meals	2.7
Regulatory Comm	201.1
Outride Services	121.9
Misc	6.4
Alloc Gen Office	7,125.1

SUMMARY OF EARNINGS	DRA
Alloc Region Office	1,050.6
Alloc District Office	1,499.0
Maintenance	17.2
Rent	359.2
A & G Exp. Capitalized	0.0
A&G Labor	648.6
Derxeciadon	7,496.0
Other Taxes	
Property Taxes	2,612.8
Peyrol Taxes	363.9
Local Taxes	1,085.6
Income Taxes	9,376.8
Adjustment of GO Capitalized Exp	1,757.6
Total Expenses After Taxes	77,014.4
	67,637.8
Net Operating Revenues	19,302.7
Rate Base	196,708.2
Rated Return	9.81%

AT PROPOSED RATES:

Operating Reveilles	92,630.0
Uncollectibles	285.3
Local Taxes	1,085.5
Income Taxes	7,874.4
Adjustment to match DRA report	221.3
Total Expenses After Taxes	75,733.6
Net Operating Revenues	16,896.4
Rate Base	196,708.2
Rate of Return	8.59%

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APPENDIX A

RECONCILIATION EXHIBIT

SOUTHERN CALIFORNIA WATER COMPANY

Region 2 - Metropolitan A.05-02-023

TEST YEAR 2007

INCOME TAX CALCULATION	SCWC	Charge	SCWC Stipulation
AT PRESENT RATES:			
Total Operating Revenues	94,513.5	2.8	94,518.3
Operating Expenses	74,162.6	(2,931.5)	71,230.8
Interest on LTD	9,029.8	(967.4)	8,062.3

2007 Cal. PUC LEXIS 648, *

INCOME TAX CALCULATION	SCWC	Charge	SCWC Stipulation
Book Deprc'n (w/ G.O.)	(10,167.3)	1,179.7	(8,957.6)
Total Deductions	73,025.0	(2,719.5)	70,305.5
State Tax Depreciation	(6,289.2)	0.0	(6,289.2)
Other State Schedule M	702.8	(3.4)	699.5
8.84% -State Tax	1,405.7	240.4	1,646.1
Book Deprc'n (w/ G.O.)	(10,167.3)	1,179.7	(8,987.6)
Tax Depr. - Flow Through	728.1	(55.8)	672.3
State Tax Deduction	(1,405.7)	(240.4)	(1,646.1)
Other Fed Schedule M	702.8	(3.4)	699.5
Del Rev Amort - Contrib	151.4	0.0	151.4
Adjustment far Job Creation Act			(199.8)
35.00% -Federal Tax	4,024.2	1,191.0	5,215.2
TOTAL INCOME TAX	5,429.9	1,431.4	6,861.3

AT PROPOSED RATES:

Total Operating Revenues	109,166.0	(9,395.0)	99,771.0
Operating Expenses	74,376.4	(3,068.9)	71,307.5
Interest on LTD	9,029.8	(967.4)	8,062.3
Book Depren (w/ G.O.)	(10,161.3)	1,179.7	(8,087.6)
Total Deductions	73,238.8	(2,856.6)	70,382.2
State Tax Depreciation	(6,269.2)	0.0	(6,289.2)
Other State Schedule M	702.8	(3.4)	699.5
8.84% -State Tax	2,682.1	(578.3)	2,103.8
Book Deprc'n (w/ G.O.)	(10,187.3)	1,179.7	(8,987.6)
Tax Depr. - Flow Through	728.1	(55.8)	672.2
State Tax Deduction	(1,405.7)	(240.4)	(1,646.1)
Other Fed Schedule M	702.8	(3.4)	699.5
Def Rev Amen - Contrib	151.4	0.0	151.4
Adjustment for Job Creation Act			(199.8)
35.00% -Federal Tax	9,077.8	(2,050.4)	7,027.4
TOTAL INCOME TAX	11,759.9	(2,628.7)	9,131.2
[*327]			

INCOME TAX CALCULATION	Difference	Staff Stipulation	Change	Staff
AT PRESENT RATES:				
Total Operating Revenues	(1,801.4)	95,317.7	0.6	96,317.1
Operating Expenses	3,790.1	67,440.7	(196.9)	67,637.6
Interest on LTD	143.5	7,918.5	699.3	7,219.2

2007 Cal. PUC LEXIS 648, *

INCOME TAX CALCULATION	Difference	Staff Stipulation	Change	Staff
Book Deprc'n (w/ G.O.)	(187.5)	(8,800.1)	(713.0)	(8,087.1)
Total Deductions	3,746.4	66,559.2	(210.5)	66,769.7
State Tax Depreciation	(52.7)	(6,236.5)	52.7	(6,259.2)
Other State Schedule M	351.4	348.0	(354.8)	702.8
8.84% -State Tax	(464.0)	2,110.1	(8.1)	2,118.2
Book Deprc'n (w/ G.O.)	(187.5)	(8,800.1)	(713.0)	(8,087.1)
Tax Depr. - Flow Through	3.7	668.5	54.6	613.9
State Tax Deduction	464.0	(2,110.1)	8.1	(2,118.2)
Other Fed Schedule M	351.4	348.0	(354.8)	702.8
Del Rev Amort - Contrib	0.0	151.4	0.0	151.4
Adjustment far Job Creation Act	0.0	(199.8)		(71.4)
35.00% -Federal Tax	(1,720.6)	6,935.6	(322.8)	7,258.6
TOTAL INCOME TAX	(2,184.6)	9,045.9	(330.9)	9,376.8
AT PROPOSED RATES:				
Total Operating Revenues	4,978.5	94,792.5	2,162.5	92,630.0
Operating Expenses	3,889.0	67,418.5	(219.1)	67,637.6
Interest on LTD	143.8	7,918.5	699.3	7,219.2
Book Deprc'n (w/ G.O.)	(187.5)	(8,800.1)	(713.0)	(8,087.1)
Total Deductions	3,845.3	66,536.9	(232.8)	55,769.7
State Tax Depreciation	(52.7)	(6,236.5)	52.7	(6,289.2)
Other State Schedule M	351.4	348.0	(354.8)	702.8
8.84% -State Tax	126.5	1,977.3	155.1	1,792.2
Book Deprc'n (w/ G.O.)	(187.5)	(8,800.1)	(713.0)	(8,087.1)
Tax Depr. - Flow Through	3.7	668.5	54.6	613.9
State Tax Deduction	464.0	(2,110.1)	(317.9)	(1,792.2)
Other Fed Schedule M	351.4	348.0	(354.8)	702.8
Def Rev Amen - Contrib	0.0	151.4	0.0	151.4
Adjustment for Job Creation Act		(199.8)	(128.4)	(71.4)
35.00% -Federal Tax	617.6	6,409.8	327.6	6,082.2
TOTAL INCOME TAX	744.1	8,387.1	512.7	7,874.4

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APPENDIX A

RECONCILIATION EXHIBIT

GOLDEN STATE WATER COMPANY

Region 2 HQ - A.06-02-023

TEST YEAR 2007

GSWC

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS AT PRESENT RATES:	GSWC	Change	Stipulation	
Operating Revenues	0.0	0.0	0.0	
Oper. & Maint. Expenses				
Purchased Water	0.0	0.0	0.0	
Purchased Power	0.0	0.0	0.0	
Pump Taxes	0.0	0.0	0.0	
Chemicals	0.0	0.0	0.0	
Common Cust. Acct. (G	0.0	0.0	0.0	
Common Cust. Acct. (R	0.0	0.0	0.0	
Common Cust. Acct. (D	0.0	0.0	0.0	
Postage	0.0	0.0	0.0	
Uncollectibles	0.0	0.0	0.0	
Oper-Labor	38.3	(4.4)	33.9	
Oper-Others	39.8	(19.2)	20.6	
Maint-Labor	0.0	0.0	0.0	
Maint-Others	0.0	0.0	0.0	
A&G Expenses				
Office Supplies	260.1	(15.7)	244.4	
Insurance	0.0	0.0	0.0	
Injuries & Damages	0.0	(0.0)	0.0	
Pension & Benefits	70.9	(15.8)	55.0	
Business Meals	10.7	(3.6)	7.1	
Regulatory Comm	0.0	0.0	0.0	
Outside Services	195.7	(34.4)	161.4	
Misc	4.6	(0.0)	4.6	
Alloc Gen Office	0.0	0.0	0.0	
Alloc Region Office	0.0	0.0	0.0	
Alloc District Office	0.0	0.0	0.0	
Maintenance	13.7	(0.0)	13.7	
Rent	177.2	0.0	177.2	
A & G Exp. Capitalized	(308.2)	9.3	(298.9)	
A&G Labor	648.4	(11.0)	637.4	
Depreciation	208.8	0.1	207.0	
Other Taxes				
Property Taxes	9.3	0.0	9.3	
Payroll Taxes	55.6	(1.3)	54.4	
Local Taxes	0.4	0.0	0.4	
Total Expenses Excluding Income	1,423.4	(96.0)	1,327.4	
Net Operating Revenues [*329]	(1,423.4)	96.0	(1,327.4)	
SUMMARY OF EARNINGS AT PRESENT RATES:	Difference	DRA Stipulation	Change	DRA
Operating Revenues	0.0	0.0	0.0	0.0
Oper. & Maint Expenses				
Purchased Water	0.0	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0	0.0
Chemicals	0.0	0.0	0.0	0.0

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	Difference	DRA Stipulation	Change	DRA
Common Cust. Acct. (G	0.0	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0	0.0
Postage	0.0	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0	0.0
Oper-Labor	0.0	33.9	0.8	33.1
Oper-Others	0.0	20.6	0.0	20.5
Maint-Labor	0.0	0.0	0.0	0.0
Maint-Others	0.0	0.0	0.0	0.0
A & G Expenses				
Office Supplies	0.0	244.4	67.5	176.9
Insurance	0.0	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	(0.0)	0.0
Pension & Benefits	0.0	55.0	12.0	43.0
Business Meals	0.0	7.1	0.1	7.0
Regulatory Comm	0.0	0.0	0.0	0.0
Outside Services	0.0	161.4	102.8	58.5
Misc	0.0	4.6	(0.0)	4.6
Alloc Gen Office	0.0	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	0.0	0.0
Alloc District Office	0.0	0.0	0.0	0.0
Maintenance	0.0	13.7	(0.0)	13.7
Rent	0.0	177.2	0.0	177.2
A & G Exp. Capitalized	0.0	(298.9)	9.3	(308.2)
A&G Labor	0.0	637.4	77.7	559.7
Depreciation	0.0	207.0	0.1	206.8
Other Taxes				
Property Taxes	0.0	9.3	0.0	9.3
Payroll Taxes	0.0	54.4	6.4	48.0
Local Taxes	0.0	0.4	0.0	0.4
Total Expenses Excluding Income	0.0	1,327.4	276.8	1,060.6
Net Operating Revenues	0.0	(1,327.4)	(276.8)	(1,050.6)

[*330]

APPENDIX A

**RECONCILIATION EXHIBIT GOLDEN STATE WATER COMPANY Region 2 Central District Office -
A.06-02-023 TEST YEAR 2007**

SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation
AT PRESENT RATES:			
Operating Revenues	0.0	0.0	0.0
Oper. & Maint. Expenses			
Purchased Water	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0
Chemicals	1.9	0.0	1.9
Common Cust. Acct. (G	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0
Postage	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation
Oper-Labor	26.5	(0.3)	26.2
Oper-Others	24.6	0.0	24.6
Maint-Labor	4.3	(0.0)	4.2
Maint-Others	5.0	0.0	5.0
A&G Expenses			
Office Supplies	111.8	(6.6)	105.2
Insurance	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0
Pension & Benefits	28.2	(7.0)	21.2
Business Meals	3.3	(0.5)	2.8
Regulatory Comm	0.0	0.0	0.0
Outside Services	527.3	(500.0)	27.3
Misc	34.1	0.0	34.1
Alloc Gen Office	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	0.0
Alloc District Office	0.0	0.0	0.0
Maintenance	8.6	0.0	8.6
Rent	118.7	0.0	118.7
A & G Exp. Capitalized	0.0	0.0	0.0
A&G Labor	364.3	(3.6)	360.8
Depreciation	125.9	0.0	125.9
Other Taxes			
Property Taxes	6.7	0.0	6.7
Payroll Taxes	32.0	(0.3)	31.7
Local Taxes	0.7	0.0	0.7
Total Expenses Excluding Income	1,424.0	(518.4)	905.6
Net Operating Revenues [*331]	(1,424.0)	518.4	(905.6)

SUMMARY OF EARNINGS AT PRESENT RATES:	Difference	Stipulation	Change	DRA DRA
Operating Revenues	0.0	0.0	0.0	0.0
Oper. & Maint. Expenses				
Purchased Water	0.0	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0	0.0
Chemicals	0.0	1.9	0.0	1.9
Common Cust. Acct. (G	0.0	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0	0.0
Postage	0.0	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0	0.0
Oper-Labor	0.0	26.2	0.7	25.5
Oper-Others	0.0	24.6	0.0	24.6
Maint-Labor	0.0	4.2	(0.0)	4.3
Maint-Others	0.0	5.0	0.0	5.0
A&G Expenses				
Office Supplies	0.0	105.2	9.0	96.2
Insurance	0.0	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0	0.0

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	Difference	Stipulation	Change	DRA DRA
Pension & Benefits	0.0	21.2	(0.0)	21.2
Business Meals	0.0	2.8	0.0	2.8
Regulatory Comm	0.0	0.0	0.0	0.0
Outside Services	0.0	27.3	0.0	27.3
Misc	0.0	34.1	0.0	34.1
Alloc Gen Office	0.0	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	0.0	0.0
Alloc District Office	0.0	0.0	0.0	0.0
Maintenance	0.0	8.6	0.0	8.6
Rent	0.0	118.7	0.0	118.7
A & G Exp. Capitalized	0.0	0.0	0.0	0.0
A&G Labor	0.0	360.8	8.8	352.0
Depreciation	0.0	125.9	0.0	125.9
Other Taxes				
Property Taxes	0.0	6.7	0.0	6.7
Payroll Taxes	0.0	31.7	0.8	30.9
Local Taxes	0.0	0.7	0.0	0.7
Total Expenses Excluding Income	0.0	905.6	19.2	886.4
Net Operating Revenues	0.0	(905.6)	(19.2)	(886.4)

[*332]

APPENDIX A

RECONCILIATION EXHIBIT

GOLDEN STATE WATER COMPANY

Region 2 Southwest District Office - A06-02-023

TEST YEAR 2007

SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation
AT PRESENT RATES:			
Operating Revenues	0.0	0.0	0.0
Oper. & Maint. Expenses			
Purchased Water	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0
Chemicals	0.5	0.0	0.5
Common Cust. Acct. (G	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0
Postage	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0
Oper-Labor	23.1	0.0	23.1
Oper-Others	24.7	0.0	24.7
Maint-Labor	11.4	0.0	11.4
Maint-Others	1.2	0.0	1.2
A&G Expenses			
Office Supplies	136.3	0.0	136.3
Insurance	0.0	0.0	0.0

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation
Injuries & Damages	0.0	0.0	0.0
Pension & Benefits	28.9	0.0	28.9
Business Meals	2.5	0.0	2.5
Regulatory Comm	0.0	0.0	0.0
Outside Services	38.7	0.0	38.7
Misc	12.4	0.0	12.4
Alloc Gen Office	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	10
Alloc District Office	0.0	0.0	0.0
Maintenance	8.2	0.0	8.2
Rent	0.0	0.0	0.0
A & G Exp. Capitalized	0.0	0.0	0.0
A&G Labor	234.2	0.0	234.2
Depreciation	58.7	0.0	58.7
Other Taxes			
Property Taxes	2.6	0.0	2.6
Payroll Taxes	21.8	0.0	21.8
Local Taxes	7.3	0.0	7.3
Total Expenses Excluding Income	612.6	10	(612.6)
Net Operating Revenues	(612.6)	0.0	(612.6)
Rate Base	0.0	0.0	0.0
[*333]			

SUMMARY OF EARNINGS AT PRESENT RATES:	Difference	DRA Stipulation	Change	DRA
Operating Revenues	0.0	0.0	0.0	0.0
Oper. & Maint. Expenses				
Purchased Water	0.0	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0	0.0
Chemicals	0.0	0.5	0.0	0.5
Common Cust. Acct. (G	0.0	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0	0.0
Postage	0.0	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0	0.0
Oper-Labor	0.0	23.1	0.0	23.1
Oper-Others	0.0	24.7	0.0	24.7
Maint-Labor	0.0	11.4	0.0	11.4
Maint-Others	0.0	1.2	0.0	1.2
A&G Expenses				
Office Supplies	0.0	136.3	0.0	136.3
Insurance	0.0	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0	0.0
Pension & Benefits	0.0	28.9	0.0	28.9
Business Meals	0.0	2.5	0.0	2.5
Regulatory Comm	0.0	0.0	0.0	0.0
Outside Services	0.0	38.7	0.0	38.7

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	Difference	DRA Stipulation	Change	DRA
Misc	0.0	12.4	0.0	12.4
Alloc Gen Office	0.0	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	10	0.0
Alloc District Office	0.0	0.0	0.0	0.0
Maintenance	0.0	8.2	0.0	8.2
Rent	10	0.0	0.0	0.0
A & G Exp. Capitalized	0.0	0.0	0.0	0.0
A&G Labor	0.0	234.2	0.0	234.2
Depreciation	0.0	58.7	0.0	58.7
Other Taxes				
Property Taxes	0.0	2.6	0.0	2.6
Payroll Taxes	0.0	21.8	0.0	21.8
Local Taxes	0.0	7.3	0.0	7.3
Total Expenses Excluding Income	0.0	612.6	0.0	612.6
Net Operating Revenues	0.0	(612.6)	0.0	(612.6)
Rate Base	0.0	0.0	0.0	0.0

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RECONCILIATION EXHIBIT

GOLDEN STATE WATER COMPANY

Region 2 Southwest District Office - A06-02-023

TEST YEAR 2007

SUMMARY OF EARNINGS	GSWC	Change	GSM Stipulation	Difference
AT PRESENT RATES:				
Operating Revenues	0.0	0.0	0.0	0.0
Oper. & Maint. Expenses				
Purchased Water	0.0	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0	0.0
Chemicals	0.5	0.0	0.5	0.0
Common Cust. Acct. (G	0.0	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0	0.0
Postage	0.0	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0	0.0
Oper-Labor	23.1	0.0	23.1	0.0
Oper-Others	24.7	0.0	24.7	0.0
Maint-Labor	11.4	0.0	11.4	0.0
Maint-Others	1.2	0.0	1.2	0.0
A&G Expenses				
Office Supplies	136.3	0.0	136.3	0.0
Insurance	0.0	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0	0.0
Pension & Benefits	28.9	0.0	28.9	0.0
Business Meals	2.5	0.0	2.5	0.0
Regulatory Comm	0.0	0.0	0.0	0.0
Outside Services	38.7	0.0	38.7	0.0
Misc	12.4	0.0	12.4	0.0

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	GSWC	Change	GSM Stipulation	Difference
Alloc Gen Office	0.0	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	0.0	0.0
Alloc District Office	0.0	0.0	0.0	0.0
Maintenance	8.2	0.0	8.2	0.0
Rent	0.0	0.0	0.0	0.0
A & G Exp. Capitalized	0.0	0.0	0.0	0.0
A&G Labor	234.2	0.0	234.2	0.0
Depreciation	58.7	0.0	58.7	0.0
Other Taxes				
Property Taxes	2.6	0.0	2.6	0.0
Payroll Taxes	21.8	0.0	21.8	0.0
Local Taxes	7.3	0.0	7.3	0.0
Total Expenses				
Excluding Income	612.6	0.0	612.6	0.0
Net Operating Revenues	(612.6)	0.0	(612.6)	0.0
Rate Base	0.0	0.0	0.0	0.0

[*335]

SUMMARY OF EARNINGS	DRA Stipulation	Change	DRA
AT PRESENT RATES:			
Operating Revenues	0.0	0.0	0.0
Oper. & Maint. Expenses			
Purchased Water	0.0	0.0	0.0
Purchased Power	0.0	0.0	0.0
Pump Taxes	0.0	0.0	0.0
Chemicals	0.5	0.0	0.5
Common Cust. Acct. (G	0.0	0.0	0.0
Common Cust. Acct. (R	0.0	0.0	0.0
Common Cust. Acct. (D	0.0	0.0	0.0
Postage	0.0	0.0	0.0
Uncollectibles	0.0	0.0	0.0
Oper-Labor	23.1	0.0	23.1
Oper-Others	24.7	0.0	24.7
Maint-Labor	11.4	0.0	11.4
Maint-Others	1.2	0.0	1.2
A&G Expenses			
Office Supplies	136.3	0.0	136.3
Insurance	0.0	0.0	0.0
Injuries & Damages	0.0	0.0	0.0
Pension & Benefits	28.9	0.0	28.9
Business Meals	2.5	0.0	2.5
Regulatory Comm	0.0	0.0	0.0
Outside Services	38.7	0.0	38.7
Misc	12.4	0.0	12.4
Alloc Gen Office	0.0	0.0	0.0
Alloc Region Office	0.0	0.0	0.0
Alloc District Office	0.0	0.0	0.0
Maintenance	8.2	0.0	8.2
Rent	0.0	0.0	0.0
A & G Exp. Capitalized	0.0	0.0	0.0
A&G Labor	234.2	0.0	234.2
Depreciation	58.7	0.0	58.7
Other Taxes			

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	DRA Stipulation	Change	DRA
Property Taxes	2.6	0.0	2.6
Payroll Taxes	21.8	0.0	21.8
Local Taxes	7.3	0.0	7.3
Total Expenses Excluding Income	612.6	0.0	612.6
Net Operating Revenues	(612.6)	0.0	(612.6)
Rate Base	0.0	0.0	0.0

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RECONCILIATION EXHIBIT

GOLDEN STATE WATER COMPANY

GENERAL OFFICE - A.06-02-023

TEST YEAR 2007

SUMMARY OF EARNINGS	GSWC	Change	GSWC Stipulation	Difference
AT PRESENT RATES:				
Operating Revenues	170.3	(0.2)	170.2	(83.1)
COMM CUST ACCT EXPENSES				
Common Customer Account	671.4	(274.6)	396.8	0.0
Postage	769.0	(17.6)	751.4	0.0
Operation Labor	2,232.7	(130.6)	2,102.1	574.3
TOTAL ADMIN & GENERAL EXPENSES				
All Other	287.7	(46.1)	241.6	0.0
Operating Expenses				
Office Supplies & Expense	2,380.7	(326.2)	2,054.6	0.0
Property Insurance	360.9	(0.7)	360.2	58.2
Injuries and Damages	2,572.7	(78.8)	2,493.9	227.2
Pension and Benefits	14,823.6	(1,163.4)	13,660.2	1,728.1
Business Meals	89.2	0.1	89.3	23.2
Regulatory Expenses	50.3	(14.5)	35.8	0.0
Outside Services	6,740.9	(1,042.9)	5,698.0	0.0
Miscellaneous	2,009.4	1.2	2,010.6	595.0
Maintenance of General Plant	793.3	(28.3)	765.0	0.0
Rent	246.3	0.0	246.3	224.6
A&G Capitalized	(2,171.9)	287.8	(1,884.1)	0.0
A&G Labor	7,915.1	(463.0)	7,452.0	2,035.8
Depreciation	1,705.1	(29.9)	1,675.2	304.5
Other Taxes				
Property Taxes	123.9	(2.8)	121.1	16.8
Payroll Taxes	821.6	(48.1)	773.6	211.3
Total Expenses	42,422.0	(3,378.5)	39,043.5	5,998.9
SAVINGS FROM CAPITAL PROJECTS	0.0	(31.4)	(31.4)	0.0
ADJUSTMENT FOR MISSED ALLOCATIC	0.0	0.0	0.0	2,978.2
ADJUSTMENT FOR CAPITALIZED EXPEL	0.0	0.0	0.0	0.0
Net Operating Revenues	(42,251.7)	3,409.7	(38,842.0)	(9,050.2)

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SUMMARY OF EARNINGS	DRA Stipulation	Change	DRA
AT PRESENT RATES:			
Operating Revenues	253.2	0.0	253.2
COMM CUST ACCT EXPENSES			
Common Customer Account	396.8	25.7	371.1

2007 Cal. PUC LEXIS 648, *

SUMMARY OF EARNINGS	DRA Stipulation	Change	DRA
Postage	751.4	0.0	751.4
Operation Labor	1,527.8	(21.8)	1,549.6
TOTAL ADMIN & GENERAL EXPENSES			
All Other Operating Expenses	241.6	86.9	154.7
Office Supplies & Expense	2,054.6	327.1	1,727.4
Property Insurance	302.0	19.1	282.9
Injuries and Damages	2,266.7	44.5	2,222.2
Pension and Benefits	11,932.1	1,825.9	10,106.2
Business Meals	66.1	0.0	66.1
Regulatory Expenses	35.8	(0.0)	35.8
Outside Services	5,698.0	2,374.6	3,323.4
Miscellaneous	1,415.6	(0.0)	1,415.6
Maintenance of General Plant	765.0	41.9	723.1
Rent	21.7	(0.0)	21.7
A&G Capitalized	(1,884.1)	(1,579.8)	(304.4)
A&G Labor	5,416.2	(77.3)	5,493.5
Depreciation	1,370.7	63.9	1,306.8
Other Taxes			
Property Taxes	104.3	21.6	82.7
Payroll Taxes	562.2	(8.0)	570.3
Total Expenses	33,044.6	3,144.4	29,900.2
SAVINGS FROM CAPITAL PROJECTS	(31.4)	125.4	(156.8)
ADJUSTMENT FOR MISSED ALLOCATIC	(2,978.2)	0.0	(2,978.2)
ADJUSTMENT FOR CAPITALIZED EXPEL	0.0	(1,260.5)	1,260.5
Net Operating Revenues	(29,781.7)	(2,009.3)	(27,772.4)

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APPENDIX B

2006 Capital Budgets

Golden State Water Company
2006 Capital Budget
Region II - Summary

Budget Group	Description	Proposed Budget	DRA Recommended	Settlement
	General			
51-	Water Supply	8,941,600	2,447,209	6,924,895
52-	Street Improvements	2,100,000	522,413	722,400
53-	Distribution Improvements	8,620,900	4,387,834	8,274,413
55-	Miscellaneous	2,172,700	583,000	1,612,700
57-	Contingency	914,000	563,300	660,250
	Total General	22,749,200	8,503,756	18,194,658
	New Business			
60-	New Business	1,540,000	1,540,000	1,540,000
	Less Funded by Others	(1,495,000)	(1,495,000)	(1,495,000)
	Net New Business	45,000	45,000	45,000
	Blankets			
B-01-	Meters	1,291,600	957,644	1,120,800
B-02-	Services	700,000	607,000	670,000
B-06-	Minor Main Replacements	1,300,000	1,099,750	1,300,000
B-07-	Minor Pumping Plant Equipment	19,000	9,000	19,000
B-08-	Minor Purification Equipment	25,000	10,000	25,000
B-09-	Office Furniture and Equipment	286,400	71,842	218,023

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B-10-	Transportation Equipment	1,076,600	714,100	886,000
B-11-	Other Equipment	203,600	145,587	168,106
B-12-	Minor Additions to General Structures	37,900	1,620	10,000
	Total Blankets	4,940,100	3,616,543	4,416,929
	Total Region II	27,734,300	12,165,299	22,656,587
	Total Gross Budget	29,229,300	13,660,299	24,151,587

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APPENDIX B

Golden State Water Company
2006 Capital Budget
Region II: Headquarters Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
57-	Contingency	15,000	1,500	2,550
	TOTAL CONTINGENCY	15,000	1,500	2,550
B-09-	Replace 40 PCs & 15 printers	70,000	49,397	59,500
B-09-	Replace Office Furniture for Managers	27,100	0	15,000
B-09-	Office furniture	15,000	0	15,000
B-09-	Replace Automatic Vehicle Location Units	25,000	0	0
B-11-	Global Positioning System Unit for Surveys - E & P Dept.	12,500	12,500	12,500
	TOTAL BLANKETS	149,600	61,897	102,000
	TOTAL NET COST	164,800	63,397	104,550

APPENDIX B

Golden State Water Company
2006 Capital Budget
Region II: Central District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
55-	Conservation	280,000	0	0
	TOTAL MISCELLANEOUS	280,000	0	0
57-	Contingency	50,500	6,200	11,400
	TOTAL CONTINGENCY	50,500	11,000	11,400
B-09-	Office Furniture and Equipment	20,000	5,300	5,300
B-10-	Vehicle Replacement No. 621 Mileage 124,833	33,000	33,000	33,000
B-10-	Vehicle Replacement No. 766 Mileage 120,922	48,100	0	0
B-10-	Vehicle Replacement No. 771 Mileage 125,649	48,100	0	48,100

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Golden State Water Company
2006 Capital Budget
Region II: Central District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-10-	Vehicle Replacement No. 1100 Mileage 100,145	35,900	0	0
B-11-	Miscellaneous tools and safety equipment	25,000	23,000	23,000
B-12-	Minor additions to general structures	15,000	500	5,000
	TOTAL BLANKETS	225,100	61,800	114,400
	TOTAL NET COST	555,600	68,000	125,800

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APPENDIX B

Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	Artesia			
51-	Elaine # 1 Destroy Well	76,400	20,970	30,300
51-	Haibrite - clear site	132,800	0	0
51-	Roseton - install 100 R. of discharge pipe for well # 1, design and construct	19,900	17,910	19,900
51-	Centralia - install reservoir safety rails	9,200	8,280	9,200
51.	Norwalk Dace - Replace fencing & main gate, site lighting, install alarm	116,300	36,900	41,000
51-	Imperial - Replace fencing & main gate, site lighting, install alarm	184,100	36,900	41,000
51-	Imperial - install reservoir safety rails	9,200	8,280	9,200
51-	Meyer - install reservoir safety rails	9,200	8,280	9,200
51-	Studebaker - Install drain line, Phase I - Design and Permit	63,600	0	63,600
51-	Studebaker - Security, fences, install alarm	106,500	36,900	41,000
51-	Pioneer - Treatment for 2 wells, Phase I - Design and Permit	218,000	196,200	218,000
51-	Pioneer - Security, fences, intrusion alarm et. al.	217,200	66,420	82,000
51-	Pioneer - Install drainline,	57,100	0	57,100

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	Phase I - Design and Permitting			
51-	CB-23 Connection - Install intrusion alarms	25,300	20,493	25,300
51-	CB 23 - Install operator interface on electrical cabinet	15,200	12,312	15,200
51-	CB 35- Replace fencing & main gate, site lighting, install intrusion alarms	41,000	33,210	41,000
51-	CBE Miscellaneous Bowl Replacement	60,000	35,100	39,000
	TOTAL WATER SUPPLY	1,361,000	538,155	742,000
52-	Miscellaneous Street Improvements	300,000	87,000	87,000
	TOTAL STREET IMPROVEMENTS	300,000	87,000	87,000
53-	Gate Valve Replacement	75,000	1,000	75,000
53-	Fire Hydrant Replacement	50,000	2,500	50,000
	Artesia (219)			
53-	Abandon 2" standard steel main and tie over 29 Services on Alburdis/205th/206th Design Review and Construct (21900193)	55,700	50,130	55,700

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	N/o Centralia e/o Pioneer 400' of 8" & 350' of 6" (21900293)	215,600	194,040	215,600
	Design Review and Construct			
53-	Ashworth from Grayland to Norwalk, 1050 ft. of 6" CI (City Request)	294,900	265,410	294,900
53-	Ibex from 183rd to 179th, 860 ft. of 8" Main (City Request)	259,400	233,460	259,400
53-	Norwalk from 183rd to Ashworth, 1200 ft. of 8" Main (City Request)	376,700	339,030	376,700
53-	180th from Ibex to Norwalk, 350 ft. of 8" Main (City Request)	160,100	144,090	160,100
	Norwalk (220)			
53-	Mondon Ct. 100' of 8" Main (22000215), Phase I - Design and Permit	20,200	20,200	20,200

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Spry West/Arlee 200' of 8" Main (22000216), Phase I - Design and Permit	19,000	19,000	19,000
53-	Imperial-Hwy, Zeus to Pioneer, 750' of 12" Main (22000190) Design Review and Construct	255,600	0	255,600
	TOTAL DISTRIBUTION IMPROVEMENTS	1,782,200	1,268,860	1,782,200
55-	Artesia Master Plan	156,800	0	156,800
55-	Norwalk Master Plan	153,900	0	153,900
55-	Install 23 Sample Stations	132,600	132,600	132,600
	TOTAL MISCELLANEOUS	443,300	132,600	443,300
57-	Contingency	130,000	79,900	104,700
	TOTAL CONTINGENCY	130,000	79,900	104,700
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	65,000	35,000	50,000
B-01-	Meter Replacement Program - Small	85,300	34,000	60,000
B-01-	Vault Lid Replacements	21,600	13,000	17,000

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-01-	Meter Replacement Program - Large (manifold replacement)	45,200	45,200	45,200
B-01-	Automatic Meter Reading	5,000	5,000	5,000
B-02-	Services	100,000	70,000	70,000
B-06-	Minor Main Replacement	100,000	32,000	100,000
B-07-	Minor Pumping Plant Equipment and Structures	3,000	3,000	3,000
B-08-	Minor Purification Equipment and Structures	3,500	3,500	3,500
B-09-	Office Furniture and Equipment	2,500	2,500	2,500
B-09-	Blackburn Crew Quarters Relocation	100,000	0	100,000
B-10-	New Vehicle	0	0	35,000
B-10-	Replace dump truck # 27 (1981)	89,900	89,900	89,900
B-10-	Mileage 55,840			
B-10-	Backhoe	98,700	98,700	98,700

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-11-	Cement Saw Cutter	5,000	5,000	5,000
B-11-	Air Compressor	15,000	15,000	15,000
	TOTAL BLANKETS	739,700	486,800	699,800
	TOTAL GROSS COST	5,016,200	2,818,315	4,119,000
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	4,786,200	2,568,315	3,869,000

Golden State Water Company
2006 Capital Budget
Region II - Central Basin West CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51-	Bell / Bell Gardens Bissell VOC Treatment for Well # 1 and Manganese Treatment for Well # 2 - and Chemical Building, Phase I - design and permit	203,500	78,890	87,700 (Advice Letter 115,800)
51-	Bissell 1 MG Storage Tank, Phase II - construct new tank	2,500,400	0	2,500,400
51-	Hoffman - Destroy Well	113,000	12,717	30,300
51-	Darwell - Clear site	40,000	0	0
51-	Chanslor - destroy well and clear site	123,400	37,722	46,600
51-	Florence-Graham Miramonte - replace pump base, install piping, convert to water-lube pump, replace pump house for Well # 1, Phase I - Design	57,000	0	48,000
51-	Hampshire - install reservoir safety rails	9,200	7,452	9,200
51-	CB-05 Connection - Install intrusion Alarm	25,200	20,412	25,200
51-	Hollydale Coolidge - Replace fencing, site lighting	195,500	4,050	5,000
51-	Paramount Connection - Install intrusion alarm	25,200	20,412	25,200
51-	Southgate Connection - Install intrusion alarms	25,200	20,412	25,200
51-	Willowbrook Willowbrook - Site lighting, install intrusion alarm	41,000	33,210	41,000
51-	CB-51 Connection - Install intrusion Alarm	25,200	20,412	25,200

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	CBW			
51-	Miscellaneous Bowl Replacement	80,000	47,700	53,000
	TOTAL WATER SUPPLY	3,463,800	303,389	2,922,000
52-	Miscellaneous Street improvements	300,000	152,000	152,000
	TOTAL STREET IMPROVEMENTS	300,000	152,000	152,000
53-	Gate Valve Replacement	100,000	7,000	100,000
53-	Fire Hydrant Replacement	50,000	3,000	50,000
	Bell / Bell Gardens			
53-	Woodward, Gage to Bell 1,400' of 12", Phase I - Design and Permit	55,500	0	55,500

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Golden State Water Company
2006 Capital Budget
Region II - Central Basin West CM

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Selfland - acq easement + 700' of 8" main + serv (22700170), Phase I - Design and Permit	32,800	32,800	32,800
53-	Florence Graham System 87th St, Central to Zamora 1,500' of 8" (22800173), Phase I - Design and Permit	28,800	0	0
53-	Nadeau from Bell Ave. to Maie 1,500' 12" (22800192) - Permit and Construction	388,600	0	388,600
53-	Beach - Replace 500 ft. of 4" Stl & 600 ft. of 2" Stl w/ 8 DIP from alley w/o Beach from 88th to Firestone, Phase I - Design and Permit	49,300	49,300	49,300
53-	Graham - Install 2250 ft. of 12" DIP from 92nd to Firestone. Phase I -Design and Permit	56,700	56,700	56,700
53-	Grape - Replace 1100 ft. of 2" Stl. w/ 8" DIP in alley w/o Gave between 88th & Firestone, Phase I - Design and Permit	52,100	52,100	52,100
53-	Hickory - Replace 1100 ft. of 2" Stl. w/ 8" DIP in alley w/o Hickory between 88th & Firestone, Phase I -Design and Permit	51,600	51,600	51,600
	Hollydale System			

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Golden State Water Company
 2006 Capital Budget
 Region II - Central Basin West CM

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Gardendale, Brock to Merkel, 800' of 12", Phase I - Design and Permit	52,900	0	0
53-	Harding/Paramount 250' 8" (22900092), Phase I - Design and Permit	25,900	25,900	25,900
53-	Main at Industrial 500' of 12" DI + RR (22900094), Phase I - Design and Permit	25,900	25,900	25,900
53-	Willowbrook System Grandee Ave. and 131st, 450' of 8" (23000122), Phase I - Design and Permit	26,000	26,000	26,000
	TOTAL DISTRIBUTION IMPROVEMENTS	996,100	330,300	914,400
55-	Bell/Bell Gardens Master Plan	108,000	0	108,000
55-	Florence-Graham Master Plan	156,800	0	156,800
55-	Hollydale Master Plan	104,100	0	104,100
55-	Willowbrook Master Plan	104,100	0	104,100
55-	Install 31 Sample Stations	178,700	178,700	178,700
	TOTAL MISCELLANEOUS	651,700	178,700	651,700
57-	contingency	145,900	105,500	116,700
	TOTAL CONTINGENCY	145,900	105,500	116,700
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	67,000	67,000	67,000
B-01-	Meter Replacement Program - Small	89,300	43,000	66,000
B-01-	Vault Lid Replacements	11,100	6,500	6,000
B-01-	Meter Replacement Program - Large (manifold replacement)	112,600	112,600	112,600
B-01-	Automatic Meter Reading	5,000	5,000	5,000
B-02-	Services	100,000	100,000	100,000
B-06-	Minor Main Replacement	100,000	11,000	100,000
B-07-	Meter Pumping Plant Equipment and Structures	3,000	3,000	3,000
B-08-	Minor Purification Equipment and Structures	3,500	3,500	3,500
B-09-	Office Furniture and Equipment	2,500	2,500	2,500
B-10-	Replace vehicle # 11- Dump truck	89,000	89,000	89,000
	Mileage 113,127			
B-10-	Replace vehicle - # 378 Mileage	35,000	0	0

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Golden State Water Company
 2006 Capital Budget
 Region II - Central Basin West CM

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	111,244			
B-10-	Replace vehicle - # 507 Mileage	35,000	0	0
	108,272			
B-10-	Replace vehicle - # 778 Mileage	36,000	0	0
	111,128			
B-10-	Replace vehicle - # 1023 Mileage	35,500	35,000	35,000
	125,687			
B-10-	Backhoe - replace # 9	98,700	98,700	98,700
B-11-	Light Tower (one)	14,000	14,000	14,000
B-11-	Air compressor (two) - replace old compressors	30,000	30,000	30,000
B-11-	Jack Hammer (three)	7,500	7,500	7,500
B-11-	Ditch pump (two)	4,200	4,200	4,200
B-11-	14" Power Saw (two)	2,800	2,800	2,800
B-11	Valve Machine	8,000	8,000	8,000
B-12	Security System - Upgrade for Bell Gardens office	11,000	0	0
	TOTAL BLANKETS	899,200	642,800	754,800
	TOTAL GROSS COST	6,716,700	1,972,689	5,771,600
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	6,466,700	1,722,689	5,521,600

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Golden State Water Company
 2006 Capital Budget
 Region II - Culver City CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51-	Sentney - security fences, lighting and intrusion alarm	274,700	33,210	41,000
51-	Ranch Rd - security fences, lighting and intrusion alarm	73,200	35,210	41,000
51-	Bernardo - security fences, lighting and intrusion alarm	69,400	33,210	41,000
51-	Baldwin Hill Plant Slope Stabilization, Phase I - Design and Permit	89,100	80,190	89,100
51-	WB-24 Connection - Install Intrusion Alarm	25,300	20,493	25,300
51-	WB-34 Connection - Install Intrusion. Alarm	25,300	20,493	25,300
	TOTAL WATER SUPPLY	557,000	220,806	262,700
52-	Miscellaneous street improvements	200,000	23,000	23,000
	TOTAL STREET IMPROVEMENTS	200,000	23,000	23,000

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Golden State Water Company 2006 Capital Budget Region II - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Gate Valve Replacement	100,000	14,000	100,000
53-	Hydrant Replacement	50,000	0	50,000
53-	Jacob. Helm to Sentney, 2,700' of 12", Phase I - Design and Permit	60,20	0	60,200
53-	Adams, Hines to Washington 500' of 8", Phase I - Design and Permit	42,500	42,500	42,500
53-	Overland, Oregon to Braddock, 2,100' of 12", Phase I - Design and Permit	55,600	0	0
53-	Fairbanks - replace 2000 ft. 6" CI w/ 8" DIP, Phase I - Design and Permit	57,400	0	57,400
53-	Dawes Ave. - replace 750 ft. of 4" CI with 8" DIP, Phase I - Design and Permit	46,800	46,800	46,800
53-	Dobson Way - replace 1000 ft. of 8" CI w/ 12" DIP, Phase I - Design and Permit	50,600	50,600	50,600
53-	Replace 700 ft. on Harter, 375 ft. on Franklin and 350 ft. of Franklin w/ 8" DIP, Phase I - Design and Permit	57,400	57,400	57,400
53-	Rhoda Way - 1700 ft. of 6" CI w/ 8" DIP, Phase I - Design and Permit	55,900	55,900	55,900
53-	Braddock Blvd, Irving & Van Buren to Overland, 5450' of 12" DIP, Phase II - Permit and Construction (funded by Chamock proceeds D.04-07-031)	1,195,700	0	1,195,700
53-	Ince Ave. & Culver Blvd., 180 ft. of 12" DIP, Phase II - Permit and Construction (funded by Chamock proceeds D.04-07.031)	75,300	67,770	75,300
53-	National Blvd., Washington to Wesley, 950 ft. of 12" DIP, Phase II - Permit and Construction (funded by Chamock proceeds D.04-07-031)	231,200	0	231,200
	TOTAL DISTRIBUTION IMPROVEMENTS	2,078,600	334,970	2,023,000
55-	Culver City Master Plan	101,200	0	101,200
55-	Install 11 Sample Stations	63,400	63,400	63,400
	TOTAL MISCELLANEOUS	164,600	63,400	164,600
57-	Contingency	114,800	75,800	88,500

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Golden State Water Company 2006 Capital Budget Region II - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	TOTAL CONTINGENCY	114,800	75,800	88,500
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	45,000	26,000	35,000
B-01-	Meter Replacement Program - Small	55,500	42,000	48,000
B-01-	Vault Lid Replacements	12,800	7,900	7,900
B-01-	Meter Replacement Program - Large (manifold replacement)	112,600	63,000	112,600
B-01-	Automatic Meter Reading	2,500	2,500	2,500
B-02-	Services	100,000	37,000	100,000
B-06-	Minor Main Replacement	100,000	100,000	100,000
B-07-	Minor Pumping Plant Equipment and Structures	3,000	3,000	3,000
B-08-	Minor Purification Equipment and Structures	3,000	3,000	3,000
B-09-	Office Furniture	2,500	2,500	2,500
B-10-	Replace vehicle # 454	69,200	69,200	69,200
	Mileage 152,783			
B-10-	Replace vehicle # 736	26,900	0	0
B-10-	Replace vehicle # 780	36,600	0	0
	Mileage 107,745			
B-10-	Replace backhoe # 7	98,700	98,700	98,700
B-11-	New portable air compressor	15,000	15,000	15,000
B-11-	Jackhammer	2,500	2,500	2,500
B-11-	Rockdrill	2,500	2,500	2,500
	TOTAL BLANKETS	688,300	474,800	602,400
	TOTAL GROSS COST	4,063,300	1,452,776	3,424,200
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	3,813,300	1,202,776	3,174,200

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APPENDIX B

Golden State Water Company 2006 Capital Budget Region II: Southwest District Office				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
55-	Conservation	280,000	0	0

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Golden State Water Company
2006 Capital Budget
Region II: Southwest District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	TOTAL MISCELLANEOUS	280,000	0	0
57-	Contingency	44,100	4,900	13,500
	TOTAL CONTINGENCY	44,100	4,900	13,500
B-09-	Office Furniture and Equipment	14,800	2,645	8,723
B-09-	Water Quality Laboratory Equipment	7,000	7,000	7,000
B-10-	Replace vehicle # 619 Mileage 116,611	35,000	0	35,000
B-10-	Replace vehicle # 730 Mileage 152,538	35,900	35,900	35,900
B-10-	New pool vehicle	26,900	0	26,900
B-11-	Miscellaneous tools and safety equipment	29,600	2,612	16,106
B-12-	Minor additions to general structures	11,900	1,120	5,000
	TOTAL BLANKETS	161,100	49,277	134,629
	TOTAL NET COST	485,200	54,177	148,129

TAPPENDIX B

Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51-	Doty Plant iron and manganese treatment, Phase I - Design Review and Permit	37,900	0	37,900
51-	Doty Plant Booster Station Phase I - Design and Permit	67,500	0	0
51-	Dalton - Drill & Develop Dalton Well # 2 and construct chemical building, Phase I - Design and Permit	245,300	0	0
51-	Wadsworth Replace Booster Station and Plant Piping, (25002149) Phase I - Design and Permit	191,800	75,595	75,595
51-	Ballona Plant - Discharge Piping	61,300	55,170	61,300
51-	Gardena Heights - install drainage system (25002259), Phase II - construction	498,400	0	498,400
51-	Goldmedal - install backwash	478,800	0	478,800

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Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	water storage tank, drain line and sitework (RWQCB Required)			
51-	Southern Plant - demo concrete storage tank, close three driveways and replace with curb and gutter (City Request)	355,500	36,180	355,500
51-	All Active Well and Reservoir Sites - Chloramination	1,010,800	818,748	1,010,800
51-	Process Control improvements			
51-	WB # 1 - Emergency Chlorination Station, Phase I - Design and Permit	83,000	0	Advice Letter
51-	Manhattan Plant - Slope grading and landscaping, Phase I - Design and Permit	15,500	13,950	15,500
51-	Chadron - Cost of Removal	364,000	294,840	364,000
51-	Miscellaneous Bowl Replacements	150,000	90,375	100,400
	TOTAL WATER SUPPLY	3,559,800	1,384,858	2,998,195
52-	Miscellaneous Street improvements - Southwest	1,300,000	260,413	460,400
	TOTAL STREET IMPROVEMENTS	1,300,000	260,413	460,400
53-	Gate Valve Replacements	300,000	212,278	256,139
53-	Fire Hydrant Replacements	200,000	92,748	146,374
	Compton			
53-	Compton Blvd., alley w/o Central Ave. to Dwight, 2,850' of 12", Phase I - Design and Permit	62,20	0	0

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APPENDIX B

Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	Gardena			
53-	166th St., Normandie to Berendo, 2,300' of 8", Phase I - Design and Permit	59,500	53,550	59,500
53-	162nd St between Normandie and Budlong, 1,250' of 12",	52,200	46,980	52,200

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Phase I - Design and Permit Purche Ave., Rosecrans to 141st., 500' of 8" (25002092),	20,600	0	20,600
53-	Phase I - Design and Permit Denker Ave., Marine Ave. to Redondo Bch. Blvd., 1.700' of	50,000	45,000	50,000
53-	12", Phase I - Design and Permit 149th St. from Western to HaWale. 1600' of 8". Phase I -	59,500	0	59,500
53-	Design and Permit 133rd St. - Eriel Ave east, 140' of 8",	77,500	62,775	77,500
53-	Design and Construct Vermont Ave. - Artesia north, 490' of 12", Design and	121,500	98,415	121,500
53-	Construct Hawthorne Grevillea and Burin Ave. n/o Imperial Hwy., 1,900' of 8",	53,000	0	53,000
53-	Inglewood Prairie, 104th to 111th, 2,600' of 12", Phase I - Design and	62,300	56,070	62,300
53-	Permit 95th Street from Ocean Gate to Redfern, 300' of 8", Design	96,000	77,760	96,000
53-	and Construct Lennox 104th St., Felton Ave. to Ocean Gate, 550' of 8". Phase I -	11,500	10,350	11,500
53-	Design and Permit Burl Ave. - Century Blvd. to Lennox, 1200' of 8". Design and	372,300	301,563	372,300
53-	Construct Burin Ave. - Centruy Blvd. to Lennox, 1200' of 8", Design	359,900	0	359,900

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	and Construct Lawndale Eastwood - 450' of 8" in easement and relocated Services			
53-		178,400	144,504	178,400
	on Eastwood Design and Construct (City Request) Freeman Ave., 165th St. to alley n/o Redondo Bch. Blvd.,			
53-		457,400	370,494	457,400
	1,650' of 8", Design review and construct (City Request) 162nd, Prairie to Sombra, 1800' of 8", Design review and			
53-		460,300	372,843	460,300
	construct (City Request) 160th, Prairie to Sombra, 2050' of 8", Design and Construct			
53-		497,400	402,894	497,400
	(City Request) County of Los Angeles/Rosewood Area			

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Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	El Segundo Blvd., Broadway to Main, 1,450' of 12" (25002024), Phase I - Design and Permit	49,500	0	0
53-	El Segundo Blvd., Towne Ave. to Avalon Blvd., 800' of 12", Phase I - Design and Permit	45,800	0	45,800
	County of Los Angeles/Woodcrest Area			
53-	120th e/o Budlong, 1,350' of 12", Phase I - Design and Permit	65,000	58,500	65,000
53-	108th St. Denker Ave. to alley w/o Western Ave., 1,500' of 12", Phase I - Design and Permit	52,200	46,980	52,200
	TOTAL DISTRIBUTION IMPROVEMENTS	3,764,000	2,453,704	3,554,813
55-	Southwest Master Plan	144,800	0	144,800
55-	Install 36 Sampling Stations	208,300	208,300	208,300
	TOTAL MISCELLANEOUS	353,100	208,300	353,100
57-	Contingency	413,700	292,100	322,900

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	TOTAL CONTINGENCY	413,700	292,100	322,900
60-	New Business Funded by SCWC	15,000	15,000	15,000
60-	New Business Funded by Others	745,000	745,000	745,000
	TOTAL NEW BUSINESS	760,000	760,000	760,000
B-01-	Meters - New Services & Replacement, Stuck	85,000	85,000	85,000
B-01-	Meter Replacement Program - Small	163,100	80,152	100,000
B-01-	Vault Lid Replacements	54,000	31,291	42,000
B-01-	Meter Replacement Program - Large (manifold replacement)	249,000	249,500	249,000
B-01-	Automatic Meter Reading - SW	5,000	5,000	5,000
B-02-	Services	400,000	400,000	400,000
B-06-	Minor Main Replacement	1,000,000	956,750	1,000,000
B-07-	Minor Pumping Plant Equipment and Structures	10,000	0	10,000
B-08-	Minor Purification Equipment and Structures	15,000	0	15,000
B-10-	Replace Vehicle # 270 Mileage 146,257	33,000	33,000	33,000
B-10-	Replace Vehicle # 272 Mileage 135,537	33,000	33,000	33,000
B-10- [*348]	New Vehicle	0	0	26,900

Golden State Water Company
2006 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-11-	Safety Equipment	30,000	975	10,000
	TOTAL BLANKETS	2,077,100	1,874,168	2,008,900
	TOTAL GROSS COST	12,227,700	7,230,944	10,458,308
	LESS NEW BUSINESS FUNDED BY OTHERS	745,000	745,000	745,000
	TOTAL NET COST	11,482,700	6,485,944	9,713,308

2007 Capital Budget

Golden State Water Company
2007 Proposed Capital Budget
Region II - Summary

Budget Group	Description	Proposed Budget	DRA Recommended	Settlement

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2007 Proposed Capital Budget
Region II - Summary

Budget Group	Description	Proposed Budget	DRA Recommended	Settlement
	General			
51-	Water Supply	14,464,900	5,181,337	9,302,000
52-	Street Improvements	1,800,000	524,413	936,400
53-	Distribution Improvements	11,529,300	5,614,963	9,319,100
55-	Miscellaneous	854,000	45,000	294,000
57-	Contingency	761,900	494,850	575,850
	Total General	29,410,100	11,860,5632	20,427,350
	New Business			
60-	New Business	1,545,000	1,545,000	1,545,000
	Less Funded by Others	(1,500,000)	(1,500,000)	(1,500,000)
	Net New Business	45,000	45,000	45,000
	Blankets			
B-01-	Meters	1,385,400	941,144	982,900
B-02-	Services	700,000	609,000	609,000
B-06-	Minor Main Replacements	1,300,000	1,099,750	1,300,000
B-07-	Minor Pumping Plant Equipment	19,000	9,000	19,000
B-08-	Minor Purification Equipment	25,000	10,000	25,000
B-09-	Office Furniture and Equipment	145,800	73,460	108,670
B-10-	Transportation Equipment	735,000	224,000	613,300
B-11-	Other Equipment	136,300	78,381	111,700
B-12-	Minor Additions to General Structures	66,900	1,660	40,000
	Total Blankets	4,513,410	3,046,394	3,809,570
	Total Region II	33,968,500	14,951,958	24,281,920
	Total Gross Budget	35,468,500	16,451,958	25,781,920

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Golden State Water Company
2007 Capital Budget
Region II: Headquarters Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
57-	Contingency	10,700	1,290	1,900
	TOTAL CONTINGENCY	10,700	1,290	1,900
B-09-	Replace 47 PCs & 15 printers	82,000	51,419	60,900
B-09-	Office furniture	25,000	0	15,000
	TOTAL BLANKETS	107,000	51,419	75,900

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2007 Capital Budget
Region II: Headquarters Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	TOTAL NET COST	117,700	52,709	77,800

Golden State Water Company
2007 Capital Budget
Region II: Central District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
55-	Conservation Projects	280,000	0	0
	TOTAL MISCELLANEOUS	280,000	0	0
57-	Contingency	40,800	6,500	13,400
	TOTAL CONTINGENCY	40,800	6,500	13,400
B-09-	Office Furniture	10,000	5,300	10,000
B-10-	Replace Vehicle # 1100	0	35,900	35,900
	Mileage 123,996			
B-10-	Replace Vehicle # 766	0	0	48,100
	Mileage 120,922			
B-10-	Replace vehicle # 769 Mileage	113,483	49,800	0
B-10-	Replace vehicle # 989	27,800	0	0
	Mileage 103,223			
B-11-	Misc. Tools & Safety Equipment	25,000	23,000	25,000
B-12-	Minor Additions to General Structures	15,000	500	15,000
	TOTAL BLANKETS	127,600	64,700	134,000
	TOTAL NET COST	448,400	71,200	147,400

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Golden State Water Company
2007 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51-	Artesia (219) Centralia - install new suction (seismic) to boosters	110,700	89,667	110,700
51-	Vine - Destroy Well Norwalk (220)	81,700	7,533	30,300
51-	Pioneer - install drainline, Phase II - Construction	378,200	0	378,200
51-	Pioneer - Install well			

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2007 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	treatment for two wells and relocate wellhead			
	treatment for one well - Phase II Construction	3,082,900	2,497,149	3,082,900
51-	Pioneer - (22000205)	377,400	0	269,500
51-	Construct two chemical buildings	235,300	0	181,200
51-	Construct chemical building	298,500	0	298,500
	Studebaker - install drainline, Phase II - Construction CBE			
51-	Miscellaneous - Bowls	60,000	35,100	39,000
	TOTAL WATER SUPPLY	4,624,700	2,629,449	4,390,300
52-	Miscellaneous Street Improvements	300,000	88,000	88,000
	TOTAL STREET IMPROVEMENTS	300,000	88,000	300,000
53-	Artesia (219)			
	221st st. from Arline Ave. to Clarkdale, 350 ft of 8" DI.			
	Phase I - Design and Permit	40,700	36,630	40,700
53-	Arline from 183rd St. south, 700 ft of 8" DI, Phase I-Design and Permit	36,900	33,210	36,900
53-	183rd from Seine Ave. to Elaine Ave., 600 ft of 8" DI, Phase I - Design and Permit	37,900	34,110	37,900
53-	179th from Horst to Norwalk, 650 ft of 8" DI, Phase I - Design and Penult	37,900	34,110	37,900
53-	Grayland from 183rd to Ashworth, 1200 ft of 8" DI, Phase I - Design and Permit	40,500	35,45	40,500
	Norwalk (220)			

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2007 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Mondon Ct. 100' 8" DI (22000215).	65,900	45,279	55,900
53-	Phase II - Construction Spry West/Arlee, 200 ft of 8" DI (22000216),	89,600	72,576	89,600
53-	Phase II-Construction Inez, Sundance to Lakeland Ave., 1,150 ft of 8",	37,600	03	7,600
53-	Phase I - Design and Permit Arlee, Tina to Allard, 550 ft of 10",			
	Phase I- Design and Permit CBE	36,900	0	36,900
53- [*351]	Valve replacements	75,000	900	75,000

APPENDIX B

Golden State Water Company
2007 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Fire hydrant replacements	70,000	2,250	70,000
	TOTAL DISTRIBUTION IMPROVEMENTS	558,900	295,515	558,900
57-	Contingency	84,700	51,000	57,800
	TOTAL CONTINGENCY	84,700	51,000	57,800
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	67,000	36,000	36,000
B-01-	Meter Replacement Program - Small	97,700	34,000	34,000
B-01-	Vault Lid Replacements	7,900	13,000	13,000
B-01-	Meter Replacement Program- Large (manifold replacement)	45,200	45,200	45,200
B-01-	Automatic Meter Reading	5,000	5,000	5,000
B-02-	Services	100,000	71,000	71,000
B-06-	Minor Main Replacement	100,000	32,000	100,000
B-07-	Minor Pumping Plant Equipment and Structures	3,000	3,000	3,000
B-08-	Minor Purification Equipment and Structures	3,500	3,500	3,500
B-09-	Office Furniture and Equipment	2,500	2,500	2,500

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2007 Capital Budget Region II - Central Basin East CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-09-	Office Renovation (paint, carpet, furniture)	5,000	5,000	5,000
B10-	Replace vehicle # 775 Mileage 108,368	37,600	0	0
B10-	Replace vehicle # 777 Mileage 103,352	37,600	0	0
B10-	Replace vehicle # 1029 Mileage 115,539	37,600	0	0
B10-	New Vehicle	37,600	0	0
	TOTAL BLANKETS	587,200	250,200	318,200
	TOTAL GROSS COST	6,415,500	3,574,164	5,885,200
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	6,165,500	3,324,164	5,635,200
51-	Bell/Bell Gardens (227) Bissell Well Treatment, Phase II - Construction Letter	2,381,100	830,056	1,025,900 (Advice 1,355,200)
51-	Watson - install drainline Florence-Graham (288)	357,300	0	0
51-	Miramonte - replace pump base, install piping, replace pump house for Well # 1, (22800160) Phase II - Construction	449,100	0	312,500
51-	Nadeau - Replace pump base (22800157) Hollydale (229)	128,200	0	0
51-	Coolidge - install new suction (seismic) to boosters Phase I - Design Willowbrook (230)	46,400	41,760	46,400
51-	Willowbrook - seismic upgrade, Phase I - Design and Permit CBW	46,400	41,760	46,400
51-	Masc. Bowls Replacement	80,000	47,700	53,000
	TOTAL WATER SUPPLY	3,488,500	962,176	1,484,300
52-	Miscellaneous street improvements	300,000	153,000	153,000
	TOTAL STREET IMPROVEMENTS	300,000	153,000	153,000
53-	Bell/Bell Gardens (277) Woodward, Gage to Bell 1,400' of 8". Phase II - Construction	411,100	0	411,100

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2007 Capital Budget Region II - Central Basin East CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Selfland - acquire easement 700' of 8" Main and relocate Services (22700170). Phase 11- Construction Florence-Graham (288)	130,200	105,462	130,200
53-	Beach, 88th to Firestone, 1100 ft. of 8". Phase II - Construction	302,800	245,268	302,800
53-	Graham, 92nd St to Firestone, 2250 ft. of 12". Phase II -Construction	645,300	522,693	645,300
53-	Grape, 88th and Firestone 1100 ft. of 8", Phase II - Construction	258,900	209,709	258,900
53-	Hickory, 88th and Firestone, 1100 ft. of 8", Phase II- Construction	260,400	210,924	260,400
53-	Hooper - Install 1600' of 12" DIP from 69th St. to Gage, Phase I - Design & Permit	67,300	60,570	67,300
53-	Ivy, 88th to Firestone, 900' of 8", Phase I - Design and Permit	61,000	54,900	61,000
53-	Benders, 87th to 88th, 550' of 8", Phase I - Design and Permit	59,700	53,730	59,700
53-	Hollydale (229)			
53-	Main at Industrial 500' of 12" + RR (22900094), Phase II - Construction	267,200	216,432	267,200
53-	Easement east of Paramount on n/s of Golden, Abandon 250 ft. of 2" Stl Pipe (22900077), Phase I - Design and Permit	8,300	7,470	8,300
53-	Willowbrook (230)			
53-	131st, w/o Grandee Ave. 450' of 8" (23000117), Phase II- Construction	169,500	137,295	169,500
53-	131st, w/o Grandee to Compton, 700 ft. of 8", Phase I - Design and Permit	50,500	45,450	50,500
53-	CBW			
53-	Valve Replacements	100,000	6,300	100,000
53-	Fire Hydrant Replacements	50,000	2,700	50,000
	TOTAL DISTRIBUTION IMPROVEMENTS	2,842,200	1,878,903	2,842,200
55-	Bissell - Install a new two-truck garage and warehouse. Phase I - Design and Permit	169,000	0	169,000
	TOTAL MISCELLANEOUS	169,000	0	169,000
57-	Contingency	73,900	61,560	74,150

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2007 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	TOTAL CONTINGENCY	73,900	61,560	74,150
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	69,000	69,000	69,000
B-01-	Meter Replacement Program - Small	75,500	43,000	43,000
B-01-	Vault Lid Replacements	7,900	6,000	7,900
B-01-	Meter Replacement Program - Large (manifold replacement)	112,600	112,600	112,600
B-01-	Automatic Meter Reading	5,000	5,000	5,000
B-02-	Services	100,000	100,000	100,000
B-06-	Minor Main Replacement	100,000	11,000	100,000

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APPENDIX B

Golden State Water Company
2007 Capital Budget
Region II - Central Basin West CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-07-	Minor Pumping Plant	3,000	3,000	3,000
	Equipment and Structures			
B-08-	Minor Purification	3,500	3,500	3,500
	Equipment and Structures			
B-09-	Office Furniture and Equipment	2,500	2,500	2,500
B-10-	Replace Vehicle 776			35,000
	mileage 126,030			
	TOTAL BLANKETS	479,000	355,600	481,500
	TOTAL GROSS COST	7,612,600	3,671,239	5,464,150
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	7,362,600	3,421,239	5,214,150

APPENDIX B

Golden State Water Company
2007 Capital Budget
Region II - Culver City CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51-	Baldwin Hill Plant Slope Stabilization. Phase II - Construction	1,047,500	848,475	1,047,500

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2007 Capital Budget Region II - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51- Permit	Perham - Slope stabilization. Phase I - Design and	105,700	95,130	105,700
	TOTAL WATER SUPPLY	1,153,200	943,605	1,153,200
52-	Miscellaneous street improvements	200,000	23,000	23,000
	TOTAL STREET IMPROVEMENTS	200,000	23,000	23,000
53- Construction	Jacob, Helm to Sentney, 2700 ft of 12", Phase II -	609,300	0	609,300
53-	Adams, Hines to Washington, 500 ft of 8", Phase II -	163,900	132,759	163,900
53-	Overland, Oregon to Braddock, 2,100 ft of 12", Phase II - Construction	588,200	0	0
53-	Dobson Way, 1000 ft of 8", Phase II - Construction	307,500	249,075	307,500
53-	Halter, Franklin & Farragut 1425 ft of 8", Phase II -	374,500	303,345	374,500
53-	Rhoda Way -1700 ft of 6" Cl wl 8" DIP, Phase II - Construction	415,600	336,636	415,600
53-	Hydrants Replacement	50,000	0	50,000
53-	Gate Valve Replacements	100,000	12,600	100,000
	TOTAL DISTRIBUTION IMPROVEMENTS	2,609,000	1,534,415	2,020,800
55-	Chamock - Build concrete stalls to hold bulk material (ie. Dirt, asphalt, base, Sand)	80,000	0	80,000
	TOTAL MISCELLANEOUS	80,000	0	80,000
57-	Contingency	71,500	61,500	61,500
	TOTAL CONTINGENCY	71,500	61,500	61,500
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded	250,000	250,000	250,000

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2007 Capital Budget Region II - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	by Others			
	TOTAL NEW BUSINESS	260,000	260,000	260,000

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APPENDIX B

Golden State Water Company 2007 Capital Budget Region II - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
8-01-	Meters - New Services & Replacement, Stuck	46,500	26,000	26,000
B-01-	Meter Replacement Program - Small	75,700	43,000	43,000
B-01-	Vault Lid Replacements	7,900	7,900	7,900
B-01-	Meter Replacement Program - Large (manifold replacement)	112,600	64,000	64,000
B-01-	Automatic Meter Reading	2,500	2,500	2,500
B-01-	Services	100,000	38,000	38,000
B-06-	Minor Main Replacement	100,000	100,000	100,000
B-07-	Minor Pumping Plant Equipment and Structures	3,000	3,000	3,000
B-08-	Minor Purification Equipment and Structures	3,000	3,000	3,000
B-09-	Office Furniture and Equipment	4,000	4,000	4,000
B-10-	Replace Vehicle # 736 Mileage 122778	0	26,900	26,900
B-10-	Replace Vehicle # 780 Mileage 122723	0	36,600	36,600
	TOTAL BLANKETS	455,200	354,900	354,900
	TOTAL GROSS COST	4,828,900	2,677,420	3,953,400
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	4,478,900	2,427,420	3,703,400

APPENDIX B

Golden State Water Company 2007 Capital Budget Region II: Southwest District Office				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
55-	Conservation	280,000	0	0
	TOTAL MISCELLANEOUS	280,000	0	0

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2007 Capital Budget Region II: Southwest District Office				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
57-	Contingency	42,000	4,200	5,400
	TOTAL CONTINGENCY	42,000	4,200	5,400
B-09-	Office Furniture and Equipment	14,800	2,741	8,770
B-10-	Replace Vehicle # 704	27,800	0	0
	Mileage 101,050			
B-10-	Replace Vehicle # 731	27,800	0	0
	Mileage 108,445			
B-10-	Replace Vehicle # 737	27,800	0	0
	Mileage 103,630			
B-10-	Replace Vehicle # 619	0	35,000	35,000
	Mileage 127,135			
B-11-	Miscellaneous tools and safety equipment	29,600	2,706	5,000
B-12-	Minor additions to general structures	11,900	1,160	5,000
	TOTAL BLANKETS	139,700	41,607	53,770
	TOTAL NET COST	461,700	45,807	59,170

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APPENDIX B

Golden State Water Company 2007 Proposed Capital Budget Region II - Southwest CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
51-	Doty Iron & Manganese Treatment, Phase II - Construction	1,264,300	0	1,264,300
51-	Dalton - Drill Well # 2 and construct chemical building, Phase II-Demolish Reservoir	972,300	0	0
51-	Chadron - Replace booster pump station and chemical building.	322,200	0	0
51-	Phase I - Design and Permit Chadron - replace drainage system for tank overflow,	50,300	45,270	50,300
51-	Phase I - Design and Permit Gardena Heights - replace two horizontal booster pumps A and B with vertical pumps and paving	503,900	0	0
51-	Replace, Yukon A and B booster pump	97,800	79,218	97,800
51-	Athens - install drainline, corrosion control chemical system and plant site paving	676,800	0	0
51-	Ballona - building demolition	68,400	61,560	68,400

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Golden State Water Company 2007 Proposed Capital Budget Region II - Southwest CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
	and paving, Phase I - Design and Permit			
51-	Budlong - Construct two 1.5 MG reservoirs, Phase - Design and Permit	236,600	0	236,600
51-	Manhattan - Slope grading and landscaping, Phase II - Construction	216,400	175,284	216,400
51-	WB # 1 - Emergency Chlorination Station. Phase II - Construction	389,500	0	Advice Letter
51-	Chadron - Cost of Removal	240,000	194,400	240,000
51-	Miscellaneous Bowls Replacement	160,000	90,375	100,400
	TOTAL WATER SUPPLY	5,198,500	646,107	2,274,200
52-	Miscellaneous Street Improvements - Southwest	1,000,000	260,413	460,400
	TOTAL STREET IMPROVEMENTS	1,000,000	260,413	460,400
53-	Compton Compton Blvd., alley w/o Central Ave. to Dwight, 2,850 of 12*, Phase II - Construction	798,000	0	0
53-	Gardena Purche Ave.. Rosecrans to 141st, 500' of 8" DIP (25002092), Phase I Construction	230,900	0	230,900
53-	Denker Ave., Marine. Ave. to Redondo Bch. Blvd., 1,700' of 12" DIP. Phase II - Construction	384,800	311,688	384,600
53-	149th, Western to Halldale, Phase II - Construction	306,900	0	306,900
53-	168th St, Mayflower to Vermont Phase I - Design & Permit	48,100	43,290	48,100
53-	New Hampshire, 168th to south end, Phase I - Design & Permit	44,700	40,230	44,700
53-	Catalina, 168th to south end, Phase I - Design & Permit	44,700	40,230	44,700
53-	Budlong, 168th to s/o 170th, Phase I - Design & Permit	44,700	40,230	44,700
53-	Re-Chlorination Stations, Phase I - Design & Permit Hawthorne	70,600	0	0

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APPENDIX B

Golden State Water Company
2007 Proposed Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
53-	Grevillea and Burin Ave. n/o Imperial Hwy., 1,900' of 8" DI, Phase II - Construction Inglewood	465,4000	0	465,400
53-	Prairie, 104th to 111th, 2,600' of 12" and 200' of 8" DI, Phase II - Construction County of Los Angeles/Lennox Area	819,800	664,038	819,800
53-	104th St., Felton Ave. to Ocean Gate, 550' of 8", Phase II - Construction County of Los Angles/Rosewood Area	156,700	126,927	156,700
53-	EI Segundo Blvd., Broadway to Main, 1,450' of 12" (25002024), Phase II - Construction County of Los Angles/Rosewood Area	511,800	0	0
53-	120th St. e/o Budlong, 1350' of 12" DI and valve vault at Budlong and 120th Phase II - Construction	401,600	325,296	401,600
53-	53-108th St., Denker Ave. to alley w/o Western Ave., 1,500' of 12", Phase II - Construction	441,500	357,615	441,500
53-	Darker Ave. 108th to 110th, 1,250' of 12", Phase I - Design and Permit	56,200	50,580	56,200
53-	107th - Vermont to Normandie, Phase I Design and Permit	55,900	50,310	55,900
53-	122nd - Vermont to Budlong, Phase I - Design and Permit Southwest	56,300	50,670	56,300
53-	Normandy Gradient Regulators Phase I -PDR, Design and Permit	80,600	0	0
53-	Gate Valves Replacements	300,000	212,278	235,900
53-	Fire Hydrant Replacements	200,000	92,748	103,100
		5,519,200	2,406,130	3,897,200
55-	Chadron - Add Storage Facilities in Building	45,000	45,000	45,000
		45,000	45,000	45,000

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2007 Proposed Capital Budget Region II - Southwest CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
57-	Contingency	438,300	308,800	361,700
		438,300	308,800	361,700
60-	New Business	15,000	15,000	15,000
	Funded by SCWC			
60-	New Business	750,000	750,000	750,000
	Funded by Others			
		765,000	765,000	765,000
B-01-	Meters - New Services and Repl., Small Stuck	87,500	87,500	87,500
B-01-	Meters - Small Replacements	306,400	80,152	120,000
B-01-	Vault Lid Replacement	23,500	31,291	31,300
B-01-	Meters - Large Replacements	225,000	225,000	225,000
B-01-	Meters - AMR for hard to read areas	5,000	5,000	5,000

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APPENDIX B

Golden State Water Company 2007 Proposed Capital Budget Region II - Southwest CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
B-02-	Services	400,000	400,000	400,000
B-06-	Minor main replacements	1,000,000	956,750	1,000,000
B-07-	Minor pumping plant replacements	10,000	0	10,000
B-08-	Minor purification	15,000	0	15,000
B-10-	Replace Vehicle # 469 Mileage 105,432	49,800	0	49,800
B-10-	Replace Vehicle # 790 Mileage 103,420	41,500	0	41,500
B-10-	Replace Vehicle # 791 Mileage 120,464	41,500	0	41,500
B-10-	Replace Vehicle # 981 Mileage 121,458	39,000	39,000	39,000
B-10-	Replace Vehicle # 1011 Mileage 120,819	37,600	37,600	37,600
B-10-	Replace Vehicle # 1101 Mileage 116,465	27,800	0	0
B-10-	Replace Vehicle # 265- Backhoe	88,300	88,300	88,300
B-10-	New Vehicle - Dump Truck	98,100	98,100	98,100
B-11-	Safety equipment	30,000	975	30,000
B-11-	3 New Jackhammers	2,800	2,800	2,800
B-11-	New Valve Machine, and valve vacuum cleaner	48,900	48,900	48,900
B-12-	Minor additions to general structures	40,000	0	20,000

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2007 Proposed Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Stipulation
		2,617,700	2,062,368	2,391,300
		15,583,700	6,493,819	10,194,800
	LESS NEW BUSINESS FUNDED BY OTHERS	750,000	750,000	750,000
		14,833,700	5,743,819	9,444,800

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APPENDIX B

2008 Capital Budget

Golden State Water Company
2008 Capital Budget
Region II - Summary

Budget Group	Description	Proposed Budget	DRA Recommended	Stipulation
	General			
51-	Water Supply	19,107,300	3,568,074	9,408,290
52-	Street Improvements	1,800,000	704,413	727,400
53-	Distribution Improvements	12,465,400	5,043,013	8,690,000
55-	Miscellaneous	965,700	-	405,700
57-	Contingency	790,700	573,260	580,980
	Total General	35,129,100	9,888,761	19,812,370
	New Business			
60-	New Business	1,545,000	1,545,000	1,545,000
	Less Funded Others	(1,500,000)	(1,500,000)	(1,500,000)
	Net New Business	45,000	45,000	45,000
	Blankets			
B-01-	Meters	1,233,800	949,344	994,200
B-02-	Services	700,000	672,000	672,000
B-06-	Minor Main Replacements	1,300,000	1,100,750	1,203,000
B-07-	Minor Pumping Plant	19,000	9,000	14,000
	Equipment			
B-08-	Minor Purification Equipment	25,000	10,000	15,000
B-09-	Office Furniture and	161,800	64,437	100,700
	Equipment			
B-10-	Transportation Equipment	360,700	231,800	499,100
B-11-	Other Equipment	134,300	76,440	82,700
B-12-	Minor Additions to General	66,900	1,686	15,000
	Structures			
	Total Blankets	4,001,500	3,115,457	3,595,700

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Golden State Water Company
2008 Capital Budget
Region II - Summary

Budget Group	Description	Proposed Budget	DRA Recommended	Stipulation
	Total Region II	39,175,600	13,049,217	23,453,070
	Total Gross Budget	\$ 40,675,600	\$ 14,549,217	\$ 24,953,070

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APPENDIX B

Golden State Water Company
2008 Capital Budget
Region II: Headquarters Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
57-	Contingency	17,100	1,300	1,920
	TOTAL CONTINGENCY	17,100	1,300	1,920
B-09-	Replace 47 PCs & 15 printers	82,000	51,236	61,900
B-09-	Office furniture	25,000	0	15,000
B-09-	Replace Automatic Vehicle Location Units	25,000	0	0
B-10-	Replace Vehicle # 1137 Mileage 102,440	38,500	0	0
	TOTAL BLANKETS	170,500	51,236	76,900
	TOTAL NET COST	187,600	52,536	78,820

APPENDIX B

Golden State Water Company
2008 Capital Budget
Region II. Central District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
55-	Conservation Projects	280,000	0	0
	TOTAL MISCELLANEOUS	280,000	0	0
57-	Contingency	38,200	7,700	12,500
	TOTAL CONTINGENCY	38,200	7,700	12,500
B-09-	Office Furniture	10,000	5,400	10,000
B-10-	Replace Vehicle # 982 mileage 108,641	51,500	0	0
B-10-	Replace Vehicle # 769	0	0	49,800
B-10-	Replace Vehicle # 771 mileage	0	48,100	0

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2008 Capital Budget
Region II. Central District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	125,649			
B-10-	Replace Vehicle # 775 mileage	0	0	37,600
	121.671			
B-11-	Misc. Tools & Safety Equipment	25,000	23,000	23,000
B-12-	Minor Additions to General Structures	15,000	500	5,000
	TOTAL BLANKETS	101,500	77,000	125,400
	TOTAL NET COST	419,700	84,700	137,900

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Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	Artesia (219)			
51-	Armstrong - Fencing	208,600	0	0
	CBE			
51-	Miscellaneous - Bowls	60,000	36,000	36,000
	TOTAL WATER SUPPLY	268,600	36,000	36,000
52-	Miscellaneous Street improvements	300,000	89,000	89,000
	TOTAL STREET IMPROVEMENTS	300,000	89,000	89,000
	Artesia (219)			
53-	221st St., Arline Ave. to Clarkdale, 350' of 8", Phase II - Construction	100,100	81,081	100,100
53-	Arline, 183rd St. south, 700' of 8", Phase II - Construction	178,700	144,747	178,700
53-	183rd, Seine Ave. to Elaine Ave., 600' of 8", Phase II - Construction	160,800	130,248	160,800
53-	179th, Horst to Norwalk, 650' of 8", Phase II - Construction	163,200	132,192	163,200
53-	Grayland, 183rd to Ashworth, 1200' of 8", Phase II - Construction	266,700	216,027	266,700
53-	Pioneer Blvd; South St to 195th St, 2000' of 18" & 500' of 12", Design Review and Construct	794,200	0	0

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Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budge Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
53-	Pioneer Blvd; 195th St to Los Coyotes, 1850' of 18", Design Review and Construct Norwalk (220)	703,500	0	0
53-	Inez, Sundance to Lakeland Rd., 1,150' of 8" DI, Phase II - Construction	291,100	0	291,100
53-	Arlee. Tina to Allard ,550' of 10" DI, Phase II - Construction	132,400	0	132,400
53-	Silverbow, Avonlea to Markdale, 1650' of 8". Phase I - Design and Permit	59,000	0	59,000
53-	Allard, Alley e/o Pioneer to Gwynne St, 150' of 10"& 800' of 8", Phase I - Design and Permit	50,700	0	50,700
53-	Avonia, Silverbow to Civic Center, 1150' of 8". Phase I - Design and Permit	56,300	0	56,300
53-	Bayla St, Brink Ave. to Gwynne Ave., 800' of 8", Phase I -Design and Permit	49,400	0	49,400
53-	Brink, Pantheon to Bombardier, 1950' of 8", Phase I - Design and Permit	58,200	0	58,200
53-	Goller Ave, Civic Center to Silverbow, 1450' of 8", Phase I - Design and Permit	58,200	0	58,200
53-	Inez, Sundance Ave. to it Florence Ave. North, 900' of 8", Phase I - Design and Permit	49,800	0	49,800
53-	Inez, Virginia to Lakeland, 520' of 8" & 150' of 6", Phase I - Design and Permit	50,200	0	05,200

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Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budge Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
53-	Kenney St., Brink Ave. to Bombardier Ave., 1100' of 8", Phase I - Design and Permit	53,900	0	53,900
53-	Leland and Sundance, Florence to Lakeland, 2250'	64,600	0	64,600

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budge Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	of 8", Phase I - Design and Permit			
53-	Markdale, Dace to Bloomfield, 3050' of 8", Phase I - Design and Permit	68,000	0	68,000
53-	Pantheon, Arlee to Gwynne, 1250' of 8", Phase I - Design and Permit	56,200	0	56,200
53-	Sproul, Esmond, Delavan, Silverbow, Belfair, Araby, Firestone, 5800' of 8", Phase I - Design and Permit	91,600	0	91,600
53-	Thistle, Dace, and Silverbow. 2800' of 8", Phase I - Design and Permit	71,100	0	71,100
53-	Volunteer and Dace, Civic Center to Silverbow, 2150' of 8", Phase I - Design and Permit	64,200	0	64,200
53-	Pluton, Brink to Bombardier, 850' of 8", Phase I - Design and Permit CBE	49,800	0	49,800
53-	Valve replacements	75,000	900	75,000
53-	Fere hydrant replacements	50,000	2,250	45,000
	TOTAL DISTRIBUTION IMPROVEMENTS	3,866,900	707,445	2,364,200
57-	contingency	95,700	67,100	63,900
	TOTAL CONTINGENCY	95,700	67,100	63,900
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	69,000	36,000	40,000
B-01-	Meter Replacement Program - Small	61,300	34,000	35,000
B-01-	Vault Lid Replacements	7,900	13,000	13,000
B-01-	Meter Replacement Program - Large (manifold replacements)	45,200	45,200	45,200
B-01-	Automatic Meter Reading	5,000	5,000	5,000
B-02-	Services	100,000	72,000	72,000
B-06-	Minor Main Replacement	100,000	33,000	33,000

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Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
B-07-	Minor Pumping Plant Equipment and Structures	3,000	3,000	3,000
B-08-	Minor Purification Equipment and Structures	3,500	3,500	3,500
B-09- [*361]	Office Furniture and Equipment	2,500	2,500	2,500

Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
B-10-	Replace Vehicle # 775	0	37,600	0
B-10-	Replace Vehicle # 1029 mileage 132,361	0	37,600	37,600
	TOTAL BLANKETS	397,400	322,400	289,800
	TOTAL GROSS COST	5,188,600	1,481,945	3,102,900
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	4,938,600	1,231,945	2,852,900

Golden State Water Company
2008 Capital Budget
Region II - Central Basin West CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
51-	Bell /Bell Gardens (227) Bissell - seismic retrofit new suction to boosters	151,600	122,796	151,600
51-	Florence-Graham (228) Converse - seismic retrofit new suction to boosters	149,100	120,771	149,100
51-	Miramonte - demolition elevated tank Hollydale (229)	779,500	631,395	779,500
51-	Coolidge - install new suction (seismic) to boosters Phase II - Construction	161,300	130,653	161,300
51-	Willowbrook (230) Willowbrook - seismic upgrades, Phase II - Construction	139,400	112,914	139,400
51-	CBW Misc. Bowls	80,000	48,600	48,600
	TOTAL WATER SUPPLY	1,460,900	1,167,129	1,429,500

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Golden State Water Company
2008 Capital Budget
Region II - Central Basin East CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
52-	Miscellaneous street improvements	300,000	155,000	155,000
	TOTAL STREET IMPROVEMENTS	300,000	155,000	155,000
53-	Florence-Graham (228) 87th St., Central to Zamora 1,500' of 8" (22800173), Phase II - Construction	306,100	0	0
53-	Hooper, 89th St., to Gage, 1,800 ft of 12", Phase II - Construction	483,900	391,959	483,900
53-	Ivy, 88th St. to Firestone, 900 ft. of 8", Phase II - Construction	226,100	183,141	226,100
53-	Bandera, 87th to 88th, 550 ft. of 8", Phase II - Construction	123,300	99,873	123,300
53-	Hollydale (229) Gardendale Avenue, Brock to Merkel Install, 800 ft of 12", Phase II - Construction	234,100	0	0
53-	Harding and Paramount 250 ft of 8" DIP (22900092), Phase II - Construction	115,500	93,555	115,500
53-	Easement east of Paramount n/s of Golden, Abandon 2" stt. (22800077), Phase II - Construction	51,100	41,391	51,100
53-	Century, Pennsylvania to Florence (22800091), 2200 ft of B", Review & Construct	448,700	0	448,700
53-	Willowbrook (230) 131st, Grandee to Compton, 700 ft of 8", Phase II - Construction	151,200	122,472	151,200

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Golden State Water Company
2008 Capital Budget
Region II - Central Basin West CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	CBW			
53-	Valve Replacements	100,000	6,300	75,000
53-	Fire Hydrant Replacements	50,000	2,700	45,000
	TOTAL DISTRIBUTION IMPROVEMENTS	2,290,000	941,391	1,719,800
55-	Bissell - Install a new two-truck garage and warehouse, Phase II - Construction	405,700	0	405,700
	TOTAL MISCELLANEOUS	405,700	0	405,700

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2008 Capital Budget
Region II - Central Basin West CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
57- Contingency		100,100	77,260	90,160
	TOTAL CONTINGENCY	100,100	77,260	90,160
60- New Business Funded by SCWC		10,000	10,000	10,000
60- New Business Funded by Others		250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01- Meters - New Services & Replacement, Stuck		71,000	71,000	71,000
B-01- Meter Replacement Program -Small		35,500	43,000	43,000
B-01- Vault Lid Replacements		7,900	6,000	6,000
B-01- Meter Replacement Program - Large (manifold replacement)		112,600	112,600	112,600
B-01- Automatic Meter Reading		5,000	5,000	5,000
B-02- Services		100,000	100,000	100,000
B-06- Minor Main Replacement		100,000	11,000	70,000
B-07- Minor Pumping Plant Equipment and Structures		3,000	3,000	3,000
B-08- Minor Purification Equipment Structures		3,500	3,500	3,500
B-09- Office Furniture and Equipment		2,500	2,500	2,500
B-10- Replace Vehicle # 378		0	0	35,000
B-10- Replace Vehicle # 507		0	0	35,000
	TOTAL BLANKETS	441,000	357,600	486,600
	TOTAL GROSS COST	5,257,700	2,958,380	4,546,760

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APPENDIX B

Golden State Water Company
2008 Capital Budget
Region II - Central Basin West CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
TOTAL NET COST	5,007,700	2,708,380	4,295,760	

APPENDIX B

Golden State Water Company
2008 Capital Budget
Region 9 - Culver City CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2008 Capital Budget Region 9 - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
51-	Perham - Slope stabilization, Phase II - Construction	1,911,300	1,648,153	1,911,300
51-	Ranch Rd - replace booster, Phase I - Design and Permit	19,000	17,100	19,000
51-	Sentney - demolish reservoirs, Design and Construction	397,600	322,056	397,600
	TOTAL WATER SUPPLY	2,327,900	1,887,309	2,327,900
52-	Miscellaneous street improvements	200,000	200,000	23,000
	TOTAL STREET IMPROVEMENTS	200,000	200,000	23,000
53-	Dawes Ave. McDonald to Port, 750 ft. of 8", Phase II - Construction	225,300	182,493	225,300
53-	Fairbanks, Dobson to Studio, 2,000 ft. of 8", Phase II - Construction	533,400	432,054	533,400
53-	Hydrant Replacement	50,000	45,000	45,000
53-	Valve Replacements	100,000	90,000	90,000
	TOTAL DISTRIBUTION IMPROVEMENTS	908,700	749,547	893,700
57-	Contingency	91,600	91,900	70,300
	TOTAL CONTINGENCY	91,600	91,900	70,300
60-	New Business Funded by SCWC	10,000	10,000	10,000
60-	New Business Funded by Others	250,000	250,000	250,000
	TOTAL NEW BUSINESS	260,000	260,000	260,000
B-01-	Meters - New Services & Replacement, Stuck	48,000	48,000	48,000
B-01-	Meter Replacement Program - Small	39,800	43,000	43,000
B-01-	Vault Lid Replacements	7,900	7,900	7,900
B-01-	Meter Replacement Program - Large (manifold replacement)	112,600	112,600	112,600
B-01-	Automatic Meter Reading	2,500	2,500	2,500
B-02-	Services	100,000	100,000	100,000
B-06-	Minor Main Replacement	100,000	100,000	100,000

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APPENDIX BGolden State Water Company
2008 Capital Budget

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Region II - Culver City CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
B-07-	Minor Pumping Plant	3,000	3,000	3,000
	Equipment and structures			
B-08-	Minor Purification	3,000	3,000	3,000
	Equipment and Structures			
B-10-	Replace Vehicle # 779	38,900	38,000	0
	mileage 108,949			
	TOTAL BLANKETS	455,700	458,900	420,000
	TOTAL GROSS COST	4,243,900	3,647,656	3,994,900
	LESS NEW BUSINESS FUNDED BY OTHERS	250,000	250,000	250,000
	TOTAL NET COST	3,993,900	3,397,656	3,744,900

Golden State Water Company
2008 Capital Budget
Region II: Southwest District Office

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
55-	Conservation	280,000	0	0
	TOTAL MISCELLANEOUS	280,000	0	0
57-	Contingency	37,500	9,000	13,000
	TOTAL CONTINGENCY	37,500	9,000	13,000
B-09-	Office Furniture and Equipment	14,800	2,801	8,800
B-10-	Replace Vehicle # 705 Mileage	38,900	0	0
	101,187			
B-10-	Replace Vehicle # 704	0	27,800	27,800
B-10-	Replace Vehicle # 731	0	27,800	27,800
B-10-	Replace Vehicle # 737	0	27,800	27,800
B-10-	Replace Vehicle # 1101	0	0	27,800
B-11-	Miscellaneous tools and safety equipment	29,600	2,766	5,000
B-12-	Minor additions to general structures	11,900	1,186	5,000
	TOTAL BLANKETS	95,200	90,152	130,000
	TOTAL NET COST	412,700	99,152	143,000

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Golden State Water Company
2008 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
51-	Doty Plant 2.5 MG reservoir & Booster Station, Phase II -	3,629,000	0	0

2007 Cal. PUC LEXIS 648, *

Golden State Water Company 2008 Capital Budget Region II - Southwest CSA				
Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	Construction			
51-	Chadron - Replace booster pump station and chemical building, Phase II - Construction	801,500	0	0
51-	Chadron - replace drainage system for tank overflow, Phase II - Construction	143,500	116,235	143,500
51-	Dalton - Drill and equip Well # 2 and construct chemical building, Phase III - Drill and Equip Well	1,246,700	0	0
51-	Ballona - building demolition and paving - Phase II - Construction	114,600	92,826	114,600
51-	Budlong - Construct two 1.5 MG reservoirs, Phase II - Construction	4,150,300	0	4,150,190
51-	Goldmedal - 4-Cell Chemical	442,700	0	325,200
51-	Building, Phase II - Construction			
51-	Wadsworth - Booster Station & Plant	570,200	0	0
51-	Piping, Phase II - Construction			
51-	Yukon - 4-Cell & 2-Cell Chemical Buildings, Phase II - Construction	561,400	0	561,400
51-	Southwest System Water Quality Improvement Projects	3,000,000	0	0
51-	Chadron - Cost of Removal	220,000	178,200	220,000
51-	Miscellaneous Bowls	170,000	90,375	100,000
	TOTAL WATER SUPPLY	15,049,900	477,636	5,614,890
52-	Miscellaneous Street Improvements - Southwest	1,000,000	260,413	460,400
	TOTAL STREET IMPROVEMENTS	1,000,000	260,413	460,400
53-	Gardena			
53-	166th St., Normandie to Berendo, 2,300 of 8" DIP, Phase II - Construction	523,100	423,711	523,100
53-	162nd St between Normandie and Budlong, 1250' of 12" DIP, Phase II - Construction	388,500	313,065	386,500
53-	Van Ness Ave. - Marine to 147th, 1,350 ft. of 8" DI, Phase I - Design and Permit	53,800	0	53,800
53-	St. Andrew Pl. - Rosecrans to 150th, 2,400 ft. of 8" DI, Phase I - Design and Permit	63,800	0	63,800
53-	144th St. - Gramercy to St. Andrew, 300 ft. of 8" DI, Phase I - Design and Permit	44,700	0	44,700

2007 Cal. PUC LEXIS 648, *

Golden State Water Company
2008 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
53-	168th St - Vermont to Mayflower, 2,200 ft of 8", Phase II - Construction	524,700	425,007	524,700
53-	New Hampshire -168th to s/o 170th, Abandon 4" CI, Phase II - Construction	98,000	79,380	98,000
53-	Catalina Ave, 168th to south end, 650 ft of 8", Phase II - Construction	186,200	150,822	186,200
53-	Budlong Ave. 168th to 170th, 850 ft of 8", Phase II - Construction	227,600	184,356	227,600
53-	Re-Chlorination Stations - Phase II - Construction	963,800	0	0
53-	County of Los Angles/Rosewood Area El Segundo Blvd., Towne Ave. to Avalon Blvd., 800' of 12", Phase II - Construction	238,600	0	238,600

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Golden State Water Company
2008 Capital Budget
Region II - Southwest CSA

Budget Group	DESCRIPTION	Proposed Budget	DRA Recommended	Settlement
	TOTAL GROSS COST	24,965,400	6,631,148	12,948,790
	LESS NEW BUSINESS FUNDED BY OTHERS	750,000	750,000	750,000
		24,215,400	5,881,148	12,198,790

APPENDIX C

GOLDEN STATE WATER COMPANY

2006 Capital Budget

General Office

Budget Group	Description	Department	GSWC Request	DRA Recommended	Stipulation
	Phase I - New CIS/CRM System				
55-	Implementation	C S C	3,633,100	0	TBD
	E-Leaming Hosted on Internet				
55-	(Harvard or E-Comell)	EDU	39,400	0	TBD
	(2) Videoconference Systems (Bear Valley & Santa Maria)				
55-	Develop/Purchase	EDU	26,700	0	TBD

2007 Cal. PUC LEXIS 648, *

Budget Group	Description	Department	GSWC Request	DRA Recommended	Stipulation
55-	new training EDU modules TOTAL	26,000	0	TBD	
	MISCELLANEOUS		3,725,200	0	
57-	Contingency		176,500	60,000	TBD
	TOTAL CONTINGENCY		176,500	60,000	
	Workstations (10) - Replacements				
B-09-		ACCT/FINANCE	17,100	11,400	11,400
	w/monitor New Workstations (3) - Financial				
B-09-		ACCT/FINANCE	5,100	0	0
	Analyst/Financial Mgr/Tax Analyst				
B-09-	Scanner for documentation software Desktop (6) Printers Replacement	ACCT/FINANCE	5,800	5,800	5,800
B-09-		ACCT/FINANCE	6,700	2,233	2,233
	and (3) New for new employees				
B-09-	Department Printer Replacement Check Printer Replacement -	ACCT/FINANCE	3,400	3,400	3,400
B-09-		ACCT/FINANCE	5,100	5,100	5,100
	Payroll				
B-09-	Furniture Replacement	ACCT/FINANCE	6,200	0	0
B-09-	Web Server Contract Management Migration	ACCT/FINANCE	29,200	29,200	29,200
B-09-		ACCT/FINANCE	171,000	171,000	171,000
	from Citrix to Web				
B-09-	EAM - Graphical Interface Migration of Enterprise One from	ACCT/FINANCE	107,400	107,400	107,400
B-09-		ACCT/FINANCE	490,700	490,700	490,700
	XE to ERP8.11				
B-09-	Cetova Software Human Resources - Self Services	ACCT/FINANCE	130,700	130,700	130,700
B-09-		ACCT/FINANCE	267,500	267,500	267,500
	including Position control				
B-09-	Q4bis Budgeting Software upgrade	ACCT/FINANCE	42,800	42,600	42,600

2007 Cal. PUC LEXIS 648, *

Budget Group	Description	Department	GSWC Request	DRA Recommended	Stipulation
B-09-	Digital Overhead Projector	CAPITAL PROJECTS	1,900	0	TBD
B-09-	Four (4) 4-drawer Lateral File Cabinets	CAPITAL PROJECTS	4,500	0	TBD
B-09-	Primavera Sure Trak Project Manager Software	CAPITAL PROJECTS	22,200	0	TBD
B-09- [*367]	Digital camera	CAPITAL PROJECTS	2,100	0	TBD

APPENDIX C**GOLDEN STATE WATER COMPANY****2006 Capital Budget****General Office**

Budget Group	Description	Department	GSWC Request	DRA Recommended	Stipulation
B-09-	Task Chairs (2)	CAPITAL PROJECTS	1,100	0	TBD
B-09-	Workstation (1) - Replacement	CAPITAL PROJECTS	1,700	0	TBD
B-09-	Ph. 1 - Integrated Conservation Database	CONSERVATION	44,800	0	0
B-09-	Replace PCs (25)	C S C	42,700	17,649	17,649
B-09-	Shared Printing Equipment	C S C	4,700	4,700	4,700
B-09-	Office Space for new Workstations	C S C	71,600	0	TBD
B-09-	Total Fax Solution	C S C	30,000	30,000	30,000
B-09-	Teleworking CSR Equipment & Software	C S C	7,100	7,100	7,100
B-09-	Laptop PC for EDU staff Off-site training replacement	EDU	3,600	0	TBD
B-09-	-[ILLEGIBLE WORDS] Staff PCs	EDU	4,800	0	TBD
B-09-	25 Classroom chairs replacement (G.O.)	EDU	12,700	0	TBD
B-09-	Staff PC (3) replacements	EDU	7,700	0	TBD
B-09-	Training videos to augment classroom learning (5)	EDU	6,400	0	TBD
B-09-	Database replacement PC	EDU	2,600	0	TBD
B-09-	Workstation (3) -Replacements	Executive Office	5,100	5,100	5,100
B-09-	Space Planning	HR	16,800	16,800	16,800
B-09-	Workstations -	HR	3,400	0	TBD

2007 Cal. PUC LEXIS 648, *

Budget Group	Description	Department	GSWC Request	DRA Recommended	Stipulation
	New (2)				
B-09-	Office Workstations	HR	10,400	0	TBD
B-09-	Network Printer	HR	1,700	1,700	1,700
B-09-	Comparison Software	HR	3,200	3,200	3,200
B-09-	Retile & Refixture 2 Bathrooms	INFO. TECH.	58,000	0	0
B-09-	Replace Counter Tops in Cafeteria, Mail area	INFO. TECH.	7,900	0	0
B-09-	Banc Tec Cash Processing Unit w/Imaging	INFO. TECH.	357,900	0	0
B-09-	Repl Five-year old servers(3)	INFO. TECH.	56,800	56,800	56,800
B-09-	Repl Five-year old remote servers(2)	INFO. TECH.	37,900	37,900	37,900
B-09-	Expansion of Storage Area Network	INFO. TECH.	159,100	159,100	159,100
B-09-	Model Upgrade for AS/400 820 System	INFO. TECH.	231,800	231,800	231,800
B-09-	Office & Technet License Renewal	INFO. TECH.	295,600	295,600	295,600
B-09-	Replace 5 Workstations	INFO. TECH.	8,500	8,500	8,500
B-09-	Doc Mgmt - HR. Reg Affairs & Inventory	INFO. TECH.	52,700	52,700	52,700

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APPENDIX C

GOLDEN STATE WATER COMPANY

2006 Capital Budget

General Office

Budget Group	Description	Department
B-09-	Replace Pitney Bowes Paragon	INFO. TECH.
	Mailing Machine	
B-09-	IBM Laptop PC for Senior Auditor	INT AUDIT
B-09-	Office Furniture Replacement	INT AUDIT
B-09-	Laserjet Printer	INT AUDIT
B-09-	Desk with return and Credenza (1)	
	PREVENTIVE MAINT	
	Manager	
B-09-	High Back Task Chairs (2)	PREVENTIVE MAINT
B-09-	PC Workstations Replacement	
	PREVENTIVE MAINT	
	w/monitor (1)	
B-09-	New 5-drawer & 2-drawer lateral	PREVENTIVE MAINT
	files	
B-09-	Laptop PC replacement (2)	PREVENTIVE MAINT
B-09-	Table with base and chairs	PREVENTIVE MAINT

2007 Cal. PUC LEXIS 648, *

Budget Group	Description	Department
	ORDOM, SCADA, SQUID & EAM	
B-09-		PREVENTIVE MAINT
	Intergration	
	PCs Workstations - Replacements	
B-09-		REGULATORY AFFAIRS
	(3)	
B-09-	Safety Training Videos	RISK MANAGEMENT
B-09-	Safety and Testing Equipment	RISK MANAGEMENT
B-09-	Workstations with furniture	RISK MANAGEMENT
	PC Workstations Replacement	
B-09-		RISK MANAGEMENT
	w/monitor (1)	
B-09-	Digital Camera	RISK MANAGEMENT
B-09-	GPS for Company Vehicles	SECURITY
B-09-	Compliance Software	WATER QLTY.
	Furniture Replacement - VP Water	
B-09-		WATER QLTY.
	Quality	
	Auto Replacement - Replace	
B-10-		CAPITAL PROJECTS
	vehicle # 1100	
	Auto Replacement - 2000 windstar	
B-10-		INFO. TECH.
	Pool Van	
	Total Blankets	
	2006 Total G.O. Budget	

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Budget Group	GSWC Request	DRA Recommended	Stipulation
B-09-	46,800	46,800	46,800
B-09-	3,100	0	TBD
B-09-	14,500	0	TBD
B-09-	500	0	TBD
B-09-	3,100	2,400	
B-09-	2,600	0	2,000
B-09-	1,700	0	1,300
B-09-	2,400	0	1,900
B-09-	6,100	6,100	6,100
B-09-	3,100	0	2,400
B-09-	58,200	68,200	58,200
B-09-	5,100	5,100	5,100
B-09-	6,600	6,600	6,600
B-09-	28,000	5,700	14,000

2007 Cal. PUC LEXIS 648, *

Budget Group	GSWC Request	DRA Recommended	Stipulation
B-09-	10,200	5,100	TBD
B-09-	1,700	0	TBD
B-09-	1,500	1,500	1,500
B-09-	217,600	0	72,500
B-09-	46,700	46,700	46,700
B-09-	13,400	0	0
B-10-	34,500	0	TBD
B-10-	39,000	0	39,000
	3,437,100	2,400,683	
	7,338,800	2,460,683	

APPENDIX C

GOLDEN STATE WATER COMPANY

2037 Capital Budget

General Office

Budget Group	Description	Department
	Phase II - Implementation of new	
55-	CIS/CRM System Implementation	C S C
	E-Learning Hosted on Internet	
55-	(Harvard or E-Comell)	EDU
	Develop/purchase new training	
55-	modules	EUD
	Online topics (electronic job aids)	
55-	for field operations	EDU
	TOTAL MISCELLANEOUS	
57-	Contingency	
	TOTAL CONTINGENCY	
	Workstations (10) - Replacements	
B-09-	w/monitor	ACCT / FINANCE
B-09-	Furniture Replacement	ACCT / FINANCE
B-09-	Desktop (6) Printers Replacement	ACCT / FINANCE
	Check Printer Replacement -	
B-09-	ACCT / FINANCE	
	Accounts Payable	
	Enterprise One - Additional Web	
B-09-	ACCT / FINANCE	
	Modules Upgrade	
B-09-	Create Form - Software Upgrade	ACCT / FINANCE

2007 Cal. PUC LEXIS 648, *

Budget Group	Description	Department
B-09-	Showcase Vista - Software ACCT/FINANCE upgrade	
B-09-	EAM Graphical Interface ACCT / FINANCE Enhancement	
B-09-	Installation of Tax Software Desk with return & credenza -	ACCT/ FINANCE
B-09-	Replacement	CAPITAL PROJECTS
B-09-	Lateral file cabinets (4)	CAPITAL PROJECTS
B-09-	Workstation (1)	CAPITAL PROJECTS
B-09-	Desk & task chair	CAPITAL PROJECTS
B-09-	Ph. 2. Expansion of Integrated CONSERVATION Conservation Database	
B-09-	Replace PCs (8)	C S C
B-09-	Shared Printing Equipment	C S C
B-09-	Property identification Software	C S C
B-09-	Call Recording & Monitoring C S C	
B-09-	Equipment - replacement	

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Budget Group	GSWC Request	DRA Recommended	Stipulation
55-	3,815,70	0	TBD
55-	41,100	0	TBD
55-	29,400	0	TBD
55-	34,500	0	TBD
	3,920,700	0	
57-	96,300 96,300	31,300 31,300	TBD
B-09-	17,800	11,867	11,867
B-09-	4,300	0	0
B-09-	4,600	4,600	4,600
B-09-	5,300	5,300	5,300
B-09-	68,700	0	34,350

2007 Cal. PUC LEXIS 648, *

Budget Group	GSWC Request	DRA Recommended	Stipulation
B-09-	18,200	18,200	18,200
B-09-	28,500	14,250	14,250
B-09-	62,500	0	31,250
B-09-	432,500	432,500	432,500
B-09-	3,200	0	TBD
B-09-	4,600	0	TBD
B-09-	1,800	0	TBD
B-09-	600	0	TBD
B-09-	101,400	0	0
B-09-	14,300	14,300	14,300
B-09-	5,300	5,300	5,300
B-09-	7,000	7,000	7,000
B-09-	234,400	234,400	234,400

APPENDIX C

GOLDEN STATE WATER COMPANY

2007 Capital Budget

General Office

Budget Group	Description	Department
B-09-	LCD Projector& Computer (Region II) Replacement PC Lab & Training Room	EDU
B-09-	Staff PC replacements (3)	EDU
B-09-	Training Videos (5)	EDU
B-09-	Printer for PC Lab (Region II)	
B-09-	Document scanner w/feeder for Dean	EDU
B-09-	Career Development Online System	EDU
B-09-	Workstations - Replacement (3)	H R
B-09-	Fax Machine Replacement	H R
B-09-	Retile & Refixture 2 Bathrooms	INFO. TECH.
B-09-	Repl A/C Water Source Hearing Pumps(3)	INFO. TECH.
B-09-	Replace Cafeteria Furniture	INFO. TECH.
B-09-	Replace 12 year old Office Furniture	INFO. TECH.
B-09-	Repl Five-year old servers(3)	INFO. TECH.
B-09-	Rapt Five-year old remote servers(2)	INFO. TECH.
B-09-	Memory & Disk upgrade for AS/400	INFO. TECH.

2007 Cal. PUC LEXIS 648, *

Budget Group	Description	Department
	820	
B-09-	Replace 5 Workstations	INFO. TECH.
B-09-	Microsoft OS & Database License	INFO. TECH.
B-09-	Renewal	INFO. TECH.
B-09-	Replace 2 Laptop Computers	PREVENTIVE MAINT
B-09-	Laser printer/fax/Scanner/copter	REGULATORY AFFAIRS
B-09-	PCs Workstations-Replacements	(4)
B-09-	Replace 4 chairs	REGULATORY AFFAIRS
B-09-	Safety Training Videos	RISK MANAGEMENT
B-09-	Safety and Testing Equipment	RISK MANAGEMENT
B-09-	Compliance Software - Phase	WATER QLTY.
B-09-	GPS for Company Vehicles	SECURITY
B-10-	Auto Replacement 2002 WS Pool	INFO. TECH.
B-10-	Van	
B-10-	Replace Vehicle # 1118	PREVENTIVE MAINT
	Total Blanket	
	2007 Total General Office	

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Budget Group	GSWC Request	DRA Recommended	Stipulation
B-09-	31,700	0	TBD
B-09-	8,100	0	TBD
B-09-	7,400	0	TBD
B-09-	2,600	0	TBD
B-09-	2,400	0	TBD
B-09-	69,300	0	TBD
B-09-	5,400	5,400	5,400
B-09-	3,100	3,100	3,100
B-09-	60,500	0	0
B-09-	18,200	18,200	18,200
B-09-	5,700	0	0
B-09-	27,100	0	0
B-09-	59,300	59,300	59,300
B-09-	39,500	39,500	39,500
B-09-	114,300	114,300	114,300
B-09-	8,900	8,900	8,900
B-09-	190,900	190,900	190,900

2007 Cal. PUC LEXIS 648, *

Budget Group	GSWC Request	DRA Recommended	Stipulation
B-09-	4,900	4,900	4,900
B-09-	5,100	0	0
B-09-	7,100	7,100	7,100
B-09-	2,200	2,200	2,200
B-09-	6,800	6,800	8,800
B-09-	20,900	5,700	10,450
B-09-	27,000	0	27,000
B-09-	0	0	74,400
B-10-	40,700	0	0
B-10-	36,000	36,000	36,000
	1,820,100	1250,017	
	5,837,100	1,281,317	

GOLDEN STATE WATER COMPANY

2008 Capital Budget

General Office

BUDGET GROUP	DESCRIPTION	DEPARTMENT	GSWC Request	DRA Recommended	Stipulation
55-	Final Phase - Implementation of new CIS/CRM System	C S C	3,730,200	0	TBD
55-	Implementation of E-learning Hosted on the Internet (Harvard and other vendors)	EDU	36,800	0	TBD
55-	Curriculum Development (Purchase/ Development costs for Management and Operations Coursework)	EDU	59,400	0	TBD
	TOTAL MISCELLANEOUS		3,826,400	0	
57-	Contingency		42,700	9,000	TBD
	TOTAL CONTINGENCY		42,700	9,000	
B-09-	Workstations (10) - Replacements w/monitor	ACCT / FINANCE	17,600	11,867	11,867
B-09-	Desktop (10) Printers	ACCT I FINANCE	7,700	7,700	7,700
B-09-	Replacement Check Printer	ACCT / FINANCE	5,300	5,300	5,300
B-09-	Replacement - Payroll Enterprise One - Software Upgrade	ACCT/ FINANCE	67,200	33,600	33,600

2007 Cal. PUC LEXIS 648, *

BUDG- ET GROUP	DESCRIPTION	DEPARTMENT	GSWC Request	DRA Recommended	Stipulation
B-09-	HR Self Service enhancement	ACCT/ FINANCE	61,100	30,550	30,550
B-09-	Web Server (3) Upgrade	ACCT / FINANCE	30,400	0	15,200
B-09-	Laptop PCs (2)	CAPITAL PROJECTS	6,700	0	TBD
B-09-	Ph. 3 - Integrated Conservation Database	CONSERVATION	132,200	0	0
B-09-	Replace PCs (8)	C S C	14,200	14,200	14,200
B-09-	Call Center Workforce Management Software	C S C	73,600	73,600	73,600
B-09-	Teleworking CSR Equipment & Software	C S C	7,400	7,400	7,400
B-09-	Replacement of EDU Portable LCD Projector for offsite training	EDU	6,600	0	TBD
B-09-	Video capture and editing software package	EDU	5,700	0	TBD
B-09-	Staff PC replacements (3)	EDU	8,100	0	TBD

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GOLDEN STATE WATER COMPANY

2008 Capital Budget

General Office

BUDG- ET GROUP	DESCRIPTION	DEPARTMENT	GSWC Request	DRA Recommended	Stipulation
B-09-	Training videos to augments classroom learning (5)	EDU	7,000	0	TBD
B-09-	Printers for training rooms and EDU common area (3)	EDU	3,200	0	TBD
B-09-	Region III training room tables and chairs replacement	EDU	44,200	0	TBD
B-09-	Handheld digital video camera	EDU	2,900	0	TBD
B-09-	Portable Easels for Classroom (3)	EDU	3,400	0	TBD
B-09-	Ergonomic Chairs for EDU Staff (3)	EDU	2,900	0	TBD
B-09-	Upgrade Videoconference systems for G.O. and Region I	EDU	27,800	0	TBD

2007 Cal. PUC LEXIS 648, *

BUDG- ET GROUP	DESCRIPTION	DEPARTMENT	GSWC Request	DRA Recommended	Stipulation
B-09-	Replacement Workstations(3)	HR	5,300	5,300	5,300
B-09-	Replace Five-year old servers (3)	INFO. TECH.	59,200	59,200	59,200
B-09-	Replace Five Workstations	INFO. TECH.	8,900	8,900	8,900
B-09-	Replace Fax Machine	INFO. TECH.	2,300	2,300	2,300
B-09-	Replacement A/C Water Source Heat Pumps (4)	INFO. TECH.	24,200	24,200	24,200
B-09-	File Cabinets/ Remittance Section (2)	INFO. TECH.	3,800	3,800	3,800
B-09-	Replace 5 Workstations	INFO. TECH.	8,900	0	0
B-09-	Desktop Printers (2)	INFO. TECH.	1,400	1,400	1,400
B-09-	Replace GO Patio Furniture	INFO. TECH.	3,100	3,100	3,100
B-09-	Replace 2 Laptop Computers	INT AUDIT	6,400	0	TBD
B-09-	PCs Workstations - Replacements (4)	REGULATORY AFFAIRS	7,100	7,100	7,100
B-09-	Laserjet Color Printer	REGULATORY AFFAIRS	3,200	3,200	3,200
B-09-	Replace 4 chairs	REGULATORY AFFAIRS	2,200	2,200	2,200
B-09-	Safety Training Videos	RISK MANAGEMENT	7,000	7,000	7,000
B-09-	Safety and Testing Equipment	RISK MANAGEMENT	12,500	5,700	6,250
B-09-	Compliance Software - Phase 2	WATER QLTY.	26,400	0	0
B-09-	GPS for Company Vehicles	SECURITY	0	0	72,700
B-10-	Replacement of WS Pool Van	INFO. TECH.	40,600	40,600	40,600
	Total Blankets		757,900	358,217	
	2008 Total General Office		4,627,000	387,217	

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ATTACHMENT B**Attachment B: Table 1****Allocation Factor Calculation**

Description	Customers		Total Labor		Total Expenses		Average Allocation Percentage
	Amount	%	Amount	%	Amount	%	
Golden State	275,706	85.6%	14,167,563	93.6%	99,318,661	95.4%	91.5%

Description	Customers		Total Labor		Total Expenses		Average Allocation Percentage
	Amount	%	Amount	%	Amount	%	
Water Chaparral City Water	12,959	4.0%	376,839	2.5%	2,097,725	2.0%	2.8%
American States Utility Services	33,370	10.4%	588,109	3.9%	2,726,701	2.6%	5.6%
Total	322,035	100.0%	15,132,511	100.0%	104,143,087	100.0%	100.0%

SOURCE: Except for ASUS Customer number, source is Exhibit 47

Customer source is 3/9/06 Data Response to AMX-1, weighted by percentage of Services rendered (see Table 2 - Weighted Number of Customers).

Attachment B: Table 2

Weighted Number of Customers

Description of Remaining Contracts	Total Number of Customers 3/9/06 Data Response to AMX-1	Weighting % Based on Services Rendered	Weighted Number of Customers
Rowland Water District	15,000	10.0%	1,504
City of Torrance	34,000	30.1%	10,226
Brooke Utilities	7,500	30.1%	2,256
City of Bell Gardens	1,500	38.3%	574
City of Tustin	15,000	38.3%	5,744
City of Santa Fe Springs	5,500	8.2%	452
Central Basin MWD	1	100.0%	1
Fort Bliss	9,000	100.0%	9,000
Fort Lee	915	100.0%	915
Andrews AFB	780	100.0%	780
Fort Eustic/Monroe/Story	1,919	100.0%	1,919
	91,115		33,370

[*374]

1. Weighting based on Services Rendered. If multiple A&G Services provided, allocate 30.1%. If one A&G service, allocate 1/3 of 30.1% or 10.0%. If A&G plus meter reading or field work, add 1/3 of O&M % of 24.6%, or 8.2%, to the A&G, which totals to 38.3%. Since company is running military base operations, all customers are counted at such basis.

2. Weighting factors are calculated on Table 3 - Calculation of Weighting Percentage. These factors are based on figures from CPUC decisions for each Region.

Attachment B: Table 3

Calculation of Weighting Percentage

Description	Region I	Region II	Region III	Total
Operation & Maintenance Expenses (minus Supply Expense)	2,285.7	10,381.2	11,384.0	24,050.9
Administrative and General Expenses	2,538.2	13,507.3	13,304.9	29,350.4
Amortization & Depreciation	2,106.7	8,930.7	8,162.5	19,199.9

2007 Cal. PUC LEXIS 648, *

Description	Region I	Region II	RegionIII	Total
Taxes	1,914.3	12,255.9	10,815.3	24,985.5
Total	8,844.9	45,075.1	43,666.7	97,586.7
Operation & Maintenance %				24.6%
Administrative & General %				30.1%
Amortization & Depreciation %				19.7%
Taxes %				25.6%
				100.0%

ATTACHMENT C

Attachment C

List of Appendices

Appendix A	Summary of Earnings for Test Year 2007
Appendix B	Test Year 2007 Rate Schedules
Appendix C	Adopted Quantities
Appendix D	Bill Comparisons
Appendix E	Income Tax Calculations
[*375]	

Appendix A

GOLDEN STATE WATER COMPANY

REGION 2 - METROPOLITAN CSA A.06-02-023

SUMMARY of EARNINGS- TEST YEAR 2007

(Dollars in Thousands)

	AT PRESENT RATES 2007	AT ADOPTED RATES 2007
OPERATING REVENUES	94,518.6	100,888.9
OPERATION EXPENSES	-	-
Purchased Water	25,337.4	25,337.4
Purchased Power	2,337.0	2,337.0
Pump Taxes	3,894.4	3,894.4
TOTAL SUPPLY EXPENSES	31,568.9	31,568.9
REVENUE LESS SUPPLY EXPENSES	62,949.8	69,320.1
	-	-
Chemicals	452.7	452.7
Allocated Common Cust. Acct. (G.O.)	1,081.9	1,081.9
Allocated Common Cust. Acct. (Region)	-	-
Allocated Common Cust. Acct. (District)	-	-
Postage	-	-
Uncollectibles	271.7	290.0
Operation Labor	3,065.8	3,065.8
Other Operation Expenses	2,183.9	2,183.9
TOTAL OPERATION EXPENSES	38,624.9	38,643.2
	-	-
Maintenance Labor	875.6	875.6
Other Maintenance Expenses	3,754.1	3,754.1
TOTAL MAINTENANCE EXPENSE	4,629.7	4,629.7
TOTAL O&M EXCLUDING A&G	43,254.6	43,272.9
	-	-
Office Supplies & Expenses	326.0	326.0

2007 Cal. PUC LEXIS 648, *

	AT PRESENT RATES 2007	AT ADOPTED RATES 2007
Property Insurance	-	-
Injuries and Damages	-	-
Pension and Benefits	57.9	57.9
Business Meals	2.7	2.7
Regulatory Expenses	224.5	224.5
Outside Services	121.9	121.9
Miscellaneous	6.4	6.4
Allocated General Office Expenses	11,816.6	11,816.6
Allocated Region Office Expenses	1,434.7	1,434.7
Allocated District Office Expenses	1,518.0	1,518.0
Other Maintenance of General Plant	17.2	17.2
Rent	359.2	359.2
A&G Expenses Capitalized	-	-
A&G Labor	664.9	664.9
TOTAL ADMIN & GENERAL EXPENSES	16,550.0	16,550.0
DEPRECIATION AND AMORTIZATION	8,421.5	8,421.5
Property Taxes	2,667.1	2,667.1
Payroll Taxes	373.0	373.0
Local Taxes	1,107.7	1,182.3
TOTAL TAXES NOT ON INCOME	4,147.7	4,222.4
TOTAL EXPENSE EXCLUDING INCOME TAX	72,373.8	72,466.8
NET OPER REVENUE BEFORE INCOME TAX	22,144.8	28,422.2
State Income Tax	1,538.9	2,093.8
Federal Income Tax	4,824.7	7,021.7
TOTAL INCOME TAXES	6,363.6	9,115.6
TOTAL OPERATING EXPENSES	78,737.4	81,582.3
NET OPERATING REVENUE	15,781.2	19,306.6
RATE BASE	219,391.5	219,391.5
RATE OF RETURN	7.19%	8.80%
[*376]		
REVENUES (Other)	170.2	
Common Customer Account	396.8	
Postage	751.4	
Operation Labor	2,069.7	
COMM OUST ACCT EXPENSES	3,217.9	
All Other Operating Expenses	241.6	
Office Supplies & Expense	2,054.6	
Property Insurance	360.2	
Injuries and Damages	2,493.9	
Pension and Benefits	13,403.0	
Business Meals	82.5	
Regulatory Expenses	35.8	
Outside Services	5,698.0	

2007 Cal. PUC LEXIS 648, *

	2007	
Miscellaneous		2,009.4
Maintenance of General Plant		765.0
Rent		184.7
A&G Capitalized		(1,884.1)
A&G Labor		7,337.1
TOTAL ADMIN & GENERAL EXPENSES		32,781.7
DEPRECIATION & AMORTIZATION		1,684.3
Property Taxes		121.6
Payroll Taxes		761.6
TOTAL TAXES NOT ON INCOME		883.2
SAVINGS FROM CAPITAL PROJECTS		(31.4)
ADJUSTMENT FOR MISSED ALLOCATIONS		-
ADJUSTMENT FOR CAPITALIZED EXPENSES		-
TOTAL OPERATING EXP (Less REV)		35,147.7
TOTAL ALL EXPENSES (Less REV)		38,365.6
	2007	2008
RATE BASE		
Utility Plant	333,599.7	367,272.8
Acquisition Adjustment	(8,321.1)	(8,321.1)
Total Utility Plant	325,278.7	358,951.7
Depreciation Reserve	(79,168.1)	(86,399.9)
Net Utility Plant	246,110.5	272,551.8
Material & Supplies	275.4	275.4
Advances for Construction	(8,213.0)	(8,086.1)
Contribution	(17,733.5)	(18,227.4)
Rate Base before Adjustment	220,439.5	246,513.7
ACRS & MACRS Depreciation	(18,330.5)	(20,180.7)
Investment Tax Credit	(438.2)	(406.7)
Unicap 86	2,014.5	2,217.8
Connections	695.8	732.5
Advances (Gross-Up)	0.0	0.0
Contributions (Gross-Up)	0.0	0.0
Deferred Revenues	(148.6)	(148.6)
Invest. in Other Water Companies	0.0	0.0
Deferred Rate Case Expenses	0.0	0.0
Allowance for Working Cash	2,142.4	2,142.4
Common Utility Allocation	13,016.6	12,625.8
Weighted Average Rate Base	219,391.5	243,496.2
[*377]		
	2007	2008
RATE BASE		
Utility Plant	27,805.6	27,410.4
Acquisition Adjustment	(1,187.3)	(1,187.3)
Total Utility Plant	26,618.3	26,223.1

2007 Cal. PUC LEXIS 648, *

	2007	2008
Depreciation Reserve	(11,307.4)	(11,926.0)
Net Utility Plant	15,310.9	14,297.1
Material & Supplies	(17.1)	(17.1)
Advances for Construction	0.0	0.0
Contribution	0.0	0.0
Rate Base before Adjustment	15,293.9	14,280.0
ACRS & MACRS Depreciation	(411.6)	(411.6)
Investment Tax Credit	0.0	0.0
Unicap 86	40.6	40.6
Connections	0.0	0.0
Advances (Gross-Up)	3,399.2	3,250.7
Contributions (Gross-Up)	0.0	0.0
Deferred Revenues	0.0	0.0
Invest. in Other Water Companies	0.0	0.0
Deferred Rate Case Expenses	0.0	0.0
Allowance for Working Cash	106.4	106.4
Common Utility Allocation	0.0	0.0
Weighted Average Rate Base	18,428.5	17,266.1

Appendix B

Schedule No. ME-1

Metropolitan District

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Portions of the Cities of Artesia, Bell, Bell Gardens, Carson, Cerritos, Compton, Cudahy, Culver City, Downey, El Segundo, Gardena, Hawaiian Gardens, Hawthorne, Huntington Park, Inglewood, [*378] Lakewood, La Mirada, Lawndale, Long Beach, Norwalk, Paramount, Santa Fe Springs, South Gate, and the communities of Athens, Lennox, and Moneta and vicinity, Los Angeles County and portions of the City of Los Alamitos, Orange County.

RATES

Quantity Rates:

For all water delivered, per 100 cu. ft

\$ 2.249

Per Meter
Per Month

Surcredit

Service Charge for 2007:

For 5/8 x 3/4-inch meter	\$ 17.55	\$ 0.80
For 3/4-inch meter	26.35	\$ 1.15
For 1-inch meter	43.90	\$ 1.90
For 1 1/2 inch meter	87.80	\$ 4.00
For 2-inch meter	140.00	\$ 6.35

Quantity Rates:

For 3-inch meter	263.00	\$ 11.85
For 4-inch meter	439.00	\$ 19.80
For 6-inch meter	878.00	\$ 39.60
For 8-inch meter	1,405.00	\$ 63.90
For 10-inch meter	2,019.00	\$ 96.00

The service charge is a readiness-to-serve charge applicable to all metered service and to which is added the charge for water used computed at the Quantity Rates.

SPECIAL CONDITIONS

1. All bills are subject to the reimbursement fee set forth on Schedule No. UF.
2. Due to the overcollection in the Balancing-Type Memorandum Account for the period of December 1, 2004 through December 31, 2004, a surcredit will be [*379] applied to the service charges for a 36-month period, beginning on the effective date of Advice Letter 1188-WA, which is August 11, 2005. This surcharge will expire on August 10, 2008.

Schedule No. MW-3

TMetropolitan District

RECLAIMED WATER SERVICE

APPLICABILITY

Applicable to all metered reclaimed (non-potable) water service for irrigation and/or industrial use.

TERRITORY

Portions of the Cities of Artesia, Bell, Bell Gardens, Carson, Cerritos, Compton, Cudahy, Culver City, Downey, El Segundo, Gardena, Hawaiian Gardens, Hawthorne, Huntington Park, Inglewood, Lakewood, La Mirada, Lawndale, Long Beach, Norwalk, Paramount, Santa Fe Springs, South Gate, and the communities of Athens, Lennox, and Moneta and vicinity, Los Angeles County, and portions of the City of Los Alamitos, Orange County.

RATES

Quantity Rates:

For all water delivered, per 100 cu. ft... \$ 1.512

	Per Meter Per Month	Surcredit
Service Charge for 2007:		
For 5/8 x 3/4-inch meter	\$ 7.40	\$ 0.60
For 3/4-inch meter	10.40	\$ 0.90
For 1-inch meter	15.55	\$ 1.55
For 1 1/2 inch meter	30.25	\$ 3.10
For 2-inch meter	44.80	\$ 4.95
For 3-inch meter	133.00	\$ 9.25
For 4-inch meter	212.00	\$ 15.45
For 6-inch meter	363.00	\$ 30.85
For 8-inch meter	536.00	\$ 49.20
For 10-inch meter	736.00	\$ 70.95

[*380]

The Service Charge is a readiness-to-serve charge applicable to all metered service and to which is added the charge for water used computed at the Quantity Rates.

SPECIAL CONDITIONS

1. All bills are subject to the reimbursement fee set forth on Schedule No. UF.
2. Due to the overcollection in the Balancing-Type Memorandum Account for the period of December 1, 2004 through December 31, 2004, a surcredit will be applied to the service charges for a 36-month period, beginning on the effective date of Advice Letter 1188-WA, which is August 11, 2005. This surcharge will expire on August 10, 2008.

GOLDEN STATE WATER COMPANY

ADOPTED QUANTITIES

METROPOLITAN DISTRICT - A.06-02-023

TEST YEARS 2007 & 2008

	Number of Metered Services	Schedule ME-1			Schedule ME-3		
		2007	2008	2009	2007	2008	2009
5/8 x 3/4 -inch meter		81,334	81,660	81,989	0	0	0
3/4		300	302	303	0	0	0
1		10,509	10,550	10,591	0	0	0
1/1/2		2,942	2,956	2,969	0	0	0
2		3,799	3,824	3,850	9	9	9
3		319	321	323	17	18	18
4		69	69	69	8	8	8
61		21	21	21	4	4	4
8		3	3	3	1	1	1
10		2	2	2	0	0	0
TOTAL METERED							
Services		99,298	99,708	100,120	39	40	40
Total Metered							
Services - all tariffs		99,337	99,748	100,160			
Private Fire		1,707	1,728	1,750			
Total Customers		101,044	101,477	101,911			

[*381]

GOLDEN STATE WATER COMPANY

ADOPTED QUANTITIES

METROPOLITAN DISTRICT - A.06.02-023

TEST YEARS 2007 & 2008

WATER CONSUMPTION

Classification METERED Services :	Service Connection	Usage (CCF/CUST)		
		2007	2008	2009
Commercial		98,184	98,576	98,968
Industrial		252	251	249
Public Authority		693	693	694

271.1

2,994.4

2,310.4

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Classification	Service Connection	Usage (CCF/CUST)		
METERED Services :				
	2007	2008	2009	
Irrigation	155	173	191	840.0
Reclaimed	39	40	40	9,559.2
Other	14	15	16	353.8
Total Metered	99,337	99,748	100,159	
PRIVATE FIRE PROTECTION	1,707	1,728	1,750	
TOTAL CONNECTIONS	101,044	101,477	101,909	
UNACCOUNTED WATER	5.43%	5.43%	5.43%	
TOTAL WATER PRODUCTION WELLS (KCcf)				
PURCHASED WATER (KCcf)				
RECLAIMED WATER (KCcf)				

	Classification	Consumption (KCcf)		
METERED Services :		2007	2008	2009
Commercial		26,616.4	26,722.8	26,829.1
Industrial		753.4	750.1	746.8
Public Authority		1,600.9	1,601.6	1,602.3
Irrigation		130.1	145.5	160.8
Reclaimed		376.4	379.7	382.9
Other		5.0	5.4	5.8
Total Metered		29,482.3	29,605.0	29,727.7
PRIVATE FIRE PROTECTION				
TOTAL CONNECTIONS		29,482.3	29,605.0	29,727.7
UNACCOUNTED WATER		1,692.0	1,699.1	1,706.1
TOTAL WATER PRODUCTION		31,174.3	31,304.1	31,433.8
WELLS (KCcf)		12,038.1	12,038.1	12038.05
PURCHASED WATER (KCcf)		18,749.2	18,879.0	19,361.8
RECLAIMED WATER (KCcf)		387.3	387.3	387.3
31,174.6		31,304.3	31,787.1	

[*382]

Adopted Quantities

PURCHASED POWER	2007
WELLS:	
Total Production (KCcf)	12,038.1
Kwh per Ccf	\$ 1.4871
SoCal. Edison	Jul-06
Total Kwh	17,898,575
Unit Cost (\$ /Kwhr)	0.120298
Power Cost (wells)	\$ 2,153,166.6
DWR Ratio	40%
DWP Electric:	
Total Kwh	3580.4
Unit Cost (\$ /Kwhr)	0.22643
Power Cost	\$ 810.7
S. C. Gas	
Total therms	291.4
Unit Cost (\$ /therm)	2.00554
Power Cost	\$ 584.5
BOOSTERS:	

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PURCHASED POWER			2007
SoCal. Edison			
Total Production (KCcf)			31,174.6
Kwh per Ccf			0.04165
Total Kwh			1,298,293
Unit Cost (\$ /Kwhr)			0.140529
Power Cost (boosters)			\$ 182,447.6
DWR Ratio			40%
Total Purchased Power Cost			\$ 2,337,009.4
PURCHASED WATER		S/AF Cfs	KCcf
Central Basin MWD	Jan-07	\$ 525.00	4,467.8
West Basin MWD	Jan-07	\$ 572.00	13,304.8
Central Basin Reclaimed	Jan-07		
0-25 AF		\$ 322.00	10.9
26-50		\$ 299.00	10.9
51-100		\$ 278.00	21.8
Over		\$ 255.00	170.8
West Basin Reclaimed	Jan-07		
0-25 AF		\$ 337.00	10.9
26-50		\$ 317.00	10.9
51-100		\$ 297.00	21.8
101-200		\$ 277.00	43.6
Over		\$ 257.00	85.8
City of Cerritos	Jul-04	\$ 539.61	950.9
City of Inglewood	Jul-04	\$ 1,172.43	0.0
CalWater			25.7
Total KCcf			19,136.4
[*383]			

PURCHASED POWER		2008	2009
WELLS:			
Total Production (KCcf)		12,038.1	12,038.1
Kwh per Ccf		1.4871	0.0000
SoCal. Edison			
Total Kwh		17,898,575	17,898,575
Unit Cost (\$ /Kwhr)		0.120298	0.120298
Power Cost (wells)		\$ 2,153,166.6	\$ 2,153,166.6
DWR Ratio		40%	40%
DWP Electric:			
Total Kwh		3580.4	3580.4
Unit Cost (\$ /Kwhr)		0.22640	0.22643
Power Cost		\$ 810.6	\$ 810.7
S. C. Gas			
Total therms		292.6	293.5
Unit Cost (\$ /therm)		2.00184	1.99914
Power Cost		\$ 585.8	\$ 586.8
BOOSTERS:			
SoCal. Edison			
Total Production (KCcf)		31,304.3	31,399.8
Kwh per Ccf		0.04165	0.04165
Total Kwh		1,303,695	1,307,673
Unit Cost (\$ /Kwhr)		0.140364	0.140246
Power Cost (boosters)		\$ 182,991.6	\$ 183,395.3
DWR Ratio		40%	40%
Total Purchased Power Cost		\$ 2,337,554.6	\$ 2,337,959.5
PURCHASED WATER		KCcf	KCd

2007 Cal. PUC LEXIS 648, *

PURCHASED POWER	2008	2009
Central Basin MWD	4498.1	4,520.4
West Basin MWD	13,397.8	13,466.3
Central Basin Reclaimed		
0-25 AF	10.9	10.9
26-50	10.9	10.9
51-100	21.8	21.8
Over	170.80	170.8
West Basin Reclaimed		
0-25 AF	10.9	10.9
26-50	10.9	10.9
51-100	21.8	21.8
101-200	43.6	43.6
Over	85.80	85.8
City of Cerritos	957.3	962.1
City of Inglewood	0.0	0.0
CalWater	25.7	25.7
Total KCcf	19,266.1	19,136.6

[*384]

Adopted Quantities

Central Basin MWD \$		
Quantity Charge		
Peaking Surcharge	\$ 0.0	
Capacity Reservation Charge	\$ 11,572	
Service Charge	\$ 31/Cfs	73
West Basin MWD \$		
Quantity Charge		
Peaking Surcharge	\$ 0.0	
Capacity Reservation Charge	\$ 29,800	
Service Charge	\$ 21/CFS	160
Central Basin Reclaimed \$		
West Basin Reclaimed \$		
City of Cerritos		
Quantity Charge		
Capacity Reservation Charge	\$ 3,353.13	
Service Charge	\$ 594.15	
Suburban Water System		
Service Charge	\$ 377.33	
City of Inglewood \$		
Service Charge	\$ 360.00	
City of Paramount		
Service Charge	\$ 71.50	
Cal Water		
Service Charge	\$ 1,122.00	
Total Purchased Water Cost		

	2007	2008	2009
Central Basin MWD \$			
Quantity Charge	\$ 5,384,750.5	\$ 5,421,251.7	\$ 5,448,129.2
Peaking Surcharge	\$ 0.0	\$ 0.0	\$ 0.0
Capacity Reservation Charge	\$ 138,864.0	\$ 138,864.0	\$ 138,864.0
Service Charge	\$ 27,156.0	\$ 27,156.0	\$ 27,156.0
West Basin MWD \$			
Quantity Charge	\$ 17,470,953.4	\$ 17,593,058.1	\$ 17,682,969.2
Peaking Surcharge	\$ 0.0	\$ 0.0	\$ 0.0

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Capacity Reservation Charge	\$ 357,600.0	\$ 357,600.0	\$ 357,600.0
Service Charge	\$ 40,320.0	\$ 40,320.0	\$ 40,320.0
Central Basin Reclaimed \$	\$ 129,410.8	\$ 129,410.8	\$ 129,410.8
West Basin Reclaimed \$	\$ 109,523.1	\$ 109,523.1	\$ 109,523.1
City of Cerritos			
Quantity Charge	\$ 1,177,904.0	\$ 1,185,889.0	\$ 1,191,768.0
Capacity Reservation Charge	\$ 40,237.6	\$ 40,237.6	\$ 40,237.6
Service Charge	\$ 7,129.8	\$ 7,129.8	\$ 7,129.8
Suburban Water System	\$ 0.0	\$ 0.0	\$ 0.0
Service Charge	\$ 4,528.0	\$ 4,528.0	\$ 4,528.0
City of Inglewood \$	\$ 0.0	\$ 0.0	\$ 0.0
Service Charge	\$ 4,320.0	\$ 4,320.0	\$ 4,320.0
City of Paramount	\$ 0.0	\$ 0.0	\$ 0.0
Service Charge	\$ 858.0	\$ 858.0	\$ 858.0
Cal Water	\$ 0.0	\$ 0.0	\$ 0.0
Service Charge	\$ 13,464.0	\$ 13,464.0	\$ 13,464.0
Total Purchased Water Cost	\$ 24,907,019.1	\$ 25,073,610.0	\$ 25,196,277.6

[*385]

REPLENISHMENT TAX		S/AF
Water Replenishment District		
Total Well Production (AF)	Jul-06	\$ 138.00 /AF
Pump Tax Cost		

Administration Costs

Total Replenishment Cost

Leased Water Rights

S/AF

Leased Water Rights

From Central Basin

\$ 184.00

From West Basin

\$ 77.50

Chevron Water Rights

\$ 116.00

Leased Water Rights Cost

From Central Basin

From west Bawl

Chevron Water Rights

Total Leased Water Rights Cost

Total Chemical Cost

REPLENISHMENT TAX	KCcf	KCcf	KCcf
Water Replenishment District			
Total Well Production (AF)	12,038	12,038	12,038
Pump Tax Cost	\$ 3,813,707.4	\$ 3,813,707.4	\$ 3,813,707.4
Administration Costs	\$ 80,736.4	\$ 80,736.4	\$ 80,736.4
Total Replenishment Cost	\$ 3,894,443.8	\$ 3,894,443.8	\$ 3,894,443.8
Leased Water Rights	KCcf	KCcf	KCcf
Leased Water Rights	19	19	19
From Central Basin	14	14	14
From West Basin	4	4	4
Chevron Water Rights	1,591	1,591	1,591
Leased Water Rights Cost			
From Central Basin	\$ 6,066.9	\$ 6,066.9	\$ 6,066.9
From west Bawl	\$ 763.3	\$ 763.3	\$ 763.3
Chevron Water Rights	\$ 423,550.8	\$ 423,550.8	\$ 423,550.8
Total Leased Water Rights Cost	\$ 430,381.0	\$ 430,381.0	\$ 430,381.0
Total Chemical Cost	\$ 452,744.0	\$ 461,889.5	\$ 470,879.8

[*386]

Schedule ME-1

Bill Comparison for 5/8-inch Meter

2007 Rates Monthly Usage (Cubic Feet)	At Present Rates	At Adopted Rates	Increase Amount	Percent Increase
500	\$ 27.12	\$ 28.80	\$ 1.68	6.20%
1,000	\$ 37.58	\$ 40.04	\$ 2.46	6.55%
1,500	\$ 48.05	\$ 51.29	\$ 3.24	6.74%
2,300 (Avg.)	\$ 64.79	\$ 69.28	\$ 4.49	6.93%
2,500	\$ 68.98	\$ 73.78	\$ 4.80	6.96%
3,000	\$ 79.44	\$ 85.02	\$ 5.58	7.02%
4,000	\$ 100.37	\$ 107.51	\$ 7.14	7.11%
10,000	\$ 225.95	\$ 242.45	\$ 16.50	7.30%

2008 Rates Monthly Usage (Cubic Feet)	2007 Rates	2008 Rates	Increase Amount	Percent Increase
500	\$ 28.80	\$ 30.28	\$ 1.49	5.16%
1,000	\$ 40.04	\$ 41.91	\$ 1.87	4.67%
1,500	\$ 51.29	\$ 53.54	\$ 2.26	4.40%
2,300 (Avg.)	\$ 69.28	\$ 72.15	\$ 2.87	4.14%
2,500	\$ 73.78	\$ 76.80	\$ 3.02	4.10%
3,000	\$ 85.02	\$ 88.43	\$ 3.41	4.01%
4,000	\$ 107.51	\$ 111.69	\$ 4.18	3.89%
10,000	\$ 242.45	\$ 251.25	\$ 8.80	3.63%

Appendix D

GOLDEN STATE WATER COMPANY

METROPOLITAN DISTRICT - A.06-02-023

Schedule ME-3

Bill Comparison for 3-inch Meter

2007 Rates Monthly Usage (Cubic Feet)	At Present Rates	At Adopted Rates	Increase Amount	Percent Increase
5,000	\$ 175.30	\$ 208.60	\$ 33.30	19.00%
10,000	\$ 243.45	\$ 284.20	\$ 40.75	16.74%
25,000	\$ 447.90	\$ 511.00	\$ 63.10	14.09%
58,800 (Avg.)	\$ 908.59	\$ 1,022.06	\$ 113.46	12.49%
75,000	\$ 1,129.40	\$ 1,267.00	\$ 137.60	12.18%
100,000	\$ 1,470.15	\$ 1,645.00	\$ 174.85	11.89%
120,000	\$ 1,742.75	\$ 1,947.40	\$ 204.65	11.74%
150,000	\$ 2,151.65	\$ 2,401.00	\$ 249.35	11.59%
[*387]				

2008 Rates Monthly Usage (Cubic Feet)	2007 Rates	2008 Rates	Increase Amount	Percent Increase
5,000	\$ 208.60	\$ 242.85	\$ 34.25	16.42%
10,000	\$ 284.20	\$ 321.70	\$ 37.50	13.19%
25,000	\$ 511.00	\$ 558.25	\$ 47.25	9.25%
58,800 (Avg.)	\$ 1,022.06	\$ 1,091.28	\$ 69.22	6.77%

2007 Cal. PUC LEXIS 648, *

Monthly Usage (Cubic Feet)	2007 Rates	2008 Rates	Increase Amount	Percent Increase
75,000	\$ 1,267.00	\$ 1,346.75	\$ 79.75	6.29%
100,000	\$ 1,645.00	\$ 1,741.00	\$ 96.00	5.84%
120,000	\$ 1,947.40	\$ 2,056.40	\$ 109.00	5.60%
150,000	\$ 2,401.00	\$ 2,529.50	\$ 128.50	5.35%

Appendix E

GOLDEN STATE WATER COMPANY

REGION 2 - METROPOLITAN CSA A.06-02-023

COMPUTATION of TAXES ON INCOME

(Dollars in Thousands)

	AT PRESENT RATES 2007	AT ADOPTED RATES 2007
Operating Revenues	94,518.6	100,888.9
Deductions:		
Operating Expenses	72,373.8	72,466.8
Book Depreciation - CSA	(8,421.5)	(8,421.5)
Book Depreciation - General Office	(566.3)	(566.3)
Interest	8,051.7	8,051.7
Deductions Excluding Depreciation	71,437.7	71,530.7
State Tax Calculation:		
Taxable Income Before Tax Depreciation and Other Schedule M's	23,080.9	29,358.3
Add (Deduct):		
Tax Depreciation - State	(6,279.9)	(6,279.9)
Other Schedule M Items	607.3	607.3
State Taxable Income	17,408.3	23,685.7
Total State Tax @ 8.84%	1,538.9	2,093.8
Federal Tax Calculation:		
Taxable Income before Tax Depreciation and Other Schedule M's	23,080.9	29,358.3
Add (Deduct):		
Excess Tax Depreciation - Flow Through	671.6	671.6
Book Depreciation - CSA	(8,421.5)	(8,421.5)
Book Depreciation - G.O.	(566.3)	(566.3)
State Tax	(1,538.9)	(1,538.9)
Other Schedule M Items	607.3	607.3
Deferred Revenue Amortization - Contrib.	151.4	151.4
Adjustment, for Job Creation Act	(199.8)	(199.8)
Federal Taxable Income	13,784.8	20,062.1
Federal Tax @ 35.00%	4,824.7	7,021.7
Total Federal & State Tax	6,363.6	9,115.6
[*388]		

Legal Topics:

For related research and practice materials, see the following legal topics:

Administrative Law Agency Adjudication Prehearing Activity Energy & Utilities Law Pooling & Unitization Compulsory
Pooling Energy & Utilities Law Utility Companies Buying & Selling of Power



20 of 99 DOCUMENTS

In the Matter of the Application of Roseville Telephone Company (U 1015 C) to Review
Its New Regulatory Framework

Decision No. 01-06-077, Application No. 99-03-025 (Filed March 8, 1999)

California Public Utilities Commission

2001 Cal. PUC LEXIS 604

June 28, 2001

HEADNOTES: [*1] **I. Summary**

This decision addresses Roseville Telephone Company's first triennial review of its New Regulatory Framework (NRF). By this decision, we (1) retain the sharing mechanism; (2) eliminate depreciation reviews, (3) suspend the I-X (inflation minus productivity) portion of the price adjustment formula, (4) eliminate most Z-factor adjustments; (5) establish a limited exogenous (LE) factor mechanism; and (6) modify the monitoring report requirements. In addition we require Roseville Telephone Company (RTC) to amend its shareable earnings filing for 1999 to reflect certain adopted results of an affiliate transactions audit conducted by the Office of Ratepayer Advocates (ORA). We also order a refund and a permanent revenue reduction related to post-retirement benefits other than pensions (PBOP).

Mark P. Schreiber, Attorney at Law, and E. Garth Black for Roseville Telephone Company, applicant.

Colleen O'Grady and Mary Vanderpan, Attorneys at Law, for Pacific Bell, intervenor.

Sindy J. Yun and Jason Zeller, Attorneys at Law, for the Office of Ratepayer Advocates.

PANEL: Loretta M. Lynch, President; Richard A. Bilas, Carl W. Wood, Geoffrey F. Brown, Commissioners

OPINION: Mark P. Schreiber, Attorney [*2] at Law, and E. Garth Black for Roseville Telephone Company, applicant.

Colleen O'Grady and Mary Vanderpan, Attorneys at Law, for Pacific Bell, intervenor.

Sindy J. Yun and Jason Zeller, Attorneys at Law, for the Office of Ratepayer Advocates.

OPINION

II. Background

In Application (A.) 95-05-030, RTC requested to change its intrastate rates and charges and to implement a NRF. In Decision (D.) 96-12-074, the Commission adopted new rates and a NRF, effective February 1, 1997. Ordering Paragraph 7 of the decision required RTC to file an application for NRF review on or before October 1, 1998. On April 17, 1998, the Executive Director granted RTC an extension of time to file its NRF review application until no later than 150 days after the Commission issued its order in A.98-02-003 and Rulemaking (R.) 98-03-040, the Pacific Bell (Pacific) and Verizon California Inc. n1 (Verizon) third triennial NRF review proceeding. The order, D.98-10-026, was adopted on October 8, 1998. Accordingly, RTC's NRF review application was due no later than March 8, 1999.

n1 Formerly known as GTE California, Incorporated.

[*3]

In D.96-12-074 the Commission adopted, with some modifications, the basic NRF framework already established for Pacific, Verizon, and Citizens Telecommunications Company of California (CTC). n2 The Commission adopted RTC's proposal to freeze, or cap, rates for three years, by suspending the I minus X factor portion of the NRF formula until the first review of RTC's NRF. Nevertheless, the order adopted the GDPPI as the inflation index and a 4.0% productivity factor.

n2 The NRF price cap formula adopted for Roseville was: $R(t) = R(t-1) * (1 + I - X + Z/R)$, where $R(t)$ is the rate to be effective on January 1, of the coming year, $R(t-1)$ is the rate effective December 31 of the current year, I is inflation, measured by the percentage change in the gross domestic product price index (GDPPI), X is the productivity factor, based on telecommunications industry productivity plus a stretch factor, Z is the annualized dollar effect of exogenous factors, and R is the annualized total local exchange carrier (LEC) revenues which match the Z estimate.

[*4]

RTC's current NRF also includes sharing consistent with that initially adopted for Pacific and Verizon. There is no sharing between the market and benchmark rates of return, 50% sharing between the benchmark and ceiling rates of return, and 100% return to ratepayers of earnings above the ceiling. The market rate of return is 10%. The benchmark rate of return is 150 basis points above the market rate of return and the ceiling rate of return is 500 basis points above the market rate of return.

A trigger mechanism, which initiates a review of the benchmark rate of return, applies if both the 30-year Treasury bond rate and the three-year forecast of the same rate differ by 150 basis points or more for at least three consecutive months from 6.86% (the average 30-year Treasury bond rate on the last days of July through November 1996). A floor rate of return 325 basis points below the market rate of return was also established. RTC may petition for reconsideration of adopted inflation or productivity factors if its earnings fall to the floor rate of return or below for two years in a row.

The Commission adopted the same service categories for RTC that are used for Pacific, Verizon, and CTC. [*5] Services are classified into three categories: Category 1 for basic monopoly services, Category 2 for discretionary or partially competitive services, and Category 3 for fully competitive services. Prices for Category 1 services are fixed, and are subject to annual change by application of the NRF price cap formula. Category 2 prices are subject to flexibility within ceilings and floors. Price floors are based on direct embedded costs or incremental cost studies filed with the Commission's Telecommunications Division, and are increased each year by inflation, unless a new cost study justifies a different floor. Price ceilings were to change annually by the NRF price cap formula; however, this portion of RTC's NRF was suspended. Category 3 prices are subject to the maximum pricing flexibility allowed by law.

RTC must also submit an annual application for review of its depreciation rates. These applications must address issues generally covered by both rescription and a technical update of depreciation rates.

Finally, the Commission adopted a series of NRF monitoring reports.

III. Procedural History

On March 8, 1999, RTC filed an Application for its first triennial review of [*6] its NRF. On April 19, 1999, the Office of Ratepayer Advocates (ORA) filed a Protest to RTC's Application.

On May 13, 1999, ORA filed a Motion to Consolidate the pending verification and non-regulated operations audit of RTC.

On June 14, 1999, in D.99-06-051, the Commission ordered ORA to file and serve the final audit report in this proceeding.

On September 27, 1999, ORA submitted its pre-filed testimony concerning RTC's NRF. On October 18, 1999, RTC submitted its pre-filed rebuttal testimony. The Commission held evidentiary hearings on November 1-2, 1999.

On January 3, 2000, ORA filed an audit report in this proceeding in accordance with D.99-06-051. Thereafter, on January 7, 2000, a second prehearing conference (PHC) was held to discuss the audit report, and to determine whether

additional evidentiary hearings would be needed in light of the audit report. The assigned Administrative Law Judge (ALJ) ruled that ORA would be permitted to submit additional testimony on the results of the audit report.

ORA submitted additional testimony on the audit report on February 9, 2000. ORA also submitted an errata to the audit report at that time.

On March 31, 2000, RTC submitted its rebuttal [*7] testimony. On April 3, 2000, ORA served both proprietary and non-proprietary versions of the audit report testimony.

On April 17-21, 2000, evidentiary hearings were held on the audit. Opening briefs were filed by ORA and RTC on May 22, 2000. Reply briefs were filed on June 20, 2000, whereupon the proceeding was submitted.

IV. Comments on the Proposed Decision

The proposed decision in this matter was mailed to the parties in accordance with Section 311(d) of the Public Utilities Code, and Rule 77.1 of the Commission's Rules of Practice and Procedure. Comments were filed on January 9, 2001, and reply comments were filed on January 16, 2001. All comments were considered. Corrections and modifications were made to the decision to correct errors and omissions, and to add clarity.

The alternate proposed decision of Commissioner Lynch was mailed to the parties in accordance with Section 311(e) of the Public Utilities Codes and Rule 77.6 of the Commission's Rules of Practice and Procedure. Comments by RTC and ORA were filed on June 21, 2001 and reply comments by the same parties were filed on June 26, 2001. Where warranted, these comments are addressed in the text of this decision.

[*8]

V. Overview

On March 8, 1999 RTC filed A.99-03-025 to review its NRF. RTC's specific proposals are as follows:

- . Suspend sharing
- . Eliminate price indexing
- . Suspend price indexing
- . Change the Z-factor criteria
- . Change the monitoring requirements
- . Increase pricing flexibility
- . Re-affirm authority to make promotional offerings.

VI. The Audit

A. Background

In D.99-06-051 the Commission ordered the audit that is addressed in this proceeding. The audit addressed affiliate and non-regulated telephone relationships and transactions of Roseville Communications Company (RCC). The audit period is January 1, 1997 through June 30, 1999. The audit was included in the scope of this proceeding to the extent that it relates to the issue of whether sharing should be eliminated.

The audit was performed for ORA by Overland Consulting. ORA's overall recommendation is based on its conclusion that RTC overallocated costs to regulated operations as demonstrated by 33 audit calculations.

In the course of this proceeding, RTC made numerous objections to how the audit was conducted. However, in this proceeding we are concerned with specific audit recommendations. We analyze each recommendation [*9] individually on its merits, and base our decision on our analyses. Therefore, we need not address in this proceeding the overall performance of the audit.

B. Corporate Organization, Operations and Affiliate Relationships

RTC and its affiliates are owned by RCC. RCC is a holding company. The following is a description of the corporate organization, operations and affiliate relationships.

1. Organizational Overview

. **Roseville Telephone Company (RTC)** - Provides regulated local exchange and intraLATA toll services within an exchange territory encompassing Roseville, California and surrounding areas. RTC provides various non-regulated communications services, including telecommunications equipment and wiring, alarm monitoring, coin telephone and competitive local access services to business customers outside local exchange boundaries.

. **Roseville Directory Company (RDC)** - Sells directory advertising and arranges for printing and distribution of RTC's exchange area white and yellow page directories. RDC also publishes an independent (competing) telephone directory in the Auburn-Grass Valley area of central California (outside RTC's exchange boundary), and [*10] publishes the exchange area directory for Foresthill Telephone, a small neighboring local exchange company. RDC began operating in March, 1997.

. **Roseville Long Distance (RLD)** - Resells Sprint long distance service to RTC and to residential and business customers of RTC. RLD began offering service commercially in September, 1997, coincident with RTC's implementation of intraLATA pre-subscription.

. **Roseville PCS and RCS Wireless** - Provides wireless PCS phone services in and around Roseville, California. RCS Wireless began offering commercial wireless telephone service in July, 1999, one month after the audit period.

. **Roseville Cable** - A shell created to operate the Roseville, California cable TV operation that RCC attempted to acquire from Jones Cable. The acquisition did not take place. Roseville Cable is currently inactive.

. **RCS Internet** - This subsidiary was launched in mid 1999. RCS Internet provides internet connectivity and modem installation. The subsidiary was formed to complement digital subscriber line services, which were rolled out at approximately the same time.

2. Overview of Non-Regulated Telephone Operations

RTC is engaged [*11] in both regulated and non-regulated telephone businesses. Regulated telephone services consist of exchange telephone, exchange access and intraLATA toll services. Non-regulated telephone services consist of everything else. Key non-regulated telephone businesses include.

. **Customer Premises Equipment, Networks and Wiring** - RTC sells and leases telephone equipment, designs local and wide area networks, and sells and repairs inside wiring. Sales are primarily to business customers in the Roseville area.

. **Alarm Monitoring** - RTC monitors alarms for approximately 30,000 alarm vendors who resell the service on a retail basis.

. **Coin Phone** - Through a separate RTC division, RTC installs unregulated coin phones in and around its local exchange service territory.

. **Competitive Local Exchange (CLEC) Service** - Near the end of the audit period, RTC began selling transmission and wide area network services outside RTC's exchange boundary. In September, 1999, RTC began providing local area network service. There were no measurable revenues during the audit period.

3. Overview of Affiliate Relationships

Affiliate relationships and transactions are [*12] covered in the audit. The following list includes the most significant relationships.

1. Services and Facilities Provided By RTC to Affiliates

. RTC provides corporate executive, administrative and general services on behalf of RCC to all affiliates. Corporate administrative and general services include accounting, finance, shareholder, human resources, regulatory, information management, computer operation and maintenance, procurement, distribution and corporate communications.

. RTC provides office facilities, computers, office equipment and vehicles to all affiliates.

. RTC provides advertising, marketing, sales and various customer services to RCS Wireless and RLD. RTC provides advertising and customer services to RDC.

. RTC provides inside plant engineering, installation, provisioning and maintenance services to RCS Wireless.

. RTC provides transmission facilities, central office space and support systems and space on towers and roofs for antennas and equipment to RCS Wireless.

. RTC provides billing and collection services to RLD and RDC.

. RTC provides interconnection to RCS Wireless to enable connection to the public switched network.

2. RDC provides directory [*13] advertising sales, compilation, contract printing and contract distribution (collectively referred to as directory publishing) to RTC.

3. RLD provides long distance telephone service to RTC.

4. RCS Wireless provides PCS wireless phone service to RTC.

C. Individual Audit Calculations

1. Audit Calculation 1 - Costs Attributable to Duplicated Holding Company Responsibilities

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 141,452)	-	(\$ 138,018)	-	(\$ 140,018)

a. ORA

ORA proposes to remove an amount equal to one half of the RTC allocation of RCC chairman Robert Doyle's \$ 330,000 salary from regulated expense.

Doyle retired as RTC's Chief Executive Officer (CEO) in 1993. ORA believes that Doyle has no involvement in the day-to-day activities of RTC or RCC. Therefore, there is no need to have two persons earning CEO salaries. ORA removed only half of Doyle's salary because he would receive retirement pay of about that much. Since regulated expenses may already have accrued an amount for Doyle's retirement expenses, ORA believes this is a conservative adjustment.

ORA states that it is not making [*14] a recommendation that Doyle should not be paid. ORA merely recommends that the costs should not be entirely allocated to ratepayers.

b. RTC

RTC opposes the reduction because it is outside the scope of the audit and Doyle's salary was found reasonable in RTC's general rate case D.96-12-074.

c. Discussion

In D.96-12-074 we addressed this issue and declined to adopt a similar recommendation by ORA. Since the situation appears to be substantially the same here, we will not adopt ORA's recommendation.

2. Audit Calculation 2 - The CEO and Chief Financial Officer (CFO) and Their Staffs Failed to Charge Their Development Efforts to Affiliates

Proposed Adjustments:

	1997		1998		1999	
	RTC	ORA	RTC	ORA	RTC	ORA
Adjustment to Expenses	-	(\$ 97,377)	-	(\$ 112,598)	-	(\$ 145,854)

a. ORA

ORA found that during the audit period the CEO, CFO and their staffs allocated only 8 of 31,000 hours directly to affiliate and non-regulated telephone company businesses. The CEO and CFO timesheets, which were not filled by the CEO and CFO themselves, contained no information describing the activities performed. ORA found evidence of time directly spent [*15] on affiliate business development such as cable TV. ORA allocated 10% of the CEO's, CFO's and their staff's time to non-regulated businesses because it believes that at least that much could have been directly allocated.

ORA believes that it is entirely appropriate and practical to directly bill executive time when the activities performed are clearly related to specific affiliates. Examples would include time when the executive is away on affiliate related business or in meetings related to specific affiliates.

b. RTC

RTC's CFO, Michael D. Campbell, testified that he and the CEO, and consequently their staffs, spend almost all of their time directly involved with RTC operations and allocate the remainder using a three-factor formula. RTC also notes that ORA did not interview the CEO or CFO during the audit. Each affiliate has its own management team which runs its operations. In addition, the majority of the development of the Roseville Cable, Roseville PCS and RCS Wireless operations was performed in 1997 by RTC staff who directly assigned their time. Therefore, it is inappropriate to assign executive time to those development efforts for the entire audit period as ORA did.

RTC [*16] states that ORA's adjustment should not be adopted because it is contradicted by RTC's CFO and ORA's analysis is flawed because it is attempted to assign development costs over the entire audit period.

c. Discussion

The CEO and CFO are charged with oversight of the entire corporate family. Not surprisingly, most of the operations are more directly managed by subordinate management. Therefore, we would expect that the vast majority of the CEO and CFO's time would be allocated rather than directly assigned. However, we find that RTC's direct assignment of only 8 out of 31,000 hours to affiliate and non-regulated business is not credible. We would expect that more time be devoted to specific affiliates in order to understand what each affiliate is doing and to provide some oversight of the affiliates' management. Such time could be directly assigned.

However, the issue here is whether such increased direct assignment would result in a substantially different allocation than achieved by the three-factor formula. While ORA's claim that more time should be directly allocated is reasonable, its 10% estimate is unsupported. We are not convinced that the end result would be substantially [*17] different. We will not adopt ORA's recommendation.

3. Audit Calculation 3 - The Vice President of Network Development Failed to Properly Charge His Effort in Developing RCS Wireless.

Proposed Adjustments:

	1997		1998		1999	
	RTC	ORA	RTC	ORA	RTC	ORA
Adjustment to Expenses	-	(\$ 24,681)	-	(\$ 25,885)	-	(\$ 29,120)

a. ORA

ORA alleges that Rulon Blackburn, RCC's Vice President of Network Development, charged none of his, his secretary's or his administrative assistant's time to RCS Wireless during the audit period. However, during the period, Blackburn played a role in the development of RCS Wireless. He attended at least two related conventions and kept the RCC Board of Directors informed about development progress. ORA also states that Blackburn does not fill out or check his own timesheets.

ORA assigned 10% Blackburn's time to RCS Wireless for the audit period.

b. RTC

Blackburn testified that he spent very little time on RCS Wireless in 1997 and 1998. In 1999, a portion of his time was assigned to RCS Wireless. RTC states that ORA did not interview Blackburn during the audit. Instead, ORA relied heavily on articles in an employee newsletter [*18] and Board of Directors meeting minutes. RTC believes that this is inadequate to justify ORA's adjustment.

c. Discussion

ORA relies on articles in the employee newsletter to indicate that Blackburn did spend time on RCS Wireless. Blackburn states that he spent very little time on RCS Wireless. He does not say that he spent no time on RCS Wireless. The issue here is how much time Blackburn spent on RCS Wireless. ORA's estimate of 10% is not sufficiently supported. Therefore, we will not adopt it.

4. Audit Calculation 4 - RTC Did Not Properly Allocate Cost for the Vice President of Customer Service to RDC.

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 15,786)	-	(\$ 17,053)	-	(\$ 24,226)

a. ORA

ORA states that Jay Kinder, RCC's Vice President of Customer Service is, among other things, in charge of the directory publishing subsidiary RDC. Kinder charged no time to RDC during 1997, when RDC was initially staffed. In 1998, RTC's accountant caught the error and retroactively allocated 10% of Kinder's time to RDC in 1997. The allocation was reduced to about 2% in July, 1998. None of the costs [*19] of Kinder's administrative staff was allocated or assigned to RDC during the audit period. Since Kinder is the primary executive responsible for RDC, ORA allocated 10% of the costs of Kinder's office to RDC.

b. RTC

Kinder testified that very little of his or his administrative staff's time was spent on RDC. Kinder directly assigns time spent on RDC to RDC. Time not directly assigned is allocated using the three-factor method. RTC states that ORA's allocation of Kinder's time has no factual support and should be rejected.

c. Discussion

The issue here is how much of Mr. Kinder's office's time should have been directly charged to RDC. Kinder states that he spends very little time on RDC and directly assigns what time he does spend on RDC. We find this credible. ORA's 10% adjustment is not supported. We will not adopt it.

5. Audit Calculation 5 - Marketing Executive Costs Charged But Not Billed to Roseville Cable Development

Proposed Adjustments:

	1997	1998	1999

Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	\$ (7,036)	(\$ 7,036)	-	-	-	-

a. ORA

ORA says that 127 hours of RCC's Vice President of Marketing, Phillip Germand's time [*20] should have been billed to Roseville Cable.

b. RTC

RTC agrees with ORA on this adjustment.

c. Discussion

Since ORA and RTC agree, we will adopt the adjustment.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Expenses	(\$ 7,036)	-	-

6. Audit Calculation 6 - Accounting, Budget and Finance Efforts Attributable to Affiliate Development

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 9,614)	-	(\$ 4,716)	-	-

a. ORA

ORA alleges that RTC failed to identify and assign development efforts directly attributable to specific subsidiaries during the audit period. Based on a checklist prepared by a consultant for RTC for development of RLD, ORA estimated that 500 hours of time should have been assigned to RLD for development efforts. Notwithstanding the existence of the checklist, ORA believes that the need to set up a financial plan, develop accounting policies, coding, financial reporting, inter-company payment procedures, etc. is an obvious requirement. ORA believes that its estimate is conservative.

b. RTC

RTC says that it has a centralized accounting system which is [*21] not organized along subsidiary or divisional lines. Accounting service costs are allocated using the three-factor formula rather than directly assigned because it is impractical to directly assign time.

RTC states that its accounting employees did not incur significant time to establish accounting policies and procedures for RLD because the policies and procedures were largely based on existing policies and procedures. Additionally, RTC believes that the establishment of policies and procedures for intercompany payments benefits all affiliates, not just RTC.

RTC also points out that the checklist ORA relied on was never used and is, therefore, invalid. In addition, development work for affiliates, if any, was done in 1997 only. RTC concludes that ORA's adjustment has no factual basis and should be rejected.

c. Discussion

The accounting practices and procedures developed for RLD were essentially those that RTC had already developed. Therefore, we expect that very little time was needed. However, we believe such time should have been directly allocated. ORA's adjustment is based on a checklist that was not used. However, we agree that at least some of the tasks

in the checklist [*22] would have to be accomplished. Therefore, we will adopt half of ORA's adjustment for 1997, the year in which development would have taken place.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	(\$ 4,807)	-	-

7. Audit Calculation 7 - Revenue Accounting Efforts Attributable to Non-Regulated Accounts and to Affiliates

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 15,782)	(\$ 2,960)	(\$ 10,851)	-	-

a. ORA

ORA's proposed adjustment has two components. The first is to increase the 1998 non-regulated telephone allocations of RTC's Revenue Accounting Manager's cost to 6%. In 1997, RTC retroactively adjusted the non-regulated telephone share of the manager's cost to 6.5% based on a study RTC conducted. In 1998, the manager charged only 35 hours to non-regulated telephone. RTC's overall assignment of time by the accounting section is in line with non-regulated revenue as a percentage of total revenue. Therefore, ORA used a similar figure, 6%, for 1998.

ORA's second component is the assignment of 1,000 hours of the Revenue Accounting Department's time to development of [*23] the long distance affiliate, RLD. RTC allocated no time to RLD accounting procedure development efforts. Based on the checklist referred to in Audit Calculation 6, ORA estimated that 1,000 hours should have been directly allocated to RLD in 1997 and 1998.

b. RTC

RTC agrees with ORA's adjustment of the Revenue Account Manager's time for 1998. However, RTC does not agree with the assignment of 1,000 hours to RLD. RTC argues that ORA should not have used the checklist because it was never followed. RTC also states that RTC did not incur costs to set up accounting procedures for RLD because the procedures already existed. The procedures are the same as used to set up billing and collection programs for other interexchange carriers.

RTC also states that if such costs had been incurred, they would have been incurred in 1997 when development work for RLD occurred.

c. Discussion

RTC agrees with ORA's adjustment to the Revenue Account Manager's time. We will adopt it. However, we find credible RTC's claim that the accounting procedures used for RLD were already in existence. Therefore, we will not adopt the balance of ORA's recommendation.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	-	(\$ 2,960)	-

[*24]

8. Audit Calculation 8 - Information Services Costs

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 36,397)	-	(\$ 101,171)	-	\$ 132,734

a. ORA

ORA adjusts various information services cost allocations. First, ORA believes that RTC's three factor formula is heavily weighted in prior year's telephone plant purchases and is, therefore, inappropriate to allocate current year information services costs. ORA believes that the Federal Communications Commission (FCC) general allocator is more appropriate.

Second, ORA states that the end user service order and payment and collection factors are based on out of date studies, and were calculated using the wrong methodology. Additionally, the non-regulated allocation of common customer-related costs was omitted.

Third, ORA believes that RTC's general purpose computer allocator is flawed. Virtually all of the computer infrastructure is on RTC's books, much of which provides benefits to all affiliates. RTC's allocator is based on the relative levels of computer assets in each affiliate's balance sheet. This method, therefore, inappropriately overallocates these [*25] costs to RTC.

ORA's adjustment revises the allocations and corrects various mistakes and other omissions.

b. RTC

RTC states that it allocates information services costs pursuant to a study which analyzed the extent of utilization of the services by affiliates and non-regulated operations. Some costs are assigned directly, while others are allocated using the three factor formula, the end user payment and collection factor and the end user service order factor as appropriate. Remaining costs are considered common and allocated to non-regulated using the general allocator.

RTC states that ORA's adjustment should not be adopted because it would have RCS Wireless pay for part of the development of a customer information system it does not use. RTC also claims that ORA's use of revenues, much less book revenues, does not reflect the use of the information systems. Additionally, RTC states that the FCC has determined that revenues do not measure the amount of resources used by an activity.

RTC states that ORA's adjustment is inconsistent with FCC rules, is not reflective of cost causation and should be rejected.

c. Discussion

RTC's end user service order and payment collection factors [*26] are based on out of date studies. RTC's allocations overallocate computer asset costs to RTC because the computer infrastructure is on RTC's books. Therefore, some adjustment is appropriate. However, ORA's allocation based on revenues is also flawed. Therefore, we will adopt half of ORA's adjustments.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Expenses	(\$ 18,198)	(\$ 50,586)	\$ 66,367

9. Audit Calculation 9 - Valuation Project Costs Attributable to RCS Wireless**Proposed Adjustments:**

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	-	-	(\$ 19,125)	-	-

a. ORA

ORA believes that the cost of a valuation study performed to justify transferring RTC's interest in RCS Wireless to RCC at book value was incorrectly charged to RTC. ORA states that the cost should not be charged to RTC because it would not have occurred if RTC had not chosen to get into the non-regulated wireless business, and ratepayers should be indifferent to the existence of non-regulated affiliates.

b. RTC

RTC asserts that since the Commission required the valuation study to determine the fair market value of RTC's interest in [*27] RCS Wireless, the costs should be charged entirely to RTC. However, RTC decided to allocate about one-third to RCS Wireless given the nature of the regulatory requirement for the valuation.

c. Discussion

RCC decided to acquire RTC's interest in RCS Wireless. RCC was required to follow the Commission's transfer pricing rules which in turn necessitated the determination of the fair market value of RTC's interest. Although the study was performed to satisfy a Commission requirement, it was the result of RCC's decision to acquire RTC's interest. Therefore, RTC's ratepayers should not have to pay for the study. The costs should not have been charged to RTC. We will adopt ORA's adjustment.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	-	(\$ 19,125)	-

10. Audit Calculation 10 - Regulatory Costs Charged But Not Billed to Roseville Cable Development

Proposed Adjustments:						
	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	(\$ 5,966)	(\$ 5,966)	-	-	-	-

a. ORA

ORA identified 190 hours charged to Roseville Cable during 1997 that were not charged or billed to below-the-line accounts.

b. RTC

RTC [*28] agrees that those charges should have been recorded to Roseville Cable.

c. Discussion

Since the parties agree, we will adopt the adjustment.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	(\$ 5,966)	-	-

11. Audit Calculation 11 - Human Resource Costs Attributable to Affiliate Development

Proposed Adjustments:						
	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 5,273)	-	(\$ 10,253)	-	(\$ 10,252)

a. ORA

ORA states that during the audit period, RTC failed to identify and assign 675 human resources hours for development and initial staffing. These costs should have been directly assigned to RDC and RCS Wireless. ORA did not find a problem with RTC's common cost treatment of routine human resource activities related to maintaining staffing at existing subsidiaries.

b. RTC

RTC claims that its allocation of human resource expense is reasonable. RTC's human resource functions are centralized. Individual affiliates do not have separate human resource organizations. RTC allocates human resource costs among affiliates based on a head count factor. RTC believes that it is impractical to identify [*29] blocks of human resource time spent on RTC or other individual affiliates. RTC also states that RTC staffed the majority of RDC's sales force by hiring employees of the contractor that had previously worked on RTC's telephone directory. Therefore, the recruiting costs for these personnel were less than might otherwise have been the case.

RTC also alleges that ORA's allocation double counts the allocation of expenses to RDC and RCS Wireless. The double counting takes place because ORA directly assigned costs to RDC and RCS Wireless without removing those same costs from the common cost pool.

c. Discussion

We do not find credible RTC's contention that it is impractical to directly assign any human resource costs. However, we agree with RTC's contention that staffing of RDC should have required less than might have otherwise been expected since the majority of the sales force came from the previous contractor. It also appears that some double counting may have occurred in ORA's adjustment. Therefore, we will adopt 1/4 of ORA's adjustments.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Expenses	(\$ 1,318)	(\$ 2,563)	(\$ 2,563)

12. Woman, Minority and Disabled [*30] Veteran (WMDV) Program Purchasing Costs

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 11,640)	-	(\$ 4,615)	-	(\$ 4,092)

a. ORA

ORA claims that RTC directly assigned two-thirds of the cost of administering the WMDV purchasing program to regulated accounts. ORA states that these costs should have been recorded in common purchasing accounts and allocated to RTC and all affiliates. The WMDV program serves both RTC and its affiliates and, therefore, should be paid for by RTC and the affiliates.

b. RTC

RTC states that the WMDV program is administered solely to meet the Commission's requirements for RTC. It is not administered for any unregulated affiliate. Therefore, RTC believes that these costs should be directly assigned to RTC. However, RTC recognizes that unregulated affiliates may derive some benefit such as expansion of the vendor pool. Therefore, RTC directly assigned two-thirds of the costs to regulated operations and one-third to the common cost pool to be allocated to non-regulated operations and affiliates using the three factor formula.

c. Discussion

We agree that the WMDV program [*31] was created to satisfy Commission requirements. We also agree that non-regulated operations and affiliates derive some benefit. Therefore, given that the WMDV program was created due to a regulatory requirement, we do not believe RTC's allocation is unreasonable. We will not adopt the ORA recommendation.

13. Audit Calculation 13 - Purchasing Costs Attributable to Affiliates

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA

Expenses	-	-	-	(\$ 67,297)	-	(\$ 69,254)

a. ORA

ORA alleges that during 1998 and 1999, RTC treated common purchasing costs as residual costs which were unattributable to specific cost objectives. Therefore, RTC allocated these costs based on its three factor formula. ORA believes that these costs should be attributed to affiliates based on measures of purchasing activity. ORA allocated purchasing costs for RCS Wireless based on the value of RCS Wireless purchases during the audit period.

ORA states that RCS Wireless was allocated 1% of the purchasing costs during a period when 30% of the capital expenditures were for RCS Wireless. ORA believes that while the value of purchases is not [*32] the best allocator, it is more consistent with the underlying nature of purchasing services than RTC's three factor allocation.

b. RTC

RTC believes that allocating purchasing costs based on the relative capital expenditures is not reasonable because it is not consistent with the nature of the purchasing services provided to RCS Wireless. RTC's purchasing department does not evaluate supplier's products, select suppliers, negotiate prices or set standards for RCS Wireless. RCS Wireless performs these functions. RTC's primary role is merely to process RCS Wireless's purchase orders.

RTC says that ORA's adjustment is inappropriate because the vast majority of RCS Wireless purchases did not occur until the last quarter of 1998. Additionally, \$ 11 million of the \$ 11.5 million in capital expenditures by RCS Wireless in 1998 was for the single purchase of a central office switch in November, 1998.

c. Discussion

We find that RTC has provided a reasonable explanation of why its small allocation of purchasing costs to RCS Wireless was appropriate even though its relative amount of purchases was high. We will not adopt ORA's adjustments.

14. Audit Calculation 14 - Common Office [*33] Equipment Maintenance Costs

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 1,991)	-	(\$ 7,303)	-	(\$ 14,890)

a. ORA

ORA found that, during the audit period, RTC failed to allocate office equipment maintenance to affiliates. ORA believes that these are residual costs which should be allocated using the general allocator as required by FCC rules.

b. RTC

RTC does not object to the premise that office equipment maintenance costs should be treated as common costs. However, RTC believes that since these costs are indirectly attributable to affiliate operations, the general allocator is not appropriate. Rather, RTC's three factor formula should be used. Use of the common allocator is not consistent with FCC rules because the costs are indirectly attributable. RTC believes that no adjustment is necessary.

c. Discussion

RTC and ORA agree that office equipment maintenance cost are common costs. We are not convinced, however, that they are not indirectly attributable. Therefore, we will not adopt ORA's adjustments.

15. Audit Calculation 15 - Common Telephone Museum Administration Costs

[*34]

Proposed Adjustments:

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	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	(\$ 966)	(\$ 2,675)	-	-	-	-

a. ORA

ORA determined that the Museum Administrator charged approximately 900 hours to a regulated product management subaccount in 1997. ORA believes that the Museum Administrator's function benefits the corporation as a whole. Therefore, ORA allocated these costs using the FCC general allocator.

b. RTC

RTC agrees that the Museum Administrator should charge his time to a common account. The time was properly charged in 1998 and 1999. RTC agrees that the 1997 time was not properly charged, but disagrees with ORA's calculation. RTC believes that the general allocator should be used because the museum displays are RTC or telephone related. However, RTC believes that ORA's general allocator is inflated by counting goods and services that are resold.

c. Discussion

RTC and ORA agree that the museum administrator's time in 1997 should have been charged to a common account. The disagreement is in the calculation of the allocator.

As discussed under Audit Calculation 32, we believe ORA's calculation of the general allocator is [*35] correct. We will adopt ORA's adjustment.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	(\$ 2,675)	-	-

16. Audit Calculation 16 - Product Development Section Efforts Attributable to Non-Regulated Telephone Activities

Proposed Adjustments:						
	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 16,622)	-	(\$ 16,727)	-	(\$ 16,242)

a. ORA

ORA found that Product Development Section employees directly assigned nearly all of their efforts. ORA analyzed, among other things, the time charged during specific periods when news articles featured articles describing marketing work on non-regulated services. Therefore, ORA determined that the amount of time RTC's Product Development Section employees charged to non-regulated services was too low. ORA believes that the amount of time charged to non-regulated services should have been proportional to the relative regulated and non-regulated revenue.

b. RTC

RTC points out that FCC rules state that costs should be directly assigned where possible. This is what RTC did. In addition, RTC states that the FCC has found that revenues are disfavored as an allocator. [*36]

c. Discussion

We agree that direct assignment of expenses is preferable to an allocation when direct assignment is possible. We are not convinced that ORA's allocation is more reflective of actual cost causation than RTC's recorded direct assignment. Therefore, we will not adopt ORA's adjustments.

17. Audit Calculation 17 - Product Development Section Management and Administration Costs Attributable to RLD

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 10,938)	-	(\$ 12,895)	-	(\$ 13,942)

a. ORA

ORA found that RTC's Product Development Section's managers and their administrative assistants charged virtually none of their time to non-regulated activities. ORA believes that, with the exception of the Long Distance Product Manager whose efforts are entirely attributable to non-regulated operations, 50% of the Development Section's operations benefited both RTC and RLD. Therefore, ORA recommends that those costs should be treated as common costs and allocated as such.

b. RTC

RTC states that for 1997 through August 1998, RLD did not report to the Marketing and Product Development Manager, [*37] therefore, no time recorded by the Marketing and Product Development Management or its administrative staff should be assigned to RLD. Additionally, there is no common administrative staff shared by RTC and RLD.

c. Discussion

RTC has offered a reasonable explanation as to how these costs were assigned. The explanation was provided by RTC's Marketing and Product Development Manager. We find RTC's explanation more credible than ORA's estimate. Therefore, we will not adopt ORA's adjustments.

18. Audit Calculation 18 - Sales Section Efforts Attributable to Development of RLD

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	(\$ 241)	(\$ 4,581)	-	-	-	-

a. ORA

Based on a checklist prepared by an RTC consultant, ORA determined that 200 hours should have been assigned to RLD for sales and marketing development efforts. ORA asserts that even though the checklist was not actually used to develop RLD, the tasks included in the checklist would have been performed. Given that RTC charged only 10 hours to RLD during the development period, ORA believes that its adjustment is reasonable.

b. RTC

RTC states [*38] that the checklist was not used and the activities were never performed. RTC, however admits that 10.5 hours were incorrectly not billed to RLD by RTC for development work during 1997. These costs should be reallocated to non-regulated activities.

c. Discussion

ORA relied on a checklist that was not used. In addition, RTC says that the functions on the checklist were never performed. Therefore, we are not convinced that ORA's adjustment is reasonable and will not adopt it. We will, however, adopt the 10.5 hours adjustment for 1997 proposed by RTC.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Expenses	(\$ 241)	-	-

19. Audit Calculation 19 - Alarm Monitoring, Sales Misallocated to Regulated Expense

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	(\$ 43,695)	(\$ 43,695)	(\$ 47,037)	(\$ 47,037)	(\$ 21,242)	(\$ 21,242)

a. ORA

ORA discovered that RTC allocated approximately 20% of the labor costs and certain non-labor costs from the Alarm Monitoring Sales Section to regulated accounts.

b. RTC

RTC agrees that it did not charge the Alarm Monitoring Sales Section's time properly. [*39]

c. Discussion

Since the parties agree, we will adopt ORA's adjustments.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Expenses	(\$ 43,695)	(\$ 47,037)	(\$ 21,242)

20. Audit Calculation 20 - Customer Services Support Costs

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	(\$ 5,968)	(\$ 104,760)	(\$ 11,443)	(\$ 135,891)	-	(\$ 176,600)

a. ORA

ORA states that customer service support activities, which support common regulated and non-regulated customer service functions, are themselves common. ORA reassigned customer service support costs that RTC had treated as "regulated only" to common subaccounts. ORA then allocated these costs based on the relative amount of regulated and non-regulated revenue managed by the customer service functions.

b. RTC

RTC states that the Customer Service Support Section does not support affiliate operations. It supports RTC's regulated and non-regulated operations. The time is charged directly to regulated or non-regulated operations or common costs depending on the work performed.

RTC discovered that the section supervisor's time was incorrectly [*40] charged to a regulated account. It should have been charged to a common account for 1997 and 1998. Additionally, in 1999 the section was reorganized and given additional responsibilities. Accordingly, the section's time reporting for administrative functions are now recorded as common costs and allocated to non-regulated activities using the customer services manager allocation factor.

RTC states that ORA's use of an allocator based on revenues is inappropriate. RTC states that its adjustments for 1997 and 1998 should be adopted.

c. Discussion

ORA has not provided convincing evidence that RTC failed to properly allocate these costs with one exception. RTC and ORA agree that the section supervisor's time should not have been allocated exclusively to regulated operations. Additionally, we do not find ORA's use of revenues to be more appropriate than RTC's method. Therefore, we will only adopt the adjustments for the supervisor's time as calculated by RTC.

Adopted Adjustments:

Adjustment to Expenses	1997 (\$ 5,968)	1998 (\$ 11,443)	1999 -

21. Audit Calculation 21 - Customer Service Collection Costs

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	(\$ 145,528)	(\$ 331)	(\$ 124,153)	(\$ 155)	(\$ 143,454)

a. ORA

ORA found that RTC allocated almost all of the RTC collection representatives time to regulated accounts. During the audit period, 21,000 hours were assigned to regulated activities, 221 hours to non-regulated coin phone collection and 11 hours to all remaining categories of non-regulated services. ORA reassigned the time as common and allocated it between regulated and non-regulated services based on the amount of regulated vs. non-regulated revenues.

ORA states that RTC's allocation factor is based on the number of regulated and non-regulated lines printed on bills. ORA believes that relative revenues are more reflective of collection costs than the relative number of lines on bills.

b. RTC

RTC claims that the FCC's rules provide that costs are not to be allocated when direct assignment or indirect allocation is possible. Additionally, relative revenues are disfavored as an allocator. RTC states that many of the unregulated services are not supported by RTC's Customer Services Collection Section or are services provided to businesses that require significantly less collection time. Also, RTC states that adjusting ORA's methodology to eliminate non-regulated revenues [*42] that do not involve collection activities produces a non-regulated allocation very close to the amount RTC used. RTC made a correction to its accounting by moving its Collections Supervisor and one of his employee's time from a regulated account code to a common account code for 1998 and 1999.

c. Discussion

We believe that, as stated by RTC, some non-regulated activities would require little or no collection effort. Since RTC's recalculation of ORA's adjustment excluding such non-regulated revenues is very close to RTC's allocation, we will not adopt ORA's adjustment. We will, however, adopt RTC's correction adjustments.

Adopted Adjustments:

Adjustment to Expenses	1997 -	1998 (\$ 331)	1999 (\$ 155)

22. Audit Calculation 22 - Alarm Monitoring Costs Attributable to the Non-Regulated Vendor Alarm Business

Proposed Adjustments:

Proposed Adjustments:		
	1997	
Adjustment to	RTC	ORA
Expenses	(\$ 159,278)	(\$ 159,278)
	1998	
Adjustment to	RTC	ORA
Expenses	(\$ 127,828)	(\$ 127,828)

	1999	
Adjustment to	RTC	ORA
Expenses	(\$ 180,822)	(\$ 180,822)

a. ORA

ORA found that RTC had improperly recorded and allocated certain alarm monitoring costs.

[*43] **b. RTC**

RTC agrees with ORA's adjustment and states that it has taken steps to correct the errors.

c. Discussion

The parties agree on the adjustments. Therefore, we will adopt them.

Adopted Adjustments:

	1997	1998	1999
Adjustment to			
Expenses	(\$ 159,278)	(\$ 127,828)	\$ 180,822)

23. Audit Calculation 23 - Employee Health Insurance Attributable to RDC

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	(\$ 46,610)	(\$ 46,610)	-	-	-	-

a. ORA

ORA determined that certain health insurance costs were paid by RTC on behalf of RDC. RTC caught the mistake in 1998 but did not record an adjustment for 1997. ORA's adjustment makes the correction for 1997.

b. RTC

RTC agrees that the change should have been made for 1997.

c. Discussion

Both parties agree that the adjustment should be made. We will adopt it.

Adopted Adjustments:

	1997	1998	1999
Adjustment to			
Expenses	(\$ 46,610)	-	-

24. Audit Calculation 24 - Corporate Advertising Charged to Regulated Accounts

Proposed Adjustments:

	1997		1998		1999	
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Expenses	-	-	-	-	(\$ 1,918)	(\$ 29,558)

[*44]

a. ORA

In 1999, RCC took out a full page ad on the back cover of the RTC directory. The ad features the names and logos of various subsidiaries and non-regulated businesses. The entire cost of the ad was charged to regulated accounts. ORA points out that the Commission does not permit any of the cost of corporate image advertising to be allocated to regulated operations. However, for conservatism, ORA's adjustment allocates 1/5 of the cost to RTC's regulated operations because the ad listed five RCC subsidiaries of which RTC is one. As an alternative, ORA recommends that none of the costs be allocated to RTC.

b. RTC

RTC does not object to the treatment of this cost as common. However, RTC believes that ORA's allocation based on the number of subsidiaries is inappropriate because it does not reflect the benefits received by each affiliate. RTC believes that its three factor formula is more reflective of the benefits received.

c. Discussion

The Commission does not allow recovery from ratepayers of institutional or goodwill advertising (D.83162 (1974), 77 CPUC 117, 154-5. D.96-12--074, *mimeo* p. 135-6). The advertising that is at issue here had the logos of RTC and four [*45] other affiliates on it. Therefore, we conclude that it was institutional and/or goodwill advertising. As a result we will not allow any of it.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	-	-	(\$ 36,948)

25. Audit Calculation 25 - Development Costs Billable to RLD

Proposed Adjustments:

Adjustment to	RTC	1997	ORA
			(\$ 79,287)
Expenses	-		
Adjustment to	RTC	1998	ORA
			-
Expenses	-		
Adjustment to	RTC	1999	ORA
			-
Expenses	-		

a. ORA

ORA states that during 1997, RTC employees charged approximately 2,567 hours to RLD. However, RTC did not bill RLD for 1,500 of those hours. ORA's adjustment reflects the billing of the additional 1,500 hours for RLD.

ORA states that RTC pays more than the market price for the long distance service it buys from RLD. The difference between what RTC pays RLD and what RLD pays Sprint for the use of Sprint's long distance network goes to the benefit of RCC's shareholders. Therefore, RTC is not the primary beneficiary of RLD's development or operations.

b. RTC

RTC allocates new product and service feasibility analyses, which occur prior to product development and implementation, [*46] to each subsidiary based on RTC's three factor formula, and to RTC's non-regulated division based on the general allocator.

RTC believes this is reasonable because:

- . it addresses costs related to products or services that ultimately are not implemented,
- . all subsidiaries benefit because existing support costs are spread to more subsidiaries,
- . existing subsidiaries benefit from resulting economies of scale, and
- . new products directly benefit the provision of regulated services.

In this case RTC states that the formation of RLD benefited RTC by using RTC's access and billing and collection services.

c. Discussion

The 1,500 hours that ORA assigns to RLD were for the development of RLD. RLD was created and is in operation. While RTC may benefit from RLD's operations, all costs directly related to RLD should have been charged to RLD. We will adopt ORA's adjustment.

Adopted Adjustments:			
Adjustment to	1997	1998	1999
Expenses	(\$ 79,287)	-	-

26. Audit Calculation 26 - Network Engineering Costs Attributable to RCS Wireless

Proposed Adjustments:

		1997	
Adjustment to Expenses	RTC		ORA
	-		-
		1998	
Adjustment to Expenses	RTC		ORA
	-		(\$ 49,033)
[*47]			
		1999	
Adjustment to Expenses	RTC		ORA
	-		(\$ 49,154)

a. ORA

ORA states that inside plant engineering of the RCS Wireless network was performed by RTC. During the audit period, ORA found that RCS Wireless accounted for 20% of the Central Office plant added by RCC. However, RTC inside plant engineering employees charged less than 2% of their time to RCS Wireless. ORA estimates that at least 5% of their time should have been charged to RCS Wireless.

b. RTC

RTC states that the major plant expense for RCS Wireless was for installation of a central office switch. The engineering and installation work for the switch was done by a contractor and paid for by RCS Wireless. RTC's involvement was minimal and was directly assigned to RCS Wireless.

c. Discussion

RTC has demonstrated that the major plant addition by RCS Wireless did not significantly involve RTC's inside plant engineering employees. The costs were paid for or directly allocated to RTC. Therefore, we are not convinced that ORA's adjustments are reasonable and will not adopt them.

27. Audit Calculation 27 - Central Office Facilities Attributable to RCS Wireless

Proposed Adjustments:

Proposed Adjustments:		1997		1998		1999	
Adjustment to Revenues	RTC	ORA	RTC	ORA	RTC	ORA	
	-	-	-	\$ 20,052	-	\$ 147,316	
[*48]							

a. ORA

ORA determined that RCS Wireless occupied central office space at RTC's Citrus Heights central office from October, 1998 until the end of the audit period. RCS Wireless was not charged for the space it occupied. ORA's adjustment includes the revenue that RTC should have received from RCS Wireless for use of the space. The amount is based on the \$ 167,000 RTC claims it charged to RCS Wireless at the close of 1999.

b. RTC

RTC states that it was unable to determine the correct market price to charge RCS Wireless until it completed an agreement with a third party for use of such space. RTC states that before it closed its books for 1999, it recorded an adjustment of \$ 167,000 for the period of November 1998 through December 1999 based on RTC's proposed collocation prices. RTC will true-up those charges based on the charges that will be set for collocation in a pending arbitration proceeding with Covad Communications (Application 00-01-012).

c. Discussion

We find that ORA is correct that RCS Wireless was not charged for collocation during the audit period. RTC booked collocation revenues of \$ 167,368 in late 1999, after the audit period. Our calculation of the audit [*49] results is based on 1999 recorded data except for Audit Calculation 32. Therefore, we will adopt a revenue adjustment of \$ 20,052 for 1998 and subtract this amount from 1999.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Revenues	-	\$ 20,052	\$ 20,052

28. Audit Calculation 28 - Office Space Costs Attributable to RCS Wireless and RDC

Proposed Adjustments:

		1997	
Adjustment to	RTC		ORA
Revenues	\$ 58,012		\$ 58,012
		1998	
Adjustment to	RTC		ORA
Revenues	\$ 63,286		\$ 63,286
		1999	
Adjustment to	RTC		ORA
Revenues	\$ 137,608		\$ 137,608

a. ORA

ORA determined that RTC charged RCS Wireless and RDC a market rate of \$ 1.35 per square foot for leased office space. The Commission's transfer pricing rules require the use of the higher of the fully distributed costs or market costs. RTC's fully distributed costs were \$ 2.75 per square foot. RTC should have charged the higher cost as reflected in ORA's adjustment.

b. RTC

RTC agrees that ORA's calculation of office space costs is correct.

c. Discussion

Since both parties agree, we will adopt ORA's adjustments.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Revenues	\$ 58,012	\$ 63,286	\$ 137,608

[*50]

29. Audit Calculation 29 - Tower License and Roof Space Attributable to RCS Wireless

Proposed Adjustments:

		1997		1998		1999
Adjustment to	RTC	ORA	RTC	ORA	RTC	ORA
Revenues	-	-	-	\$ 15,064	-	\$ 60,258

a. ORA

ORA found that in September, 1998, RTC entered into five-year lease agreements with RCS Wireless to provide space on its antennas and roofs at a specific rate. Within eight months, RTC had entered into contracts to provide similar space to other non-affiliated providers at rates averaging 38% to 56% more. ORA's adjustment assumes that RCS Wireless should have been charged the same as non-affiliated providers.

b. RTC

RTC states that the September 1998 price charged to RCS Wireless was based on the lease prices negotiated with an unaffiliated third party. RTC signed a lease with a third party that provided for the same rate over the lifetime of the lease as was charged to RCS Wireless. In addition, the price was comparable with prices RCS Wireless negotiated with unaffiliated third parties. As market prices have risen, RTC has increased its prices for more recent leases.

c. Discussion

If RTC negotiated a lease price that met our requirements [*51] at the time, subsequent unforeseen developments do not make the lease unreasonable. ORA has not stated that the initial negotiated price was unreasonable at the time. We will not adopt ORA's adjustments.

30. Audit Calculation 30 - Indirect Facilities Overheads Attributable to Non-Regulated and Affiliate Operations

Proposed Adjustments:

	1997	
Adjustment to Expenses	RTC (\$ 184,071)	ORA (\$ 663,480)
Rate Base	\$ 2,921,652	\$ 2,921,652
	1998	
Adjustment to Expenses	RTC (\$ 304,389)	ORA (\$ 899,507)
Rate Base	\$ 2,846,933	\$ 2,846,933
	1999	
Adjustment to Expenses	RTC (\$ 422,928)	ORA (\$ 1,188,646)
Rate Base	\$ 2,792,994	\$ 2,792,994

a. ORA

ORA found that during the audit period, RTC allocated facilities costs to non-regulated RTC operations using a "land and building" allocator based on an outdated building usage study. ORA computed a facilities loading factor of 37.02% to be applied to employee labor dollars to correct RTC's allocation.

ORA states that its calculation matches current activities performed for affiliates and non-regulated operations with current facilities costs. Additionally, ORA's calculation includes [*52] all capital and expense costs associated with facilities. ORA states that RTC did not allocate any land and building costs to affiliates.

ORA believes that although RTC's calculation somewhat refines ORA's calculation, it is not accurate. Therefore, ORA believes that a factor between RTC's 22.6% factor and its 37.02% factor should be used.

ORA notes that in RTC's calculation of its expense adjustment, it not only used a lower factor, but it also applied the factor only to the much smaller pool of labor hours included in its other proposed adjustments.

b. RTC

RTC agrees that its usage study is outdated. However, it does not agree with ORA's 37.02% factor, RTC states that ORA's calculation is wrong because:

- . it assumes all employees use space equally,
- . RTC's outside plant employees have building and plant space dedicated to their use,
- . some land and space are used exclusively by RTC,
- . RCS Wireless leases space from an unaffiliated party,
- . some building investments were excluded by ORA,
- . ORA excluded contract labor used by RTC, and
- . the FCC requires that space be allocated based on how it is actually used.

RTC states that it has not finished updating its [*53] study. Therefore, RTC agrees to use its revised calculation of ORA's factor for this proceeding (22.61%). RTC's revised calculation corrects errors it found in ORA's calculation.

c. Discussion

It appears that ORA's factor of 37.02% is imperfect. RTC's allocation factor has not been shown to be correct. Therefore, as recommended by ORA, we will use a factor in between the two. Since neither calculation has been shown to be better than the other we will split the difference. We will use a factor of 29.8%. Since there is no disagreement on the rate base adjustments, we will adopt them.

Adopted Adjustments: (Does not include expense effect of adopted factor.)

Adjustment to	1997	1998	1999
Rate Base	\$ 2,921,652	\$ 2,846,933	\$ 2,792,994

31. Audit Calculation 31 - Residual Costs Attributable to Affiliates

Proposed Adjustments:

		1997	
Adjustment to	RTC		ORA
Expenses	(\$ 18,126)		\$ 123,958
		1998	
Adjustment to	RTC		ORA
Expenses	(\$ 65,534)		(\$ 834,113)
		1999	
Adjustment to	RTC		ORA
Expenses	-		(\$ 1,887,952)

a. ORA

ORA determined that RTC allocated residual general and administrative costs using a three factor formula. [*54] ORA states that RTC's three factor formula is flawed because:

- . it assigns costs based on assets recorded in prior years,
- . it classifies common assets as belonging to RTC,
- . it classifies employees with administrative and general functions as RTC employees,
- . the three factor formula is applied to the same pool of costs to which the FCC general allocator is applied for allocating to non-regulated telephone activities.
- . use of the three factor formula and the general allocator to allocate the same pool of costs is prohibited by the FCC.
- . the FCC rejected use of the three factor formula for allocating residual costs.

ORA states that residual general and administrative costs should be allocated to affiliates the same way they are allocated to non-regulated operations using the general allocator.

b. RTC

RTC states that use of its three factor formula for allocation to affiliates is appropriate because it is based on cost causation. Since there is a direct link between resource utilization and the size and nature of operations, the three factor formula is appropriate. The three factor formula is based on gross plant, total expenses and employee headcount. RTC states [*55] that since ORA's allocator is not based on available cost-causative indicators, it is inconsistent with FCC requirements. RTC states that its use of the general allocator for allocation of the same pool of costs to non-regulated operations is also appropriate because no cost-causative relationship exists for non-regulated operations. This is because while the affiliates are free standing with respect to RTC, RTC's non-regulated operations are not.

c. Discussion

We will adopt ORA's proposed adjustment. We find that RTC's three-factor formula does not reflect cost causation and leads to an under-allocation of common general and administrative expenses to unregulated affiliates. ORA's use of the general allocator based on expenses is the better of the two approaches in the record.

We begin our analysis by noting that the parties agree that we should apply Part 64 rules. RTC is correct that those rules establish a hierarchy of approaches to allocating costs. Part 64 favors allocation based, whenever possible, upon direct analysis of the origin of the costs and, as a second choice, based upon "an indirect, cost causative linkage" to another cost category (or categories). If neither [*56] of these options are feasible, Part 64 directs the use of a "general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and nonregulated activities." (47 CFR Section 64.901(b)(3)). RTC claims that its three-factor formula comports with the second-choice use of an indirect, cost causative allocator. ORA disagrees that RTC's formula reflects cost causation and concludes that the general allocator must be used.

The fact that RTC claims that its three-factor formula is based on cost causation does not make it so. The issue here is whether the factors identified by RTC would fairly approximate the extent to which common general and administrative costs are caused by RTC, on the one hand, or RTC's regulated affiliates, on the other hand. RTC's three factors are gross plant (i.e., a comparison of the assets of RTC with those of its affiliates); expenses (i.e., a comparison of the expenses of RTC with those of its affiliates) and employee headcount (i.e., a comparison of the number of employees of RTC with those of its affiliates).

We are persuaded by ORA that RTC's three-factor formula does not reflect cost causation and instead over-allocates [*57] costs to RTC. ORA correctly points out that the three-factor formula over emphasizes asset accumulations, both through the gross plant factor and through depreciation expense reflected in the expense factor. As a mature company, RTC has accumulated considerable assets over a long period of time. In contrast, in a dynamic and fast changing period in the telecommunications industry, most of RTC's affiliates - including RDC, RLD, Roseville PCS and RCS Wireless, and RCS Internet--were just coming into existence during the audit period. Even though these affiliates obviously required the expenditure of general and administrative costs, they have had little time to accumulate assets. Consequently, the use of accumulated assets as a significant factor in allocating common costs - as reflected in the gross plant factor and the depreciation component of the expense factor - does not provide a reasonable approximation of the extent to which affiliates caused common costs to be incurred.

ORA makes the point quite well:

"In 1997, Roseville performed financial forecasting and budgeting for a significant new affiliate - RCS Wireless. The amount of budgeting and forecasting effort in 1997 may [*58] have been indirectly related to RCS Wireless' *future* size, but it was definitely not related to RCS Wireless' *past* size (RCS Wireless had no past size). However, for the budgeting and forecasting effort conducted by RTC, RCS Wireless gets no allocation from the asset component of Roseville's three-factor formula, because RCS Wireless has yet to buy the assets being budgeted. RCS Wireless also gets no allocation from the headcount or operating expense components of the formula, because it has yet to hire the employees being forecasted. Using Roseville's backward-looking three factor formula, another subsidiary (guess which one) must have 'caused' the 1997 financial forecasting and budgeting effort conducted for RCS Wireless. The budgeting and forecasting costs in this example were 'caused' by current period activities, not by past-period asset acquisitions. The FCC's general allocator produces a rational allocation of residual cost because it is based on a composite of costs incurred in conducting current period activities. While the general allocator is not perfect (indeed, the forecasting effort described above demonstrates why it is important to identify and directly assign [*59] efforts associated with an affiliate), it is certainly better than an allocator loaded with decades of prior period regulated asset accumulations." (ORA Opening Brief at 70, emphasis in original).

The reasoning of the FCC's Order on Reconsideration in which it modified the Part 64 rules applied here buttresses our conclusion that RTC's three-factor formula over-emphasizes past activities as an estimator of current cost causation. There, in determining how to calculate the general allocator, the FCC rejected AT&T's proposal to use expense data from the prior year. The FCC found:

"AT&T's proposal, to use prior year's data updated quarterly, would appear to produce skewed results in an environment in which nonregulated services offered through the network are expected to grow dramatically. Use of last year's data would consistently understate non-regulated usage." n3

n3 *In re Separation of Costs of Regulated Telephone Service from Costs of Nonregulated Activities*, 2 FCC Rcd. 6283, Par. 83 (1987).

Even though [*60] the FCC wrote those words in 1987, they are more relevant today, when services provided by unregulated affiliates have proliferated and grown exponentially. In this environment, use of an allocator - such as RTC's three-factor formula--that emphasizes past asset accumulation would "consistently understate" usage by unregulated affiliates.

In comments on the Alternate Proposed Decision, RTC cites examples in which it believes the use of the general allocator would have the effect of over-allocating costs to unregulated affiliates. In particular, RTC states that the operating expenses of unregulated affiliates such as RLD and RDC include significant levels of expenses that are billed for activities that are "likely" not reflective of activities performed by RTC personnel, such as the purchase of switched access, long distance service for resale, or directory services. (RTC Opening Comments at 5, citing Ex. RTC-13).

At best, RTC is contending that there are instances in which the general allocator does not lead to perfect cost allocations. n4 However, RTC does not attempt to disprove ORA's showing that, with respect to other instances of establishing new affiliates (such as RCS Wireless), [*61] the emphasis on past asset accumulation in two of RTC's three factors does not lead to a cost-causative allocation of costs, but rather to an over-allocation of costs to RTC.

n4 However, the use of the qualifying word "likely" in RTC's testimony is telling. ORA's points regarding RCS Wireless, quoted above, are equally applicable to RLD, as RLD was a new affiliate during the audit period. General and administrative services such as budgeting, forecasting, and accounting, would also need to be performed for RLD before RLD had assets and employees. In addition, to purchase switched access and long distance for resale requires, at a minimum, planning to set up new budgeting and accounting systems. Thus, we can understand why RTC chose to qualify its testimony, because it is likely that the purchase of access and long distance services did result in the use of RTC personnel. Even if this is not the case, for the reasons explained below, RTC's argument lacks merit.

As the FCC made clear in its order adopting the Part 64 [*62] rules, the main purpose of the rules is to "guard[] against cross-subsidy of nonregulated ventures by regulated services." n5 Furthermore, under the Part 64 rules, RTC must demonstrate that its indirect allocation method is based upon a "cost-causative linkage." As we have explained, RTC has not shown that its three-factor allocator is based upon a cost-causative linkage. In fact, RTC's formula's over-reliance on past asset accumulations leads to over-allocations to the regulated entity, precisely what Part 64 is designed to prevent. Because this record lacks any method that either directly or indirectly allocates costs based on cost causation, under the Part 64 rules, the general allocator is the default allocation device to use.

n5 *In re Separation of Costs of Regulated Telephone Service from Costs of Nonregulated Activities*, FCC 86-564, 62 Rad. Reg. 2d (P&F) 163, pars. 33, 37.

Because RTC's three-factor formula is inappropriate, we adopt ORA's audit adjustment for 1997, 1998, and 1999 using the default general [*63] allocator authorized by Part 64. By this decision, we do not preclude RTC in future years from using an allocator different from the general allocator (but not the three-factor formula that we find deficient in this decision) if RTC can meet its burden of showing that such a different allocator is based on cost-causation and does not lead to cross-subsidy of its unregulated affiliates.

Adopted Adjustments:

Adjustment to	1997	1998	1999
Expenses	\$ 123,958	(\$ 834,113)	(\$ 1,887,952)

32. Audit Calculation 32 - Residual Costs Attributable to Non-Regulated Operations

Proposed Adjustments:

		1997	
to	Adjustment	RTC	ORA
	Expenses	(\$ 65,954)	(\$ 1,040,131)
		1998	
to	Adjustment	RTC	ORA
	Expenses	(\$ 71,783)	(\$ 773,786)
		1999	
to	Adjustment	RTC	ORA
	Expenses	(\$ 32,195)	(\$ 822,620)

a. ORA

ORA states that residual costs are costs for which neither direct nor indirect measures of cost allocations can be found. The FCC requires that these costs be allocated using a general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and to non-regulated activities.

ORA found that in calculating [*64] its general allocator, RTC excluded from directly assigned or attributed expenses a number of non-regulated expenses. RTC excluded all direct non-regulated expenses except alarm monitoring expenses. RTC also excluded indirect non-regulated product management, sales and advertising expenses.

ORA agrees with RTC that it is appropriate to remove the costs of goods sold as required by the FCC. However, the FCC defines the cost of goods sold as the cost of goods held in inventory for resale. ORA states that the costs RTC excluded are not items purchased for resale, and, therefore, should not have been excluded.

The Costs RTC excluded include:

- . customer telecommunications consulting and engineering services provided by RTC employees,
- . installation and maintenance labor and labor loadings related to equipment and wiring sales, equipment leases and warranties,
- . costs of installation, maintenance and collection from RTC's coin phones,
- . depreciation on leased equipment, and
- . indirect costs of product management, sales and advertising expense.

ORA recommends that its proposal, adjusted to remove "material cost of sales," "OEL Maintenance Material" and "T&M Material," be adopted. [*65]

b. RTC

RTC claims that it removed from the calculation of the general allocator only the costs of goods sold.

c. Discussion

The issue here is what is meant by the "costs of goods held in inventory for resale." We do not see how such costs as consulting, engineering, labor loadings, etc. can reasonably fit that definition. These may be related costs, but they are not the costs of the goods themselves. We do not adopt ORA's specific proposed adjustments because they depend on other adjustments we did not adopt. We will, however, adopt ORA's method for calculating the general allocator.

33. Audit Calculation 33 - Regulated Directory Revenue Shifted to RLD

Proposed Adjustments:

Adjustment to	1997		1998		1999	
	RTC	ORA	RTC	ORA	RTC	ORA
Revenues				\$ 286,222		\$ 327,516

a. ORA

ORA's calculation returns 1/2 of the regulated revenue that RTC ceded to RDC when RDC began publishing RTC's telephone directory. ORA claims that RTC's decision to have RTC publish its directory was not based on an adequate study of the costs involved. ORA believes that, as a result, RTC's revenues would be greater if the previous directory publisher had been kept. [*66] ORA recommends that its calculation of the lost revenues or an amount equal to the 5% reduction in regulated directory revenue ceded by RTC to RDC be adopted.

b. RTC

RTC says that its intention in switching publishers was to increase net revenues associated with directory publication. As a result of the change, RTC received greater directory revenues from RDC than it would have from with its previous publisher. RTC further states that had RTC not made the change, its revenues would have decreased.

RTC states that its decision to switch publishers was a management decision. This decision is beyond the scope of the audit and not related to cost allocations.

c. Discussion

ORA's proposal is based upon ORA's disagreement with a management decision to change publishers. ORA has not demonstrated that the decision was deliberately intended to reduce RTC's revenues. Therefore, we will not adopt ORA's adjustments.

D. Calculation of NRF Results of Operations and Earnings

This section addresses how overall NRF results of operations and earnings should be calculated to determine shareable earnings for 1997, 1998 and 1999. In addition to the 33 audit calculations, ORA takes issue with [*67] RTC's reclassification of regulated directory revenues, RTC's expensing of software development costs, and RTC's income tax expense adjustments.

In addition to opposition to the specific adjustments proposed by ORA, RTC objects to consideration of the audit results in this proceeding at all. RTC states that the proposed adjustments are not a proper issue under the Commission's ordered audit scope. RTC also states that its shareable earnings advice letters for 1997 and 1998 were filed and not protested. They should not be reopened now.

1. Regulated Directory Revenues

Proposed Adjustments:

Adjustment to	1997		1998		1999	
	RTC	OR A	RTC	OR A	RTC	OR A
Revenues	(\$ 2,930,811)		(\$ 2,705,613)		(\$ 3,317,400)	

a. ORA

ORA states that pursuant to RTC's publishing agreement with RDC, RTC is entitled to a percentage of the revenue from RTC's directory. RDC's share is to cover all of RDC's costs including sales and marketing.

ORA alleges that RTC removed from regulated directory earnings, revenues from advertiser's in RTC's directory who are located outside of RTC's service territory. ORA represents that RTC removed these revenues prior to applying the allocation [*68] of revenues between RTC and RDC. This is the primary reason that RTC's composite intrastate separation of miscellaneous revenue for 1997, 1998 and 1999 is substantially lower than what was adopted in the 1996 GRC.

ORA states that all NRF companies are required to reflect directory advertising revenues above-the-line for calculating shareable earnings (D.89-10-031, D.96-12-074). ORA also points out that the Commission has never permitted

RTC to reclassify exchange area directory revenues as non-regulated revenues to be excluded from the sharing calculation.

ORA also points out that it agrees with RTC that revenue from publishing directories other than RTC's are properly assigned to RDC.

b. RTC

RTC states that it is appropriate to exclude revenues and expenses from advertisements in RTC's directory by businesses located outside of RTC's service territory. RTC says that such revenues and expenses are non-regulated. RTC states that it is necessary to remove this revenue in order to compensate RDC for the related costs.

c. Discussion

RTC and ORA agree that the RTC directory revenues should be included in the sharing calculation. The issue is whether revenues and expenses due to [*69] advertisers who are located outside of RTC's territory should be excluded. Our policy has been to include all directory revenues and expenses in the calculation. Additionally, the directory publishing agreement between RTC and RDC covers RDC's expenses. Therefore, we do not adopt RTC's adjustment.

2. Expensing of Software Development Costs

Proposed Adjustments:

Adjustment to	1997		1998		1999	
	RTC	ORA	RTC	ORA	RTC	ORA
Expenses					\$ 5,316,223	

a. ORA

ORA states that for 1999 RTC increased regulated operating costs by \$ 5,316,223 to cover the expense for software development. ORA opposes this adjustment because it does not match the costs with the periods over which the software will be used. ORA points out that, as required by the American Institute of Certified Public Accountants Statement of Position (SOP) 98-1, RTC capitalized the costs it incurred in 1999 to develop its "Genesys" customer software system in its books. However, RTC expenses the total cost in 1999 in its sharing calculation. ORA states that RTC has not provided in its exhibits or workpapers any explanation or justification for this adjustment.

b. RTC

RTC states that it expensed [*70] the software development costs in 1999 because the Commission has not adopted SOP 98-1 for ratemaking purposes. RTC states that there are other instances where the Commission has requirements for ratemaking purposes that are different from what is required for financial statements.

c. Discussion

It is not necessary that we specifically adopt SOP 98-1. The "Genesys" software will be used well beyond 1999 and RTC capitalized its development costs. There is no reason that RTC should expense the entire costs in 1999 in its sharing calculation. Therefore, we do not adopt RTC's adjustment.

3. Income Tax Expense

a. ORA

ORA states that RTC uses in its sharing calculations an effective income tax rate that is much higher than the combined California and federal tax rates. RTC's combined rate is 47.28% compared to a combined statutory state and federal tax rate of 40.75%. ORA further points out that RTC's books for 1999 show an effective tax rate of 40.2%. ORA represents that RTC has not justified the allowance for funds used during construction (AFUDC), interest expense and deferred item adjustments to its tax calculations that, among other things, cause the higher effective tax [*71] rate. Therefore, ORA recommends that the combined statutory rate be used.

b. RTC

RTC believes its calculation is correct. It states that it has utilized adjustments consistent with the California ratemaking rules established for RTC in D.96-12-074. RTC also states that ORA is incorrect because it did not use the correct state tax rate adopted in 1997.

c. Discussion

The income tax calculation should follow the same methodology used to develop the startup NRF revenue requirement in D.96-12-074. RTC's explanation that ratemaking adjustments could cause the effective tax rate to be higher than the effective tax rate are plausible. Therefore, we will adopt RTC's methodology to calculate the income tax expense.

E. Adopted Audit Results--Sharable Earnings

Our calculation of sharable earnings based on our adopted audit results is as follows:

	1997	1998	1999
RTC Reported Rate of Return	9.12%	10.14%	10.55%
Adjusted Rate of Return	10.77%	11.86%	14.60%
Benchmark Rate of Return	11.50%	11.50%	11.50%
Sharable Earnings	\$ 0.00	\$ 419,505	\$ 3,781,646

F. ORA's Request for Another Audit

1. ORA

ORA recommends that the Commission order another audit in connection [*72] with RTC's next NRF review. The audit would examine whether RTC's cost allocations are correct.

2. RTC

RTC opposes this recommendation. It states that the Commission established a procedure in Ordering Paragraph 16 of D.96-07-059 that ORA should follow if it believes an audit is necessary.

3. Discussion

The audit performed by ORA in this proceeding found instances where RTC had not properly accounted for its affiliated transactions. By this order, we require RTC to make the necessary corrections. We expect RTC to comply.

The Commission recently issued Order Instituting Investigation (I.) 01-04-026, in which it authorized ORA to perform an audit of RTC in connection with an investigation of RTC's intrastate revenue requirement. In light of that impending audit, we decline to mandate another audit at this time. However, in light of the findings of the audit reviewed in this decision, we expect that it will be necessary to review affiliate and non-regulated telephone relationships and transactions of RCC in connection with the next review of Roseville's NRF. In addition, we note that ORA may, at any time, exercise its broad discovery rights under the Public Utilities Code in [*73] order to fulfill its duties of representing the interests of ratepayers.

VII. Sharing

A. RTC

RTC requested that the sharing mechanism be suspended because it is unnecessary in today's competitive market. RTC also pointed out that D.98-10-026 suspended sharing for Pacific and Verizon. RTC referred to the following language in D.98-10-026.

"...we must now, at a minimum, suspend sharing, with the objective of elimination during the next NRF review (if conditions continue to warrant its elimination). Dramatic changes are underway as a result of passage of the Telecommunications Act of 1996, our opening of local exchange markets to facilities-based and resale competition, our authorizing CPCNs for over 150 CLCs, our authorizing over 100 interconnection agreements, and as CMA points out, rapid changes in technology . . . [P] We are convinced by parties advocating the elimination of sharing that sharing can distort operating and investment decisions. Sharing changes the forecast of present and future cash flows, and introduces greater uncertainty into the present and future stream of revenues, thereby changing the analysis without sharing. . . [P] While distortions to operating [*74] decisions are a vital concern, distortions to investment decisions are perhaps the most costly efficiency consequence of continued sharing, due to the long term effect of delaying or rejecting otherwise cost-effective investments. . . . [P] Moreover, sharing is asymme-

tric. That is, potential competitors . . . make operating and investment decisions without profit constraints. . . . It is imperative . . . that all firms . . . face the same financial analysis as they make operating and investment decisions. It is imperative that our policies not skew the playing field for or against any potential player, including [ILECs]. To do otherwise compromises the efficiency of the competitive process itself."

RTC stated that its experience under NRF provides no evidence contrary to the facts that led to the Commission's conclusion in D.98-10-026. RTC stated that it was not ordered to submit recommendations on market-based and related rates of return in this proceeding. RTC also stated it did not make such a request because the rates of return would be irrelevant if sharing is suspended and eventually eliminated.

B. ORA

ORA recommends that sharing should be retained for the following reasons: [*75]

- . The sharing mechanism has not deterred RTC from increasing its capital investment.
- . Retention of sharing will not result in asymmetrical treatment between RTC and its competitors.
- . There is no real competition in RTC's service area.
- . RTC's ratepayers have not received financial benefits from NRF.
- . RTC's cross-subsidization of its affiliates and other anticompetitive behavior warrant retention of sharing.

ORA alleges that according to RTC's own testimony, RTC has and is making significant investments in technology. Therefore, sharing is not a disincentive to capital investment.

ORA states that sharing only applies to Category 1 and Category 2 services. These are services that are either monopoly services or services that are not fully competitive. Sharing does not apply to Category 3 services which are competitive. Therefore, sharing does not result in asymmetrical treatment between RTC and its competitors because it does not apply to those services where full competition exists.

ORA asserts that RTC's number of access lines, number of customers, local usage minutes and net income have increased under NRF. Competitors only own 1.7% of RTC's total access lines. Therefore, [*76] ORA asserts that RTC has no real competition in its service territory.

ORA states that Pacific's and Verizon's ratepayers received benefits in the form of lower rates because the productivity factors were greater than inflation. On the other hand, even though RTC's productivity factor has been greater than inflation, RTC's ratepayers have received no benefits because price indexing has been suspended. In addition, Verizon's customers benefited from sharing whereas RTC's customers have received no refunds under sharing.

ORA represents that the audit results demonstrate that RTC has engaged in cross-subsidization of its affiliates by improperly allocating costs to and revenues away from RTC. This cross-subsidization of its affiliates is anticompetitive because it allows the affiliate to provide services below actual costs. ORA contends that this cross-subsidization has harmed ratepayers because ratepayers were deprived of sharable earnings and there is a higher likelihood that RTC will ask the Commission for revenue increases by claiming financial difficulties.

ORA also points out that the Commission has retained sharing for Citizens Telecommunications Company of California, Inc.

[*77] C. Discussion

1. Retention of Sharing Mechanism

We conclude that the current sharing mechanism should be retained for RTC. The foregoing discussion of the audit results has demonstrated that RTC has shifted to its regulated operations a significant amount of costs that should have been attributed to non-regulated operations. The audit results show that RTC has effectively cross-subsidized its affiliates at the expense of the reported earnings of RTC. Such cross-subsidization directly contravenes the pro-competitive

policies of this Commission as it unfairly disadvantages the firms which must compete against RTC's affiliates and lack the funding source of monopoly or near-monopoly services. The foregoing further demonstrates that cross-subsidization by RTC depressed RTC's earnings so significantly as to prevent sharing that otherwise would have occurred absent the cross-subsidization. By applying the sharing mechanism to RTC's corrected earnings for 1998 and 1999, shareholders will be denied a measure of the benefits from the improper cross-subsidization of RTC's affiliates. In addition, sharing will allow ratepayers to gain some of the benefits from costs for RTC that should [*78] have been lower had they been properly recorded and allocated.

Under these circumstances, we find that the sharing mechanism should continue to apply to RTC. In light of the documented cross-subsidization that occurred in the period 1997 through 1999, we cannot assume that similar cross-subsidization will not occur in subsequent years. As it has operated here, in future years, the sharing mechanism will serve to limit the benefits that shareholders may reap from any improper cost-shifting we may detect. Combined with effective auditing of RTC's books and records, sharing can serve as an important means of preventing shareholders from benefiting from cross-subsidization. n6

n6 Of course, the Commission may apply other sanctions, including penalties, if it finds that RTC or its affiliates are engaging in practices that violate and statutes or any rules, orders, or other requirements of this Commission.

In addition, we agree with ORA that RTC's experience under NRF is distinguishable from that of Pacific Bell and Verizon. [*79] Unlike customers of those two large LECs, RTC's customers have never experienced rate reductions from the inflation minus productivity portion of the NRF formula. Efficiency gains that RTC has enjoyed under NRF are thus not shared with ratepayers in the form of reductions to Category I rates and Category II rate caps. In light of the continued suspension of the NRF indexing mechanism, n7 the sharing mechanism is an important means by which we can allow ratepayers at least an opportunity to gain some tangible benefits from NRF regulation. We note that California's other similarly situated mid-sized LEC, Citizens, has agreed to retain sharing as part of a negotiated settlement.

n7 See Section IX below.

Moreover, although RTC asserts that the sharing mechanism can have an adverse impact on innovation and new investment, the record does not show that the current sharing mechanism has had that effect on RTC. Under the sharing mechanism, RTC has undertaken a variety of major investment initiatives. Through its Avalanche [*80] project, RTC has upgraded transmission quality to permit faster communications speeds over switched telephone lines. In addition, RTC has deployed DSL service and ATM service in order to provide increased bandwidth for its residential and business customers. These upgrades and new services have required substantial levels of capital investment. RTC claims to be a technologically advanced local telephone company whose advanced capabilities rival those of the largest local carriers. The record does not provide any reason to challenge this assertion.

Finally, we reject RTC's claim that the sharing mechanism places the company at a competitive disadvantage. As ORA points out, the sharing mechanism does not apply to any of Roseville's Category III services and therefore can have no effect on services for which RTC lacks significant market power. The services to which the sharing mechanism applies, Category I and II services, are by definition services over which RTC has significant market power. The sharing mechanism serves as a check to prevent excessive exploitation of that market power. In short, sharing only affects services for which competition is either weak or non-existent. Roseville [*81] does not identify any competitive harm that it has suffered as a result of the sharing mechanism. n8

n8 RTC expresses concern that Pacific Bell or Verizon, companies for which sharing has been suspended, could compete in RTC's service territory and exploit their advantage of not being subject to sharing. However, RTC's argument overlooks the fact that any competitive forays by Pacific Bell or Verizon in RTC's territory would be done by separate competitive local exchange carrier (CLEC) operations of those companies and that those CLEC operations would not be subject to sharing in any event. Thus, the suspension of sharing for Pacific and Verizon will have no impact on their ability to compete against RTC. However, RTC enjoys the significant advantages of incumbency and continues to hold dominant market shares for residential and business local service.

In comments on the Alternate Proposed Decision, RTC argues that: (1) in D.98-10-026, the Commission found that the possibility of sharing in the future was not a reason [*82] to preserve the sharing mechanism; and (2) with the suspension of the sharing mechanism, it is no longer appropriate to use a sharing mechanism as a means of ensuring that the NRF mechanism avoids excessively generous or insufficient earnings. Neither argument is persuasive.

In D.98-10-026, we did not have the record we have here, which shows, based on a fully litigated audit, that the incumbent local exchange carrier (ILEC) misallocated costs in a way that permitted cross-subsidization of an unregulated affiliate. Nor did we have a record, such as we have here, in which an ILEC's *reported* earnings were below the earnings threshold, but *corrected* earnings were above the earnings thresholds. This, this record is quite different from the record upon which D.98-10-026 was based. This record fully supports the retention of sharing as a means of preventing RTC's shareholders from benefiting from similar cost-misallocations and cross-subsidization in the future.

With respect to its second argument, RTC reads excessively narrowly our 1989 decision first adopting a NRF for Pacific Bell and (then) GTE California. There, the Commission concluded that it should adopt sharing as part [*83] of its new incentive-based regulatory mechanism to provide "self-correcting protections." n9 We stated:

A regulatory structure which combines the price cap indexing *approach* with a sharing mechanism can provide protection to both shareholders and ratepayers from the risks that the indexing method may over- or underestimate the revenue changes which are needed to keep the utility financially healthy--but not too healthy. (*Id.*, emphasis added).

n9 *Re Alternative Regulatory Frameworks for Local Exchange Carriers* (D.89-10-031), 33 CPUC 2d 43, 134.

The suspension of the inflation minus productivity component does not equate to an abandonment of the price cap indexing approach that was first adopted in D.89-10-031. In fact, as we stated in D.95-12-052, the "actual impact" of the suspension of the inflation minus productivity component of the indexing formula is to "equate the productivity factor 'X' with the GDPPI inflation factor." n10 As stated above, the record of this case, including the fact that RTC [*84] has never had a productivity factor that exceeds the inflation factor, leads us to conclude that it would be prudent to retain sharing as a means of preventing excessive earnings that may result from the price cap indexing approach that we continue to apply to RTC. n11

n10 *Re Incentive-Based Regulatory Framework for Local Exchange Carriers*, 63 CPUC 2d 377, 393. There, we noted that, for Pacific Bell, the effect of suspension was to reduce Pacific's productivity factor for that year from 5% to 2.9.

n11 Of course, RTC will also benefit from the corresponding earnings "floor" provisions of the sharing mechanism.

2. Refund of Sharable Earnings

Since sharing should have occurred in 1998, ratepayers should be made whole for the shareable earnings they did not receive. Therefore, we will require RTC to amend its 1999 shareable earnings filing to reflect the adjustments included herein. RTC shall add to the 1999 sharable earnings \$ 419,505 that should have been shared in 1998 plus interest calculated in accordance [*85] with Ordering Paragraph 16 of D.89-10-031.

The 1999 sharable earnings calculation in this decision is based on 1999 recorded data with one exception. Audit Calculation 32--Residual Costs Attributable to Non-Regulated Operations is based on partial year data. Therefore, RTC may use full year data for Audit Calculation 32 in its amendment.

In order to ensure that this decision is properly implemented, we will allow ORA additional time to review the amended 1999 shareable earnings filing. Therefore, we will require RTC to provide ORA with an advanced copy of its

amended filing, including complete workpapers, 30 days before it is filed. ORA and other parties will then have the opportunity to provide comments on the filing as provided for in General Order 96-A.

VIII. Depreciation

A. RTC

RTC requested that the requirement to annually file for approval of depreciation rates be eliminated. RTC stated that this requirement treats it differently than Pacific, Verizon and its competitors. RTC referred to the following language in D.98-10-026.

"We agree with Pacific that the lack of competitive neutrality in depreciation regulation harms competition, consumers and incumbent firms. [*86] The harm results from possible negative effects on investment decisions, leaving consumers with higher prices and fewer services. The negative influence occurs when investment decisions are skewed by regulated depreciation rates (if not equivalent to market depreciation rates) used in economic analyses for some firms but not others. We also agree with GTE that this asymmetry subjects GTE and Pacific to administrative costs not required of CLCs, and is needless with the suspension of sharing. Thus, our concern about competitive neutrality, and desire to level the playing field whenever possible, persuades us to permanently eliminate depreciation reviews and approvals."

RTC stated that, given these findings, there is no reason to continue the depreciation filings.

RTC states that by eliminating annual depreciation reviews, the Commission would shift the risk and reward of future investment decisions from ratepayers to shareholders. This will establish a risk-reward structure commensurate with what NRF was established to accomplish and on par with the evolving competitive marketplace.

RTC states that in D.98-10-026, the Commission found that elimination of depreciation reviews would [*87] permanently foreclose any potential franchise impact claim with respect to new investments and depreciation from the effective date of the decision. The Commission rejected the suggestion that the elimination of depreciation reviews would foreclose potential franchise impact claims with respect to investments made before the requirement was eliminated. The Commission also stated that it cannot rule out any stranded cost claim for past investments and depreciation. RTC requests that the Commission should make a similar statement in this proceeding.

RTC alleges that there is no need for a final depreciation study as proposed by ORA. Even if the result would be an increase in depreciation accruals, the effect on sharing would be minimal. However, if the Commission does order a final depreciation review, it should allow RTC to recover any increased expense through a revenue increase. This would be done either through increased prices or through the Z factor or Limited Exogenous (LE) factor mechanism.

RTC does not object to working with ORA to provide information on depreciation. However, it opposes ORA's proposed annual reports because they are not required from Pacific or Verizon.

[*88] B. ORA

ORA does not oppose eliminating annual depreciation filings so long as RTC is required to adhere to the following requirements which were imposed on Pacific and Verizon in D.98-10-026.

- . Permanently give up any potential franchise claim covering investment and depreciation for future investment;
- . Do not request changes in customer rates due to changes in depreciation rates; and
- . Determination of Z-factor treatment of depreciation changes resulting from the move towards economic lives should be determined only after a review of the magnitude and the cause of the change.

ORA recommends that RTC also be prohibited from recovering any franchise impact claims resulting from past investments. ORA believes this is reasonable because RTC did not make any effort to minimize the potential for franchise impact claims by aggressively pursuing competitive depreciation lives for technology accounts as Pacific and Ve-

rizon have. RTC has not changed its depreciation rates since 1994. Pacific and Verizon have aggressively pursued shorter lives and technical updates since 1990. RTC should also have done this.

ORA also recommends that, in return for elimination of depreciation filings, [*89] RTC should be required to do the following:

- . File a final depreciation study using economic lives for review and approval by the Commission; and
- . Provide an annual depreciation report to ORA by June 30 of each year setting forth the data on depreciation rates, depreciation lives used, reserve balances and any other depreciation parameters used.

ORA expects that its proposed final depreciation review will not increase depreciation rates. However, if it results in higher rates, RTC should not be granted a revenue increase because the increase would be due to RTC's failure to update depreciation rates in a timely manner. If the result is a significant decrease, RTC should be required to reduce its rates.

ORA points out that RTC's high depreciation rates have resulted in high depreciation expenses and, as a result, lower sharable earnings. Unless RTC changes its depreciation rates, sharable earnings will be reduced.

ORA says that Pacific, Verizon and CTC have voluntarily agreed to provide an annual depreciation report to ORA. In Citizen's case, the report is part of a settlement agreement adopted by the Commission. ORA believes that such reports are important tools for monitoring [*90] depreciation rates.

C. Discussion

The parties agree that depreciation reviews should be eliminated. Therefore, we will eliminate them. Regarding franchise impacts, elimination will foreclose recovery of franchise impacts for future investments and depreciation. Recovery of franchise impacts for past investments and depreciation is best addressed when and if RTC files such a request. We will not require a final depreciation review because ORA has not shown that such a review is necessary to protect ratepayers. In particular, ORA has not shown that updated depreciation rates would have any effect on sharable earnings. In fact, some of ORA's arguments suggest that, for certain accounts, RTC's depreciation expense has been lower than would be expected. We also decline to mandate annual depreciation reports, as ORA has not demonstrated that the benefit outweighs the burden. However, we expect RTC to cooperate with ORA in providing information when requested.

IX. Price Indexing

A. RTC

RTC requested that the "I-X" price indexing formula, which was adopted and suspended in D.96-12-074, continue to be suspended. RTC pointed out that, in D.98-10-026, the Commission continued suspension [*91] of the price indexing formula for Pacific and Verizon.

RTC stated that reinstatement of indexing would cause it financial harm. It stated that it would cause inefficient pricing and resource allocation because it is uniformly applied to all prices. This would cause below cost prices to move further below cost. RTC also pointed out that it cannot use market power to manipulate Category 1 rates because they are set by the Commission. For Category 2 services, it cannot charge below the floor rate and use other revenue to cross-subsidize below cost rates to gain a competitive advantage. For the above reason, RTC believes that there is no reason to reinstate price indexing.

RTC proposed that, if the suspension is lifted, a productivity factor of no more than 2.69% should be used. RTC represents that this value represents the most current information on total industry productivity.

B. ORA

ORA agrees with RTC that the suspension of price indexing should continue. Additionally, there would be no change in rate caps, ceiling or floors for Category 1 and 2 services and no change in pricing flexibility.

C. Discussion

Because the parties agree and the record does not contain a contrary [*92] proposal, we will continue suspension of the I-X portion of the price adjustment formula.

X. Z-Factor Process

A. RTC

1. General

RTC proposes that the Commission modify the Z-factor criteria to narrow the scope of exogenous events that qualify for recovery. Specifically, RTC proposes that the Z-factor criteria be changed to the following.

a. Specific existing items already identified by the Commission such as the future extended area service (EAS) transition authorized by D.96-12-074.

b. Z-factor items that are now being implemented such as the Interstate Universal Service Fund, Pay-phone Deregulation, and Ordering, Billing and Collection Equal Measure, and Fiber to the Curb Adjustments.

c. Adjustments for impacts of jurisdictional cost shifts.

d. Recovery of Commission mandated cost changes when authorized by a Commission decision.

RTC stated that, for Pacific and Verizon in D.98-10-026, the Commission authorized recovery for limited future exogenous factors and eliminated recovery of new ones except for specified adjustments already identified in other Commission proceedings. RTC cited the following language from D.98-10-026.

"elimination of new Z-factor [*93] recovery shifts risks to shareholders, is consistent with our removing the upper and lower bounds on earnings, reduces asymmetry, simplifies the regulatory process, and is compatible with our promotion of competition, as we continue through this transitional period to a fully competitive market."

RTC believes its proposal is consistent with the above language.

2. PBOP

RTC states that, at the time D.92-12-015 was issued, RTC was not a NRF company. Accordingly, RTC followed those portions of D.92-12-015 applicable to cost-of-service regulated utilities. D.92-12-015 required cost-of-service utilities to true-up their PBOP expenses as part of their next general rate case (GRC). RTC's PBOP expenses were trued up, and the switch of PBOP expenses to accrual recovery was authorized in the next GRC (D.96-12-074). Since D.96-12-074, there have been no Z-factor adjustments for PBOP or any other expenses that were the basis of RTC's NRF start-up revenue requirement set in D.96-12-074.

RTC states that the fact that actual accruals are different from those adopted in D.96-12-074 does not justify ORA's proposed revenue reduction. PBOP is no different from any other element of the results of [*94] operations forecasted in the GRC. Furthermore, ORA's proposed refund constitutes prohibited retroactive ratemaking. Additionally, if the Commission were to adjust rates prospectively for this expense, it should also do so for all other elements involved in the revenue requirement adopted in D.96-12-074.

RTC alleges that the requirements of D.92-12-015 and D.97-04-043 for NRF companies apply only to Pacific and Verizon. Since RTC has never requested Z-factor recovery of PBOP, these requirements do not apply to RTC.

RTC represents that it has been placing funds in the PBOP trust. It made contributions of \$ 129,896 in 1998 and \$ 57,801 in 1999. The lower amount in 1999 was due to the fact that the trust earned in excess of what would be expected based on the forecast 1996 GRC test year PBOP expense of \$ 98,600. Additionally, RTC says that it has been unable to place funds in the trust on a year-by-year basis because of Internal Revenue Code requirements. Accordingly, RTC has invested the additional PBOP funds until such time as they can be contributed to the trust. The funds were not diverted.

B. ORA

1. General

ORA does not oppose eliminating new Z-factor adjustments, establishing [*95] an LE mechanism, and allowing recovery for those items that have been expressly ordered by the Commission for implementation in 2000 and thereafter until they expire or the Commission orders otherwise. However, ORA opposes recovery of changes in EAS payments because such recovery is not currently a Z-factor. ORA believes that any recovery of EAS payments must be considered as an LE factor adjustment. ORA does not oppose LE factor recovery of RTC's payment of the auditor's costs of the non-regulated operations audit.

2. PBOP

ORA proposes that accrual rate recovery for PBOP be eliminated for RTC through a permanent annual revenue reduction of \$ 98,600. In addition, ORA recommends a one time refund of \$ 165,904 to ratepayers for PBOP funds that were not deposited in an independent qualified PBOP trust as required by the Commission.

ORA states that RTC did not receive Commission authorization to fund PBOP accruals until its 1996 GRC. In the 1996 GRC decision, D.96-12-074, the Commission set RTC's initial revenue requirement for PBOP accruals.

ORA states that in D.92-12-015 the Commission authorized those utilities subject to cost-of-service regulation to recover PBOP costs associated [*96] with the switch to accrual accounting and paid into independent trusts to the extent that they, among other things, establish independent PBOP trusts and make tax-deductible contributions which do not need to be grossed up by a net-to-gross multipliers. The decision also provided that NRF utilities could recover, through Z-factor filings, the amount required to be accrued that year to cover future costs less pay-as-you-go costs. Additionally, NRF utilities could recover only the amount actually put into a PBOP trust. Z-factor treatment of PBOP would be tried up in subsequent price cap filings. ORA represents that these requirements were reaffirmed in D.97-04-043.

ORA claims that RTC has not made adequate tax-deductible PBOP contributions, has not recovered PBOP costs through Z-factor filings and has not tried up PBOP costs in its annual price cap filings. Since RTC is a NRF utility and RTC has not been exempted from the requirements of D.92-12-015 and D.97-04-043, RTC is in violation of item. Therefore, the revenue requirement for PBOP should be removed from RTC's authorized revenues. This would be a permanent, reduction of \$ 98,600 in annual revenues.

ORA asserts that RTC did not [*97] make PBOP contributions to the trusts in 1997 and 1999. This resulted in over-collected revenues of \$ 165,904. ORA recommends that these funds be refunded to ratepayers.

C. Discussion

1. General

RTC and ORA agree on eliminating new Z-factor adjustments, establishing an LE factor mechanism and allowing recovery for those items that have been expressly ordered by the Commission for implementation in 2000 and thereafter. Additionally, there is no opposition to LE factor recovery of the non-regulated operations audit costs. However, ORA opposes RTC's proposal to allow recovery of specific items not already identified by the Commission for potential Z-factor treatment.

In D.98-10-026, the Commission eliminated consideration of new Z-factor adjustments. This was done in order to shift more of the risk of cost changes to shareholders and to eliminate the asymmetry with regard to competitors. Additionally, elimination is consistent with the suspension of sharing and simplifies the regulatory process.

The Commission allowed continued consideration of Z-factors then under review and allowed existing Z-factor adjustments to finish implementation. This was done because prior Z-factor [*98] treatment has increased rates in some instances, with offsetting decreases expected in later years.

The Commission implemented a streamlined advice letter process that allows Pacific and Verizon to request recovery of cost increases or decreases resulting from (1) matters mandated by the Commission and (2) changes in total intrastate cost recovery resulting from changes between federal and state jurisdictions. This process, called the LE factor mechanism, was adopted because the two allowed exceptions remain potentially significant exogenous events outside of management control. Rate changes for Commission-mandated cost changes are limited to those costs for which LE factor adjustment is authorized in the underlying Commission decision.

We see nothing unique about RTC that would justify treating it differently. Therefore, we will eliminate Z-factor recovery immediately. We will allow further consideration of Z-factors currently before us. We will also finish imple-

mentation of those Z-factors now being implemented. We will also allow LE recovery of the non-regulated operations audit costs.

In D.00-11-039 in A.99-08-043, the Commission addressed EAS replacement funding. The Commission [*99] ended Pacific Bell's payments to RTC for EAS and authorized interim recovery from the California High Cost Fund - B. The Commission also instructed the ALJ assigned to that proceeding to issue an order instituting investigation (OII) into RTC's revenue requirement to determine the amount to be recovered and whether recovery should be from RTC's stockholders, ratepayers or both. Given this development, there is no need to address EAS in this proceeding.

2. PBOP

In D.92-12-015, the Commission stated the following about PBOP:

"We must consider whether NRF utilities should make a one-time Z-factor filing or annual Z-factor filing to reflect PBOP costs. We note that pay-as-you-go costs are projected to increase over time. Furthermore, if we retained pay-as-you-go accounting, any increase in pay-as-you-go costs would not be entitled to Z-factor treatment. Therefore, the NRF utilities' additional recovery for PBOP costs through the Z-factor should be limited to the difference between what is required by accrual accounting and what their pay-as-you-go costs otherwise would have been. It appears that the difference between the amount required for PBOP costs under accrual accounting [*100] and the amount required under pay-as-you-go accounting may decrease over time. Indeed, we have earlier noted evidence that the cost of an accrual funded plan would eventually be less expensive than a pay-as-you-go plan. Therefore, we should not authorize NRF utilities to recover as a *permanent* Z-factor the increase in rates for PBOP necessary during the *first* year. If we did that, the NRF utilities might realize a windfall. Accordingly, it appears that yearly adjustments to the Z-factor recovery for PBOP costs will be required. Our decision today will order such annual adjustments." Ordering Paragraph 2, 3 and 8 of D.92-12-015 provide:

"2. Regulated utilities under traditional cost-of-service ratemaking and the new regulatory framework (NRF) shall be authorized to recover their PBOP costs associated with the adoption of the Statement and actually paid to independent trusts to the extent that the utilities:

"a. Establish and use independent trusts for the receipt, investment, administration, and disposition of PBOP.

"b. Make tax-deductible contributions which do not need to be grossed up by a net-to-gross multiplier. Earnings to the trust may be tax-free or taxable [*101] to the trust or employees.

"c. Use PBOP trust funds for only PBOP.

"d. Incur PBOP costs that the Commission finds are reasonable and necessary to meet funding requirements based on fair actuarial assumptions, contributions, and investments.

"e. Do not use PBOP to enhance pension benefits.

"f. Recovery of tax-deductible contributions in any given year shall not increase over the prior year's PBOP expense recovery by more than 1% of the utilities total prior year's operating revenue. For those utilities under NRF, the 1% limit shall be applied to the net changes in their annual price cap revenue base.

"g. The utilities shall, to the extent allowed by the Internal Revenue Service (IRS) and employee unions, apply surplus pension assets (as defined by the IRS) to fund their PBOP expense.

"3. To the extent that PBOP trust assets cannot or are not used for PBOP obligations, then those assets shall be returned to ratepayers as allowable by law. Utility rates are hereafter made subject to refund, but only to the extent necessary to allow such a return to ratepayers of any PBOP assets that cannot be used for PBOP expenses or that have been used for other purposes.

"8. In addition [*102] to the requirements of Ordering Paragraph 2, NRF utilities shall recover through annual Z-factor filings only the amount required to be accrued that year to cover future PBOP payments, *minus* their pay-as-you-go costs. Furthermore, the Z-factor should only recover this amount to the extent it is actually put into a trust. The Z-factor treatment of PBOP costs shall be trued up in each subsequent years' Z-factor filings to ensure compliance with these requirements."

When we authorized the switch to accrual accounting for PBOP, we anticipated an initial revenue requirement increase followed by decreases over time. For Pacific and Verizon, we established the revenue requirement increase as a Z-factor in D.92-12-015. We expected annual Z-factor adjustments in the PBOP as the revenue requirement decreased. Finally, in D.98-10-026, we eliminated the remaining PBOP revenue requirement and eliminated Z-factor recovery of PBOP.

In RTC's case, in D.96-12-074, we trued up PBOP costs prior to 1997 and set an initial PBOP revenue requirement. We also adopted for RTC the basic NRF as it had been adopted for Pacific and Verizon. Therefore, the NRF PBOP requirements placed on Pacific and Verizon [*103] apply to RTC. As a result, decreases in the PBOP revenue requirement for RTC should have been addressed in their Z-factor filings. Additionally, since we eliminated the PBOP revenue requirement for Pacific and Verizon in D.98-10-026, we should do so for RTC in this proceeding.

RTC argues that if other expenses reflected in its GRC in D.96-12-074 are adjusted, all expenses should be adjusted. In general we would agree. When we adopt a revenue requirement in a GRC, it is for the purpose of setting reasonable rates. It is not a rigid budget that the utility must follow in the test-year or succeeding years. However, there are exceptions. In Conclusion of Law 7 in D.92-12-015, we said:

"the utilities under traditional ratemaking and the telecommunications utilities under the NRF process should recover their PBOP costs in rates to the extent that they are able to make contributions to tax-deductible plans."

Therefore, PBOP is such an exception.

RTC and ORA agree that the PBOP revenue requirement established in D.96-12-074 for RTC is \$ 98,600. Therefore, consistent with our treatment of Pacific and Verizon, we will reduce RTC's annual revenue requirement by \$ 98,600. RTC's rates shall [*104] be adjusted accordingly.

RTC states that in 1998 and 1999 it made PBOP contributions of \$ 129,896 and \$ 57,801 respectively. RTC made no contributions in 1997. RTC states that those PBOP funds not invested in the trust because of Internal Revenue Code requirements, are invested in income producing vehicles until such time as RTC can place them in the PBOP trust. RTC also states that it would need less than \$ 300,000 in the PBOP trust to satisfy the requirement that all of the PBOP revenue requirement must be invested in the PBOP trust. RTC states that the current balance is over \$ 1.2 million. We conclude, therefore, that the PBOP trust is well funded and that RTC has not put all of the PBOP revenue requirements for 1997, 1998 and 1999 in the PBOP trust. We do not conclude, however, that RTC has diverted the excess revenue requirement funds to other uses. As a result, we will require RTC to file an advice letter to make a Z-factor adjustment to return to ratepayers the 1997 through 1999 PBOP revenues not invested in the PBOP trust. We shall also require RTC to file an advice letter to refund PBOP revenues not placed in the PBOP trust in 2000 and to reduce the 2001 annual revenue requirement [*105] by \$ 98,600 as a surcredit. The \$ 98,600 annual revenue reduction will be permanent. Once the funds have been returned to ratepayers and the \$ 98,600 revenue reduction has been implemented, the Z-factor adjustment shall be eliminated and no further Z-factor adjustments for PBOP shall be filed.

RTC states that the excess POBP revenue requirement funds have been invested. Therefore, in addition to the funds themselves, the investment proceeds earned by these excess funds, shall also be returned to ratepayers.

XI. Monitoring Reports

ORA and RTC have reached agreement to eliminate certain monitoring reports and to modify the filing frequency for others. The amended list of monitoring reports is included as Attachment A.

Since ORA and RTC are in agreement, we will adopt their recommended list of monitoring reports.

XII. Pricing Flexibility

Initially, RTC proposed that the pricing flexibility rules be modified to eliminate the need for cost studies before pricing flexibility can be exercised. RTC proposed instead that it not be allowed to set prices below what the competition is charging or the price floors already established for Pacific and Verizon.

Upon further consideration [*106] of the issue, RTC withdrew its proposal. ORA opposes RTC's initial proposal but not the withdrawal of the proposal. Therefore, we need not address RTC's initial proposal.

XIII. Promotional Offerings

A. RTC

RTC asks that the Commission re-affirm its existing authority to make promotional service offerings with no imputation requirement.

On August 27, 1998, RTC filed Advice Letter 423 requesting authorization to waive 50% of the non-recurring charges for additional access lines. At the time this application was filed, the advice letter had not been approved. The Commission approved Advice Letter 423 in Resolution T-16276 dated July 22, 1999. However, the resolution imposed an imputation requirement on RTC.

RTC states that imputation has only been a requirement for permanent pricing flexibility. The Commission has never required imputation for RTC's promotional offerings prior to Resolution T-16276.

B. ORA

ORA opposes RTC's request to remove the imputation requirement for promotional offerings. ORA recommends that, since promotional offerings involve complex pricing issues, the Commission should examine each promotional offering on an individual basis to determine whether [*107] imputation is appropriate.

C. Discussion

In the Assigned Commissioner's Ruling and Scoping Memo dated May 19, 1999, one of the issues was whether RTC could make promotional offerings. Since Resolution T-16276 approved RTC's promotional offering subsequent to the ruling, the issue of whether RTC can make promotional offerings is moot.

Imputation was not an issue at the time the Assigned Commissioner's Ruling was issued. It became an issue for RTC when the Commission adopted Resolution T-16276 on July 22, 1999. Therefore, strictly speaking, the issue of imputation is beyond the scope of this proceeding. More importantly, however, RTC's problem is with Resolution T-16276. If RTC wants to challenge Resolution T-16276, this is not the place to do so. We will not address imputation in this proceeding.

XIV. Service Quality

D.96-12-074 ordered RTC to provide as part of its NRF review a comparison of service quality measurements before and after NRF implementation. RTC submitted the required data which demonstrated that it has exceeded all General Order (GO) 133-B service quality measurement standards since becoming a NRF company. The data also shows that in most areas that are measured [*108] under those standards, service quality under NRF is better than before NRF.

A. ORA

ORA agrees that RTC's service quality is in compliance with GO 133-B service quality standards. However, ORA recommends that the Commission implement customer service guarantees for RTC. The guarantees would apply to new installations and repair orders. The purpose is to ensure that RTC's current level of customer service does not decline. ORA states that its proposal is an incentive, rather than a punitive measure. The guarantees consist of rebates to customers when new installations or repairs are delayed beyond specified times.

B. RTC

RTC opposes customer service guarantees. ORA made similar proposals in RTC's last GRC and the Commission rejected them. RTC states that competition provides it with a sufficient incentive to maintain service quality. Additionally, according to RTC, ORA's proposal is inconsistent with the move toward competition. RTC also contends that in D.00-03-052 in R.98-06-029, the Commission rejected similar proposals by ORA to modify GO 133-B.

C. Discussion

ORA correctly points out that GO 133-B does not include standards for the length of time that telephone companies [*109] should take to install and repair telephone service. n12 ORA's service guarantee proposal would provide incentives for RTC to complete installations and repairs in a timely manner. If the record disclosed any indication that customers have been adversely affected by any service quality deteriorations under NRF, we would be inclined to adopt ORA's recommendation. However, ORA has not made such a showing. Accordingly, we reject ORA's proposal.

n12 With respect to installations, GO 133-B only counts orders held over 30 days and requires reporting of the percentage of installation commitments that are not met. GO 133-B does not set a target for how long a telephone company should take to install telephone service or include incentives or penalties for installations that take longer than a reasonable period. With respect to repairs, GO 133-B only counts the number of trouble reports by customers. It does not specify a target for how long a telephone company should take to restore service or provide any incentives or penalties for repairing service in a reasonable period of time.

[*110]

In so concluding, we nevertheless underscore the importance of ensuring that our regulatory policies - including the use of incentive frameworks such as NRF - promote high quality customer service, particularly for those customers who are served by monopoly or near-monopoly providers. We encourage ORA to continue to monitor RTC's service quality and to take full advantage of its statutory discovery rights in so doing. ORA should not hesitate to bring to the Commission's attention any significant deterioration in RTC's service quality that it may detect.

Findings of Fact

1. A.99-03-025 appeared in the Commission's Daily Calendar on March 18, 1999.
2. RTC's three-factor formula for allocating common general and administrative expenses does not reflect cost causation and leads to an under-allocation of such expenses to unregulated affiliates.
3. Sharing should have occurred in 1998 in the amount of \$ 419,505.
4. The adopted audit calculations as discussed in VI. C, D and E, herein, are reasonable.
5. The adopted audit calculations show that RTC has effectively cross-subsidized its affiliates at the expense of the reported earnings of RTC.
6. RTC's cross-subsidization had the effect [*111] of preventing sharing that otherwise would have occurred.
7. The sharing mechanism serves to limit the benefits that shareholders may reap from improper cost shifting.
8. RTC's customers have never experienced rate reductions from the inflation minus productivity portion of the NRF formula.
9. The sharing mechanism is an important means by which we can allow ratepayers at least an opportunity to gain some tangible benefits from NRF regulation.
10. The record does not show that the sharing mechanism has had an adverse effect on RTC's innovation and new investment.
11. Sharing only affects services for which competition is either weak or nonexistent and does not put RTC at a competitive disadvantage.
12. Elimination of depreciation reviews will foreclose any potential franchise impact claims covering investments and depreciation from the day the elimination is effective, forward.
13. The parties agree that depreciation reviews should be eliminated.
14. The parties agree that the suspension of the I-X portion of the price adjustment formula should continue.

15. Elimination of Z-factor adjustments is consistent with suspension of sharing and simplifies the regulatory process.

16. The [*112] parties agree that new Z-factor adjustments should be eliminated and an LE factor mechanism should be adopted.

17. RTC has never filed for a Z-factor adjustment for PBOP.

18. RTC's PBOP trust is well funded.

19. RTC has not put all of the PBOP revenues for 1997, 1998 and 1999 in the PBOP trusts. The excess revenues were invested.

20. D.96-12-074 trued up RTC's PBOP costs prior to 1997.

21. The NRF PBOP requirements in D.92-12-015 apply to RTC.

22. Decreases in RTC's PBOP revenue requirements should have been addressed in Z-factor filings.

23. ORA and RTC agree to the amended monitoring requirements listed in Attachment A.

24. ORA and RTC agree to the withdrawal of RTC's request to modify the pricing flexibility rules.

25. The Commission approved RTC's Advice Letter 423 in Resolution T-16276 and imposed an imputation requirement.

26. RTC's service quality is in compliance with G.O. 133-B.

Conclusions of Law

1. RTC should amend its 1999 sharable earnings filing to reflect the adjustments adopted in VI. C, D and E.

2. RTC's sharing mechanism should be retained until further order of this Commission.

3. RTC's sharable earnings filings for future years, beginning with earnings for the [*113] year 2000, should reflect the adjustments in VI. C and D based on recorded data for the applicable year.

4. RTC should amend its accounting practices to reflect the adjustments in VI. C and D herein.

5. RTC should amend its 1999 sharable earnings filing to add \$ 419,505 to its 1999 sharable earnings that should have been shared for 1998.

6. RTC should correct its affiliate transaction accounting practices to reflect the adjustments adopted herein.

7. Depreciation reviews should be eliminated.

8. The suspension of the I-X portion of the NRF price adjustment formula should be continued.

9. New Z-factor adjustments should be eliminated.

10. Z-factor adjustments currently before the Commission should be considered.

11. Z-factors now being implemented should finish implementation.

12. LE factor recovery of non-regulated operations audit costs should be allowed.

13. An LE factor mechanism as established in D.98-10-026 should be established for RTC.

14. RTC's annual revenue requirement should be reduced by \$ 98,600 for PBOP.

15. RTC should return to ratepayers the PBOP revenues that were not placed in the PBOP trust plus the earnings on the investment of these funds by RTC. Once the revenues [*114] have been returned to ratepayers and the \$ 98,600 annual PBOP revenue requirement has been eliminated, the Z-factor adjustment should cease.

16. The amended monitoring requirements specified in Attachment A should be adopted.

17. Imputation as specified in Resolution T-16276 is beyond the scope of this proceeding.

18. ORA should be allowed additional time to review RTC's amended 1999 shareable earnings filing.

19. In order to implement the changes to RTC's NRF as soon as possible, this order should be effective immediately.

ORDER

IT IS ORDERED that:

1. Application 99-03-025 is approved only to the extent indicated below. In all other respects, it is denied.
2. Roseville Telephone Company (RTC) shall, within 90 days of the effective date of this decision, amend its 1999 sharable earnings filing to reflect the adjustments adopted in VI. C, D and E and to include \$ 419,505 plus interest, that should have been shared in 1998.
3. In preparing its amended 1999 shareable earnings filing, RTC may utilize 1999 full year recorded data for Audit Calculation 32.
4. The amended 1999 shareable earnings filing shall include interest calculated in accordance with Ordering Paragraph 16 of [*115] Decision 89-10-031.
5. RTC shall provide the Office of Ratepayer Advocates with an advance copy of its amended 1999 shareable earnings filing, including complete workpapers, 30 days before it is filed.
6. RTC's sharable earnings filings for future years, beginning with earnings for the year 2000 shall reflect the adjustments adopted in VI.C and D based on recorded data for the applicable year.
7. RTC shall amend its accounting practices to reflect the adjustments adopted in VI. C and D.
8. RTC's sharing mechanism shall continue in effect until further order of this Commission.
9. Depreciation reviews are eliminated.
10. The I-X portion of the price adjustment formula is suspended.
11. Z-factor adjustments are eliminated except as specified below.
12. Z-factors now being implemented shall be allowed to finish implementation.
13. An LE factor mechanism as established in D.98-10-026 is established for RTC.
14. Within 60 days, RTC shall file an advice letter to refund post retirement benefits other than pensions (PBOP) revenues not placed in the PBOP trust during 2000, as well as the proceeds from the investment of these funds, and to reduce its 2001 annual revenue requirement by \$ 98,600 [*116] as a surcredit. The \$ 98,600 annual revenue requirement reduction is permanent.
15. Within 60 days RTC shall file an advice letter to make a Z-factor adjustment to return to ratepayers PBOP revenues for 1997 through 1999 that were not placed in the PBOP trust, as well as the proceeds from the investment of these funds.
16. The amended monitoring requirements specified in Attachment A are adopted.
17. This proceeding is closed.

This order is effective today.

Dated June 28, 2001, at San Francisco, California.

I will file a dissent.

/s/ HENRY M. DUQUE

Commissioner

I will file a concurrence.

/s/ RICHARD A. BILAS

Commissioner

CONCURBY: RICHARD A. BILAS, Commissioner

Commissioner Bilas, concurring:

At today's Commission meeting, I voted in favor of both the Proposed Decision and President Lynch's Alternate. The Alternate, which was successful, differed in one main aspect from the Proposed Decision--namely the continuation of the sharing mechanism. Both the Proposed Decision and the Alternate eliminate depreciation reviews, eliminate most Z-factor adjustments, establish a Limited Exogenous factor, and modify the required monitoring reports. I fully support all of these changes.

On the [*117] issue of the sharing mechanism, I stated that the decision to discontinue sharing is more art than science. In my opinion, this is the right time to end sharing, but admittedly this is a close call for me. The most disconcerting fact for me is that the next time the issue of the sharing mechanism will be raised is in the next New Regulatory Framework (NRF) review. This review will not take place for three years. By then, I do not think the question to discontinue sharing will still be more art than science. At that future point in time, Roseville will most certainly be overdue in being relieved of the requirement to maintain the sharing mechanism.

Considered as an entire package, I support today's decision. However, I am troubled by our continued imposition of the sharing mechanism--especially because we as a Commission are unlikely to look at this issue for at least three years.

San Francisco, California
June 28, 2001

DISSENTBY: Henry M. Duque, Commissioner

Commissioner Henry M. Duque, dissenting:

The key issue here is whether sharing should be suspended or kept for Roseville. The Commission suspended sharing of earnings for Verizon in 1993 before we had any measurable competition. For [*118] Pacific Bell, it was suspended in 1995 when competition was at its infancy. Six years later, Roseville faces real and present competition in its area. XO Communication, ELI, Pacific Bell, PacWest and others are deploying networks and have started to provide competing services. Roseville has reportedly lost about 10% of its customers to its competitors, which is greater than that lost by others when we suspended sharing for them.

Roseville's competitors, including Pacific, are facilities-based carriers that are not subject to the sharing of earnings. This is an important issue for Roseville and its customers because retained earnings are a key source of investment. Roseville's competitors, at their management's discretion, can invest their entire earnings into plant to expand their services and provide high capacity and other advanced services in competition with Roseville. Should not Roseville have the same ability to access similar capital as its competitors? By keeping the share of earnings, the effect is that Roseville's source of capital will be reduced by one half and thus its ability to effectively compete will be diminished.

The use of retained earnings is all the more important [*119] in the case of Roseville because the company has a track record that shows low debt and high equity capital. Suspension of sharing would allow this company to continue to finance growth and service expansion at low cost.

I understand that often we find ourselves at the borderline of changing market conditions and past regulatory regimes. There is a great uncertainty. In this decision, we are trying to unshackle Roseville from the command and control regulatory procedures such as those described by both decisions: depreciation review, periodic rate adjustment, and others. The implicit purpose of eliminating these methods is to facilitate Roseville's participation in a competitive market. By keeping sharing while taking the other proper actions, we are showing that it is extremely difficult for us to let go. Suspending sharing is a necessary component in opening in opening the market for competition.

Moreover, keeping the sharing of earnings in today's market conditions is inequitable, anticompetitive, and unproductive. Customers are far better off with the conveniences of choice, advanced services and real competition than from some nickels and dimes that may come to them at the cost [*120] of foregoing capital investment.

June 28, 2001

San Francisco, California

Legal Topics:

For related research and practice materials, see the following legal topics:

Communications LawTelephone ServicesPayphone ServicesCommunications LawTelephone ServicesWireless ServicesEnergy & Utilities LawUtility CompaniesGeneral Overview

ATTACHMENT A

ROSEVILLE TELEPHONE COMPANY

NRF Monitoring Reports

#	NRF MONITOR- ING REPORT CODE	REPORT NAME	FREQUENCY	REPORT DESCRIPTION
1	R.A.01-00	G.O. 152, Private Line Alarm	Quarterly	Uniform standards for the installation, maintenance, and operation of private line alarm service provided by telephone utilities.
2	R.A.01-01	G.O. 133-C Telephone Service Levels	Quarterly	Uniform standards for the installation, maintenance, and quality of telephone service.
3	R.A.02-00	Report on Informal Service Complaints (Proprietary)	Quarterly	Identifies the number of informal customer complaints by category of complaint.
4	R.A.02-01	Quality Improvement and Cost Reduction Programs (Proprietary)	Upon Request	Identifies all significant capital and/or expense planned to be incurred in quality improvement and cost reduction programs that RTC intends to begin in the following year.
5	R.A.02-02	Notification of Major Service Interruption	Per Occurrence	Measures customer and network impacts of service interruptions, and details the cause of the failure and restoration of service.
6	R.A.02-03	Summary of Major Service Interruption	Monthly	Summarizes instances of service interruptions shown

#	NRF MONITOR- ING REPORT CODE	REPORT NAME	FREQUENCY	REPORT DESCRIPTION
				in the Major Service Interruptions Report.
7	R.A.02-04	G.O. 95 Underground Conversions	Upon Request	Provides information on the underground conversion of existing facilities.
8	R.A.02-05	Quality of Service Performance Report (Proprietary)	Quarterly	Measures service quality based on customer opinions. Used to monitor service quality.
9	R.A.04-00	Detailed Schedule of Access Lines (Proprietary)	Quarterly	Provides a detailed schedule of residential, business and other switched access lines.
10	R.A.05-00	Summary of Category II Rate Changes	Annually	Reflects the changes in rates for Category II services.
11	R.A.XX-00	G.O. 95, Accident & Line Statistics	Annually	Provides information on facility related accidents and line statistics.
12	R.A.XX-01	Customer Information Notices	Quarterly	Bill inserts sent to customers, pursuant to legislative and CPUC orders.
13	R.A.XX-02	Emergency Spanish Language Assistance Bureau (ESLAB)	Annually	Details the requirements for bilingual services to be provided by telephone utilities in the State of California.
14	R.A.XX-03	Non-English Speaking Percentage by Exchange	Annually	Identifies serving areas/exchanges where non-English speaking minorities comprise 5% or more of the population.
15	R.A.XX-04	G.O. 107-B, Practice Used to Assure Privacy & Secrecy	As Issued	Contains notification of any changes in the company's internal employee practice regarding the privacy of and/or secrecy of communications.
16	R.A.XX-05	G.O. 107-B, Telephone	Annual	Contains information on

#	NRF MONITOR- ING REPORT CODE	REPORT NAME	FREQUENCY	REPORT DESCRIPTION
		Tap Devices Discovered (Proprietary)		instances where a wire tap device is reported, found or believed to be installed.
17	R.A.XX-06	G.O. 95, Infraction Cleared	Monthly	Details information regarding an infraction and the date of clearance.
18	R.A.XX-07	Universal Lifeline Telephone Service (ULTS)	Quarterly	Financial statement for the ULTS fund, and includes the number of ULTS users.
19	R.B.01-00	Expense Matrix (Proprietary)	Quarterly	Provides the types of costs incurred, costs and hours per workload indicator and employee force count data on a functional basis.
20	R.C.01-00	1 Year Capital Budget Summary & Network Planning Report (Proprietary)	Annually	Information on capital costs associated w/assets, growth, replacement, drivers, projects, products & services. (Includes previous reports R.C.XX-00, R.C.XX-01, R.C.XX-02 & R.F.03-00)
21	R.D.01-00	Monthly Operations Report (Proprietary)	Monthly	Provides company financial data such as; income statement, balance sheet, and analysis of operating expenses and revenues.
22	R.D.04-00	Separated Results of Operations (101 Report) (Proprietary)	Monthly	Provides information on RTC's operations in the state and interstate jurisdictions. Separated operating revenue, expense, rate of return and rate base information is included in this report.
23	R.D.07-00	Service Specific Revenue and Cost Data for Categories I, II & III, Including New Services. (Proprietary)	Quarterly	Contains income statement information for NRF categories I, II & III, and new services, including cost data when available. (Includes previous reports R.F.01-00 & R.F.01-NS00).

#	NRF MONITOR- ING REPORT CODE	REPORT NAME	FREQUENCY	REPORT DESCRIPTION
24	R.D.XX-00	G.O. 104-A, Report to FCC, Form M	Annually	An annual report that contains balance sheet, income statement and operational data.
25	R.D.XX-01	Annual Report to Shareholders (SEC 10K)	Annually	Contains income statement information, balance sheet information, and operational data.
26	R.D.XX-02	Quarterly Report to Shareholders (SEC 10Q)	Quarterly	Contains income statement information, balance sheet information, and operational data.
27	R.D.XX-03	Interest During Construction (IDC)	Annually	Report shows mechanics of using quarterly indices to derive a monthly IDC rate to book amount of IDC each month.
28	R.D.XX-04	G.O. 77-K, Membership Dues, Contributions & Donations (Proprietary)	Annually	Contains data on membership dues, contributions, donations and salaries over \$ 60,000.
29	R.D.XX-06	G.O. 96-A Tariff Contracts & Deviations	Annually	Provides information for those contracts and services rendered at rates or under conditions other than provided in RTC's filed tariff schedules.
30	R.D.XX-07	Weighted Average Cost of Capital	Annually	Provides financial data used to calculate the weighted average cost of capital for a rolling 12 month period.
31	R.D.XX-08	DEAF Trust	Quarterly	Lists agencies that request TDD's, agencies that are supplied TDD's and provides an explanation when requests are denied.
32	R.E.01-00	Central Office Equipment Deployment & Utilization Forecasts	Annually	Provides annual forecasted switching data by switching technology.

#	NRF MONITOR- ING REPORT CODE	REPORT NAME	FREQUENCY	REPORT DESCRIPTION
		(Proprietary)		
33	R.E.01-01	Interoffice Facilities Deployment & Utilization (Proprietary)	Annually	Provides annual utilization forecasts for interoffice facilities by geographic area, by technology, by channels, by capacity working and by percent utilization.
34	R.E.01-02	Outside Plant Deployment & Utilization Forecasts (Proprietary)	Annually	Provides annual forecasts for outside plant by technology and geographic operating areas.
35	R.F.06-00	Affiliate Company Transactions & Intercompany Activities	Per Occurrence	Provides information on the sale or transfer of RTC assets to affiliates, transfer of employees to affiliates and organizational changes.
36	R.F.08-00	Notification of Diversification Activities (Proprietary)	Per Occurrence	Designed to provide timely notification of RTC's intentions to diversify its business activities.
37	R.F.09-00	Complaints From Competitors (Proprietary)	Per Occurrence	To provide information regarding informal complaints made by competitors.
38	R.F.XX-00	Service Specific Tariff Imputation Report (Proprietary)	Annually	Track the tariff rates of monopoly services bundled with competitive services under one Category II rate and compare that sum to the floor price of the bundled service.
39	R.X.XX-00	Results of Operations (bound) Annual Form M	Annually	Provides a comprehensive view of RTC's operations. Contains financial and operational information and statistics, and summaries of major Commission decisions impacting RTC.
40	R.X.XX-01	Shareable Earnings	Annually	Shows the sharing (if any) of revenues that RTC has

2001 Cal. PUC LEXIS 604, *

#	NRF MONITOR- ING REPORT CODE	REPORT NAME	FREQUENCY	REPORT DESCRIPTION

earned in the previous
year.

[*121]

Supplemental TAWC-2-14

Florida Administrative Code

25-30.115 Uniform System of Accounts for Water and Wastewater Utilities.

Water and wastewater utilities shall, effective January 1, 1998, maintain their accounts and records in conformity with the 1996 NARUC Uniform Systems of Accounts adopted by the National Association of Regulatory Utility Commissioners. All inquiries related to the interpretation of these uniform systems of accounts shall be submitted to the Commission's Division of Economic Regulation in writing. Note: The National Association of Regulatory Utility Commissioners published separate uniform systems of accounts for three classes of water and wastewater utilities: Class A (defined as those having annual water or wastewater operating revenues of \$1,000,000 or more); Class B (defined as those having annual water or wastewater operating revenues of \$200,000 or more but less than \$1,000,000); Class C (defined as those having annual water or wastewater revenues of less than \$200,000). Copies of these systems of accounts may be purchased from the office of said Association, Post Office Box 684, Washington, D.C. 20044.

Specific Authority 367.121(1)(b), (f) FS. Law Implemented 367.121(1)(b) FS. History—Amended 2-3-70, 9-12-74, 1-2-79, 8-21-79, 9-25-85, Formerly 25-10.04, 25-10.004, Amended 8-17-96.



1 of 3 DOCUMENTS

CODE OF LAWS OF SOUTH CAROLINA ANNOTATED
Copyright (c) 2009, The State of South Carolina

*** THIS DOCUMENT IS CURRENT THROUGH STATE REGISTER ***
*** VOLUME 33, ISSUE NO. 9, EFFECTIVE SEPTEMBER 25, 2009 ***

CODE OF REGULATIONS
CHAPTER 103. PUBLIC SERVICE COMMISSION
ARTICLE 7. WATER UTILITIES
SUBARTICLE 2. RECORDS AND REPORTS

S.C. Code Regs. 103-719 (2009)

103-719. Accounting Procedures.

All books and records of the utility shall be maintained in accordance with the NARUC Uniform System of Accounts for Class A, B and C Water Utilities to the extent applicable, and such records must be made available for examination by the ORS or its authorized representatives at all reasonable hours. Full cooperation will be provided by the utility during rate adjustment audits or compliance audits conducted by the ORS or its representatives.

HISTORY: Amended by State Register Volume 10, Issue No. 6, eff June 27, 1986; State Register Volume 31, Issue No. 5, eff May 25, 2007.

NOTES:

Effect of Amendment

The 1986 amendment added "to the extent possible" following "Water Utilities" in first sentence.

The 2007 amendment substituted "ORS" for "Commission" in two locations. Editor's Note

**CLASS A & B
WATER UTILITY
ANNUAL REPORT**

OF THE

NAME _____

(Here show in full the exact corporate, firm or individual name of the respondent)

LOCATED AT _____

(Here give the location, including street and number of the respondent's main business office within the State)

COMPANY # _____

(Here give the APSC-assigned company number)

TO THE

ARKANSAS PUBLIC SERVICE COMMISSION



COVERING ALL OPERATIONS

FOR THE YEAR ENDING DECEMBER 31, 2____

REPORT TO ARKANSAS PUBLIC SERVICE COMMISSION

LETTER OF TRANSMITTAL

To: Arkansas Public Service Commission
Post Office Box 400
Little Rock, Arkansas 72203-0400

Submitted herewith is the annual report covering the operation of _____
(Company)
of _____ for the year ending December 31, 2_____. This report is submitted in
(Location)
accordance with Section 51 of Act 324 of the 1935 Acts of Arkansas.
The following report has been carefully examined by me, and I have executed the verification given below.

(Signature)

(Title)

.....
VERIFICATION

STATE OF)
) **ss.**
COUNTY OF)

I, the undersigned, _____ of the
(Name and Title)
(Company)

been prepared under my direction from the original books, papers, and records of said utility: that I have carefully examined the same, and declare the same a complete and correct statement of the business and affairs of said utility in respect to each and every matter and thing set forth, to the best of my knowledge, information, and belief; and I further say that no deductions were made before stating the gross revenues, and that accounts and figures contained in the foregoing statements embrace all of the financial transactions for the period in this report.

(Signature)

Subscribed and sworn to before me this _____
day of _____
My Commission Expires _____

(Signature of Notary)

GENERAL INSTRUCTIONS, DEFINITIONS, ETC.

1. Two (2) copies of this report, properly filled out and verified shall be filed with the Utility Division of the Arkansas Public Service Commission, Little Rock, Arkansas, on or before the 31st day of March following the close of the calendar year for which the report is made.
2. This form of annual report is prepared in conformity with the Uniform System of Accounts for Public Utilities prescribed by the Public Service Commission and all accounting words and phrases are to be interpreted in accordance with the said classification.
3. The word "respondent" in the following inquiries means the person, firm, association or company in whose behalf the report is made.
4. Instructions should be carefully observed, and each question should be answered fully and accurately. Where the word "none" truly and completely states the fact, it should be given to any particular inquiry.
5. If any schedule does not apply to the respondent, such fact should be shown on the schedule by the words "not applicable."
6. Except in cases where they are especially authorized, cancellations, arbitrary check marks, and the like must not be used either as partial or entire answers to inquiries.
7. Reports should be made out by means which result in a permanent record. The copy in all cases shall be made out in permanent black ink or with permanent black typewriter ribbon. Entries of a contrary or opposite character (such as decreases reported in a column providing for both increases and decreases) should be shown in red ink or enclosed in parentheses.
8. This report will be scanned in. Please bind with clips only.
9. Answers to inquiries contained in the following forms must be complete. No answer will be accepted as satisfactory which attempts by reference to any paper, document, or return of previous years or other reports, other than the present report, to make the paper or document or portion thereof thus referred to a part of the answer without setting it out. Each report must be complete within itself.
10. In cases where the schedules provided in this report do not contain sufficient space or the information called for, or if it is otherwise necessary or desirable, additional statements or schedules may be inserted for the purpose of further explanation of accounts or schedules. They should be legibly made on paper of durable quality and should conform with this form in size of page and width of margin. This also applies to all special or unusual entries not provided for in this form. Where information called for herein is not given, state fully the reason for its omission.
11. Each respondent is required to send in connection with its report to this Commission's Utilities Division, one (1) copy of its latest annual report to stockholders.
12. Schedules supporting the revenue accounts and furnishing statistics should be so arranged as to effect a division in the operations as to those inside and outside the state.
13. Answers to all inquiries may be in even dollar figures, with cents omitted and with agreeing totals.
14. Each respondent should make its report in duplicate, retaining one copy for its files for reference, in case correspondence with regard to such report becomes necessary. For this reason, several copies of the accompanying forms are sent to each utility company concerned.

REPORT TO ARKANSAS PUBLIC SERVICE COMMISSION

Give the name, title, office address, telephone number and e-mail address of the person to whom any correspondence concerning this report should be addressed:

Name _____ **Title** _____

Address _____

Telephone Number _____

E-Mail _____

Give the name, address, telephone number and e-mail address of the resident agent:

Name _____ **Telephone Number** _____

Address _____

E-Mail _____

IDENTITY OF RESPONDENT

1. Give the exact name by which respondent was known in law at the close of the year. Use the initial word "The" only when it is part of the name:
2. Give the location (including street and number) of (a) the main Arkansas business office of respondent at the close of the year, and (b) if respondent is a foreign corporation, the main business office if not in this state:

(a) _____ (b) _____
3. Indicate by an x in the proper space (a) the type of service rendered, and (b) the type of organization under which respondent was operating at the end of the year.

(a) ☐ Electric, ☐ Gas, ☐ Water, ☐ Telephone, ☐ Other

(b) ☐ Proprietorship, ☐ Partnership, ☐ Joint Stock Association,
☐ Corporation, ☐ Other (describe below): _____
4. If respondent is not a corporation, give (a) date of organization, and (b) name of the proprietor or the names of all partners, and the extent of their respective interest at the close of the year.

(a) _____

(b) _____
5. If a corporation, indicate (a) in which state respondent is incorporated, (b) date of incorporation, and (c) designation of the general law under which respondent was incorporated, or, if under special charter, the date of passage of the act:

(a) _____

(b) _____

(c) _____
6. State whether or not respondent during the year conducted any part of its business within the State of Arkansas under a name or names other than that shown in response to inquiry No. 1 above, and, if so, give full particulars:

7. State whether respondent is a consolidated or merged company. If so, (a) give date and authority for each consolidation or merger, (b) name all constituent and merged companies, and (c) give like particulars as required of the respondent in inquiry No. 5 above:

(a)

(b)

(c)

8. State whether respondent is a reorganized company. If so, give (a) name of original corporation, (b) date of reorganization, (c) reference to the laws under which it was reorganized and (d) state the occasion of the reorganization, whether because of foreclosure of mortgage or otherwise, giving full particulars.

(a)

(b)

(c)

(d)

9. Was respondent subject to a receivership or other trust at any time during the year? _____

If so, state:

(a) Name of receiver or trustee: _____

(b) Name of beneficiary or beneficiaries for whom trust was maintained:

(c) Purpose of the trust: _____

(d) Give (1) date of creation of receivership or other trust, and (2) date of acquisition of respondent: (1) _____ (2) _____

10. Did the respondent act in any of the capacities listed in Paragraph (a) below during the past year? _____ If so,

(a) Indicate the applicable one by an **X** in the proper space:

() Guarantor, () Surety, () Principal--obligor to a surety contract,
() Principal--obligor to a guaranty contract.

(b) Insert a statement showing the character, extent, and terms of the primary agreement or obligation, including (1) names of all parties involved, (2) extent of liability of respondent, whether contingent or actual, (3) extent of liabilities of the other parties, whether contingent or actual, and (4) security taken or offered by respondent.

DIRECTORS AND COMPENSATION

Give the name and office addresses of all directors at the close of the year, dates of beginning and expiration of terms, and total compensation (including payments and cost of other benefits, such as health insurance, etc. and excluding any reimbursements for business travel). Chairman (*) and Secretary (**) marked by asterisks.

Item No.	Name of Director	Office Address	Date of Term		Compensation
			Beginning	End	

PRINCIPAL OFFICERS AND KEY MANAGEMENT PERSONNEL

Give the title of the principal officers, managers and key personnel, the names and office addresses of persons holding such positions at the close of the year, and the annual salary of each.

Item No.	Title	Name of person holding office at close of year	Office Address	Annual Salary
	TOTAL			\$ -

[illegible]

Item No.	Name of Stockholder	Address	No. of Shares Held	No. of Voting Shares	Other Vote Empowered Securities
	Total listed above				
	Total all stockholder				

VOTING POWERS AND ELECTIONS (Cont'd)

5. State the total number of votes represented and voted at the last general meeting for the election of directors of the respondent:

6. Give the date and place of such meeting:

7. Give the names of each of the persons who cast the five highest number of votes. Give also the number of votes cast in his own behalf and the number of votes cast by proxy:

Item No.	Name of Voter	Total	On account of shares held	As proxy for others	Remarks

REMARKS

(This space may be used for remarks on inquiries on any of the preceding pages)

COMPARATIVE BALANCE SHEET - WATER

Account Number	Assets and Other Debits	Ref. Page	Previous Year 20__	Current Year 20__
I. Utility Plant				
101	Utility Plant in Service	W-5	\$ -	\$ -
102	Utility Plant Leased to Others	W-5	-	-
103	Property Held for Future Use	W-5	-	-
104	Utility Plant Purchased or Sold	W-5	-	-
105	Construction Work in Progress	W-5	-	-
106	Completed Construction Not Classified	W-5	-	-
108	Accumulated Depreciation			
108.1	Accum. Depr. of Utility Plant in Service	W-9	-	-
108.2	Accum. Depr. of Utility Plant Leased to Others			
108.3	Accum. Depr. of Property Held for Future Use			
110	Accumulated Amortization			
110.1	Accum. Amort. of Utility Plant in Service			
110.2	Accum. Amort. of Utility Plant Leased to Others			
114	Utility Plant Acquisition Adjustments	W-5	-	-
115	Accumulated Amortization of Utility Plant Acquisition Adjs	W-17	-	-
116	Other Utility Plant Adjustments	W-5	-	-
	Total Net Utility Plant		\$ -	\$ -
II. Other Property and Investments				
121	Nonutility Property	W-10		\$ -
122	Accumulated Deprec & Amortization of Nonutility Property	W-10		
123	Investment in Associated Companies	W-10		-
124	Utility Investments	W-10		-
125	Other Investments	W-10		
126	Sinking Funds	W-10		
127	Other Special Funds	W-10		
	Total Other Property and Investments		\$ -	\$ -
III. Current and Accrued Assets				
131	Cash			
131.1	Cash on Hand			
131.2	Cash in Bank			
132	Special Deposits			
133	Other Special Deposits			
134	Working Funds			
135	Temporary Cash Investments			
141	Customer Accounts Receivable			
142	Other Accounts Receivable			
143	Accum Prov for Uncollectible Accts			
144	Notes Receivable			
145	Accts Receivable from Associated Companies			
146	Notes Receivable from Associated Companies			
151	Plant Material & Supplies			
152	Merchandise			
153	Other Materials & Supplies			
161	Stores Expense			
162	Prepayments			
171	Accrued Interest and Dividends Receivable			
172	Rents Receivable			
173	Accrued Utility Revenues			
174	Miscellaneous Current & Accrued Assets			
	Total Current and Accrued Assets		\$ -	\$ -

COMPARATIVE BALANCE SHEET - WATER

Account Number	Assets and Other Debits (Cont'd)	Ref. Page	Previous Year 20__	Current Year 20__
	IV. Deferred Debits			
181	Unamortized Debt Discount and Expense	W-11		\$ -
182	Extraordinary Property Losses			
183	Preliminary Survey & Investigation Charges			
184	Clearing Accounts			
185	Temporary Facilities			
186	Miscellaneous Deferred Debits			
186.1	Deferred Rate Case Expense			
186.2	Other Deferred Debits	W-11		-
187	Research & Development Expenditures			
190	Accumulated Deferred Income Taxes			
190.1	Federal			
190.2	State			
190.3	Local			
	Total Deferred Debits		\$ -	\$ -
	Total Assets and Other Debits		\$ -	\$ -

COMPARATIVE BALANCE SHEET - WATER

Account Number	Liabilities and Other Credits	Ref. Page	Previous Year 20__	Current Year 20__
V. Equity Capital				
201	Common Stock Issued	W-12		-
202	Common Stock Subscribed			
203	Common Stock Liability for Conversion			
204	Preferred Stock Issued			
205	Preferred Stock Subscribed			
206	Preferred Stock Liability for Conversion			
207	Premium on Capital Stock	W-12	-	-
209	Reduction in Par or Stated Value of Capital Stock			
210	Gain on Resale or Cancellation of Reacquired Capital Stock			
211	Other Paid-In Capital			
212	Discount on Capital Stock			
213	Capital Stock Expense			
214	Appropriated Retained Earnings			
215	Unappropriated Retained Earnings	W-19	-	-
216	Reacquired Capital Stock	W-12		-
218	Proprietary Capital (for proprietorships and partnerships only)			
	Total Equity Capital		\$ -	\$ -
VI. Long-Term Debt				
221	Bonds	W-13		
222	Reacquired Bonds	W-13		
223	Advances from Associated Companies	W-13		
224	Other Long-Term Debt	W-13		
	Total Other Property and Investments		\$ -	\$ -
VII. Current and Accrued Liabilities				
231	Accounts Payable			
232	Notes Payable	W-13		-
233	Accounts Payable to Associated Companies			
234	Notes Payable to Associated Companies	W-13		-
235	Customer Deposits	W-15	-	-
236	Accrued Taxes			
236.1	Utility Operating Income	W-14		
236.11	Taxes Other Than Income	W-14		
236.12	Income Taxes	W-14		
236.2	Other Income and Deductions			
237	Accrued Interest			
237.1	Interest Accrued on Long-Term Debt			
237.2	Interest Accrued on Other Liabilities	W-14	-	-
238	Accrued Dividends			
239	Matured Long-Term Debt			
240	Matured Interest			
241	Miscellaneous Current and Accrued Liabilities			
	Total Current and Accrued Liabilities		\$ -	\$ -

COMPARATIVE BALANCE SHEET - WATER

Account Number	Liabilities and Other Credits (Cont'd)	Ref. Page	Previous Year 20__	Current Year 20__
	VIII. Deferred Credits			
251	Unamortized Premium on Debt			
252	Advances for Construction	W-15	-	-
253	Other Deferred Credits	W-14	-	-
255	Accumulated Deferred Investment Tax Credits	W-16	-	-
255.1	Utility Operations			
255.2	Non-Utility Operations			
	Total Deferred Credits		\$ -	\$ -
	IX. Operating Reserves			
261	Property Insurance Reserve			
262	Injuries and Damages Reserve			
263	Pensions and Benefits Reserve			
265	Miscellaneous Operating Reserves			
	Total Operating Reserves		\$ -	\$ -
	X. Contributions in Aid of Construction			
271	Contributions in Aid of Construction	W-15	\$ -	\$ -
272	Acc. Amort. Of Contributions in Aid of Construction			
	Total Contributions in Aid of Construction		\$ -	\$ -
	XI. Accumulated Deferred Income Taxes			
281	Acc Def Income Taxes - Accelerated Amortization	W-16		
282	Accumulated Deferred Income Taxes - Liberalized Depr.	W-16		
283	Accumulated Deferred Income Taxes - Other	W-16		
	Total Accumulated Deferred Income Taxes		-	-
	Total Liabilities and Other Credits		-	-

Line No.	Acct. No.	UTILITY PLANT - SYSTEM	Ref. Page	Beginning Balance	Additions	Retirements	Adjustments	Balance at End of Year
1	101	Utility Plant in Service	W-1					\$ -
2	102	Utility Plant Leased to Others	W-1					-
3	103	Utility Plant Held for Future Use	W-1					-
4	104	Utility Plant Purchased or Sold	W-1					-
5	105	Construction Work in Progress	W-1					-
6	106	Completed Construction not Classified	W-1					-
7	114	Utility Plant Acquisition Adjustments	W-1					-
8		Sub-Total		\$ -	\$ -	\$ -	\$ -	\$ -
9	116	Other Utility Plant Adjustments	W-1					\$ -
10		TOTAL		\$ -	\$ -	\$ -	\$ -	\$ -
Line No.	Acct. No.	UTILITY PLANT - ARKANSAS		Beginning Balance	Additions	Retirements	Adjustments	Balance at End of Year
1	101	Utility Plant in Service	W-1					\$ -
2	102	Utility Plant Leased to Others	W-1					-
3	103	Utility Plant Held for Future Use	W-1					-
4	104	Utility Plant Purchased or Sold	W-1					-
5	105	Construction Work in Progress	W-1					-
6	106	Completed Construction not Classified	W-1					-
7	114	Utility Plant Acquisition Adjustments	W-1					-
11		Sub-Total		\$ -	\$ -	\$ -	\$ -	\$ -
12	116	Other Utility Plant Adjustments	W-1					\$ -
15		TOTAL		\$ -	\$ -	\$ -	\$ -	\$ -

WATER PLANT IN SERVICE							
Acct. No.	Account	Ref. Page	Balance at Beginning of Year	Additions	Retirements	Adjustments	Balance at End of Year
301.1	I. INTANGIBLE PLANT						
302.1	Organization						\$
339.1	Franchises						-
	Other Plant & Miscellaneous Equipment						-
	Total Intangible Plant		\$ -	\$ -	\$ -	\$ -	\$ -
303.2	II. SOURCE OF SUPPLY						
304.2	& PUMPING PLANT						\$
305.2	Land and Land Rights						-
306.2	Structures and Improvements						-
307.2	Collecting and Impounding Reservoirs						-
308.2	Lake, River and Other Intakes						-
309.2	Wells and Springs						-
310.2	Infiltration Galleries and Tunnels						-
311.2	Supply Mains						-
339.2	Power Generation Equipment						-
	Pumping Equipment						-
	Other Plant & Miscellaneous Equipment						-
	Total Supply & Pumping Plant		\$ -	\$ -	\$ -	\$ -	\$ -
303.3	III. WATER TREATMENT PLANT						
304.3	Land and Land Rights						\$
320.3	Structures and Improvements						-
339.3	Water Treatment Equipment						-
	Other Plant & Miscellaneous Equipment						-
	Total Water Treatment Plant		\$ -	\$ -	\$ -	\$ -	\$ -
303.4	IV. TRANSMISSION AND DISTRIBUTION						
304.4	Land and Land Rights						\$
330.4	Structures and Improvements						-
331.4	Distribution Reservoirs & Standpipes						-
333.4	Transmission and Distribution Mains						-
334.4	Services						-
335.4	Meters and Meter Installations						-
339.4	Hydrants						-
	Other Plant & Miscellaneous Equipment						-
	Total Intangible Plant		\$ -	\$ -	\$ -	\$ -	\$ -

WATER PLANT IN SERVICE						
Acct. No.	Account	Ref. Page	Balance at Beginning of Year	Additions	Retirements	Adjustments
	VI. GENERAL PLANT					
303.5	Land and Land Rights					-
304.5	Structures & Improvements					-
340.5	Office Furniture & Equipment					-
341.5	Transportation Equipment					-
342.5	Stores Equipment					-
343.5	Tools, Shop & Garage Equipment					-
344.5	Laboratory Equipment					-
345.5	Power Operated Equipment					-
346.5	Communication Equipment					-
347.5	Miscellaneous Equipment					-
348.5	Other Tangible Property					-
	Total General Plant		\$ -	\$ -	\$ -	\$ -
	TOTAL WATER PLANT IN SERVICE	W-1 W-5	\$ -	\$ -	\$ -	\$ -

ACCUMULATED DEPRECIATION - PLANT IN SERVICE							
Acct. No.	Account	Ref. Page	Balance at Beginning of Year	Additions	Retirements	Adjustments	Balance at End of Year
301.1	I. INTANGIBLE PLANT						
302.1	Organization						\$
339.1	Franchises						-
	Other Plant & Miscellaneous Equipment						-
	Total Intangible Plant		\$ -	\$ -	\$ -	\$ -	\$ -
303.2	II. SOURCE OF SUPPLY & PUMPING PLANT						
304.2	Land and Land Rights						\$
305.2	Structures and Improvements						-
306.2	Collecting and Impounding Reservoirs						-
307.2	Lake, River and Other Intakes						-
308.2	Wells and Springs						-
309.2	Infiltration Galleries and Tunnels						-
310.2	Supply Mains						-
311.2	Power Generation Equipment						-
339.2	Pumping Equipment						-
	Other Plant & Miscellaneous Equipment						-
	Total Supply & Pumping Plant		\$ -	\$ -	\$ -	\$ -	\$ -
303.3	III. WATER TREATMENT PLANT						
304.3	Land and Land Rights						\$
320.3	Structures and Improvements						-
339.3	Water Treatment Equipment						-
	Other Plant & Miscellaneous Equipment						-
	Total Water Treatment Plant		\$ -	\$ -	\$ -	\$ -	\$ -
303.4	IV. TRANSMISSION AND DISTRIBUTION						
304.4	Land and Land Rights						\$
330.4	Structures and Improvements						-
331.4	Distribution Reservoirs & Standpipes						-
333.4	Transmission and Distribution Mains						-
334.4	Services						-
335.4	Meters and Meter Installations						-
339.4	Hydrants						-
	Other Plant & Miscellaneous Equipment						-
	Total Intangible Plant		\$ -	\$ -	\$ -	\$ -	\$ -

ACCUMULATED DEPRECIATION - PLANT IN SERVICE							
Acct. No.	Account	Ref. Page	Balance at Beginning of Year	Additions	Retirements	Adjustments	Balance at End of Year
303.5	VI. GENERAL PLANT						
304.5	Land and Land Rights						\$ -
340.5	Structures & Improvements						-
341.5	Office Furniture & Equipment						-
342.5	Transportation Equipment						-
343.5	Stores Equipment						-
344.5	Tools, Shop & Garage Equipment						-
345.5	Laboratory Equipment						-
346.5	Power Operated Equipment						-
347.5	Communication Equipment						-
348.5	Miscellaneous Equipment						-
	Other Tangible Property						-
	Total General Plant		\$ -	\$ -	\$ -	\$ -	\$ -
	TOTAL ACC DEPR-PLANT IN SERVICE	W-1	\$ -	\$ -	\$ -	\$ -	\$ -

[illegible]

I. Other Physical Property (Accounts 121 and 122)

IV. Other Funds (Accounts 125, 126 and 127)						
Item No.	Description	Ref. Page	Beginning Balance	Debits	Credits	Ending Balance
						\$ -
						-
						-
						-
						-
						-
						-
	TOTAL	W-1	\$ -	\$ -	\$ -	\$ -
Total Other Property & Investments						<u>\$ -</u>

EXTRAORDINARY PROPERTY LOSS			
Item No.	Description	Years to Amortize	Total Amount to Amortize as Authorized by APSC
			\$ -
			-
			-
			-
			-
			-
			-
	TOTAL		\$ -

AMORTIZATION OF EXTRAORDINARY PROPERTY LOSSES (Account 186.2)							
			Annual Amortization				
Item No.	Balance At Beginning of Year	Ref. Page	Approval Order #	Debit Amount	Credit		Balance at End of Year
					Acct. #	Amount	
							\$ -
							-
							-
							-
							-
							-
							-
							-
							-
Total	\$ -	W-2		\$ -		\$ -	\$ -

DEBT DISCOUNT AND EXPENSE (Account 181)						
Item No.	Description	Ref. Page	Balance At Beginning of Year	Debits	Credits	Balance at End of Year
						\$ -
						-
						-
						-
						-
						-
						-
						-
						-
	TOTAL	W-3	\$ -	\$ -	\$ -	\$ -

CAPITAL STOCK						
Item No.	Kind of Stock	Ref. Page	Par or Stated Value Per Share	No. of Shares Authorized	No. of Shares Outstanding End of Year	Capital Stock Outstanding End of Year (\$)
						\$
	TOTAL	W-3		-	-	\$ -

PREMIUM AND ASSESSMENT ON CAPITAL STOCK							
Item No.	Kind of Stock	Ref. Page	Balance At Beginning of Year	Realized During the Year	Released During Year	Balance at End of Year	Acct Credited With Premium Written Off
	Total	W-3	\$ -	\$ -	\$ -	\$ -	

DIVIDENDS							
Item No.	Class of Stock	Ref. Page	Date Declared	Date Paid	No. of Shares	Dividend Per Share	Total Amount Paid
Total		W-19			-	\$ -	\$ -

REACQUIRED CAPITAL STOCK							
Item No.	Kind of Stock	Ref. Page	Date acquired	Re-	No. of Shares Reacquired	Cost	Par or Stated Value of Stock
	TOTAL	W-3			-	\$ -	\$ -

I. LONG-TERM DEBT* (Accounts 221-224)

II. NOTES PAYABLE TO ASSOCIATED COMPANIES (Account 234)

III. OTHER NOTES PAYABLE (Account 232)

* All security issues require APSC approval.

TOTAL DEBT OUTSTANDING

\$

ACCRUED TAXES (Accounts 236 & 241)							
Item No.	Kind of Tax	Ref. Page	Balance at Beginning of Year	Accrued During Year	Paid During Year	Adjustments	Balance at End of Year
1	Federal Income						-
2	State Income						-
							-
							-
							-
							-
							-
							-
	TOTAL	W-3	\$ -	\$ -	\$ -	\$ -	\$ -

INTEREST ACCRUED ON OTHER LIABILITIES						
Item No.	Description	Ref. Page	Balance at Beginning of Year	Debits	Credits	Balance at End of Year
						\$ -
						-
						-
						-
						-
						-
	TOTAL	W-3	\$ -	\$ -	\$ -	\$ -

OTHER CURRENT AND ACCRUED LIABILITIES						
Item No.	Description	Ref. Page	Balance at Beginning of Year	Debits	Credits	Balance at End of Year
						\$ -
						-
						-
						-
						-
						-
	TOTAL	W-3	\$ -	\$ -	\$ -	\$ -

OTHER DEFERRED CREDITS						
Item No.	Description	Ref. Page	Balance at Beginning of Year	Debits	Credits	Balance at End of Year
						\$ -
						-
						-
						-
						-
						-
	TOTAL	W-4	\$ -	\$ -	\$ -	\$ -

CONSUMER ADVANCES FOR CONSTRUCTION (Account 252)

Item	Ref. Page	Amount
Balance at Beginning of Year	W-4	
Additions		
Refunds		
Transfers: (Account Credited & Amount)		
Balance at End of Year	W-4	\$ -

CONTRIBUTIONS IN AID OF CONSTRUCTION (Account 271)

For Additions Show Whether Cash or Other Contributions and by Whom Contributed	Ref. Page	Amount
Balance at Beginning of Year	W-4	
Additions		
Debits: (Account Credited & Amount)		
Balance at End of Year	W-4	\$ -

CUSTOMER DEPOSITS (Account 235)

Item	Ref. Page	Amount	
		System	Arkansas
Balance at Beginning of Year	W-3		
Credits:			
Debits: (Account Credited and Amount)			
Balance at End of Year	W-3	\$ -	\$ -
Indicate Calendar Year Amount of Interest Paid Customers @ 6%			
Indicate Calendar Year Amount of Interest Paid Customers @ 8%			

COMPUTATION OF INVESTMENT CREDIT

(1) Qualified Investment in New or Used Property

Type of Prop.	Life Years	Property	(2) Cost or Basis	(3) %	Investment (Col 2 x Col 3)
		(2) Total Qualified Investment			
		(3) Tentative Investment			

INVESTMENT TAX CREDIT

Item No.	Account Credited	Ref. Page	Balance at Beginning of Year	Debits	Credits	Balance at End of Year
						-
						-
						-
						-
						-
						-
						-
						-
		W-4	-	-	-	-

DEFERRED INCOME TAXES

Item No.	Description	Ref. Page	Balance at Beginning of Year	Debits	Credits	Balance at End of Year
						-
						-
						-
						-
						-
						-
						-
						-
						-
	TOTAL	W-4	-	-	-	-

ACCUMULATED RESERVES			
Item No.	Depreciation Reserve	Amount	
		System	Arkansas
1	Balance at Beginning of Year		
	CREDITS		
2	Depreciation Expense		
3	Material & Supplies (Salvage)		
4	Other (Specify)		
5			
6			
7			
8	Total Credits	\$ -	\$ -
	DEBITS		
9	Retirement of Plant		
10	Removal Costs		
11	Other (Specify)		
12			
13			
14			
15	Total Debits	\$ -	\$ -
16	Balance at End of Year	\$ -	\$ -

Line No.	Other Reserves	Balance At Beginning of Year	Debits	Credits	Balance at End of Year
1	Amortization of utility plant acquisition adjustments				\$ -
2	Depreciation & amortization of other property				
3	Uncollectible Accounts				-
4	Other (Specify)				-
					-
					-
					-
					-
					-
					-
					-
					-
					-
					-
					-
5	TOTAL	\$ -	\$ -	\$ -	\$ -

INCOME STATEMENT				
Line No.	Description	Ref. Page		
1	Operating Revenues	W-25		\$ -
2	Operating Expenses	W-24	\$ -	
3	Taxes Other Than Income Taxes			
4	Income Taxes on Utility Operating Income			
5	Provision for Deferred Taxes			
6	Income Taxes Deferred Prior Years - Credit			
7	Investment Tax Credit - Deferred to Future Periods			
8	Investment Tax Credit - Restored to Operating Income			
9	Total Operating Expense			\$ -
10	Net Operating Income			
	Other Income:			
11	Revenues from Merchandising			
12	Costs and Expenses of Merchandising			
13	Net Revenue from Non-Utility Operations			
14	Rental Income			
15	Interest & Dividends			
16	Allowance for Funds Used During Construction			
17	Miscellaneous Non-Operating Income			
18	Total Other Income			\$ -
	Other Income Deductions:			
19	Interest on Long-Term Debt			
20	Amortization of Debt Discount & Expense			
21	Amortization of Premium on Debt - Credit			
22	Interest on Debt to Associated Companies			
23	Other Interest Expense			
24	Miscellaneous Income Deductions			
25	Total Other Income Deductions			\$ -
28	Net Income			\$ -
29	Less: Reservation of Income			
30	Balance Transferred to Earned Surplus	W-19		\$ -

CAPITAL SURPLUS

(Give below an analysis of changes in capital surplus during the year)

Item No.	Item	Ref. Page	Debits	Credits
1	Balance at Beginning of Year			
2				
3				
4				
5				
6				
7				
8				
9				
	Balance at End of Year	W-3		\$ -

EARNED SURPLUS

1. Report in this schedule an accounting for changes in earned surplus for the year.
2. Each credit and debit during the year should be identified as to the surplus account in which included and the contra account affected shown. Minor items may be grouped by classes; however, the number of items in each group should be shown.
3. For each surplus reservation, state the purpose of the reservation, the amount and the reserve account credited. In a footnote explain the basis for determining the amount reserved, and, if reservations are to be recurrent, state the number and annual amounts to be reserved as well as the total reservation eventually to be accumulated.
4. Dividend appropriations should be shown for each class and series of capital stock.

Item No.	Item	Ref. Page	Earned Surplus Account	Contra Account Affected	Amount
1	Balance at Beginning of Year				
2	Credits				
3					
4					
5					
6					
7					
8	Debits				
9					
10					
11					
12					
13					
14					
15					
16					
	Balance at End of Year	W-3			\$ -

WATER OPERATING EXPENSES

Line No.	Acct. No.	Account	Total System	Total Arkansas
		I. SOURCE OF SUPPLY EXPENSES		
		Operations		
1	601.1	Salaries and Wages - Employees		
2	603.1	Salaries and Wages - Officers, Directors and Majority Stockholders		
3	604.1	Employee Pensions and Benefits		
4	610.1	Purchased Water		
5	615.1	Purchased Power		
6	616.1	Fuel for Power Production		
7	618.1	Chemicals		
8	620.1	Materials and Supplies		
9	631.1	Contractual Services - Engineering		
10	632.1	Contractual Services - Accounting		
11	633.1	Contractual Services - Legal		
12	634.1	Contractual Services - Management Fees		
13	635.1	Contractual Services - Other		
14	641.1	Rental of Building / Real Property		
15	642.1	Rental of Equipment		
16	650.1	Transportation Expenses		
17	656.1	Insurance - Vehicle		
18	657.1	Insurance - General Liability		
19	658.1	Insurance - Workman's Compensation		
20	659.1	Insurance - Other		
21	667.1	Regulatory Commission Expenses		
22	675.1	Miscellaneous Expense		
23		Total Operations		
		Maintenance		
23	601.2	Salaries and Wages - Employees		
24	603.2	Salaries and Wages - Officers, Directors and Majority Stockholders		
25	604.2	Employee Pensions and Benefits		
26	618.2	Chemicals		
27	620.2	Materials and Supplies		
28	631.2	Contractual Services - Engineering		
29	632.2	Contractual Services - Accounting		
30	633.2	Contractual Services - Legal		
31	634.2	Contractual Services - Management Fees		
32	635.2	Contractual Services - Other		
33	641.2	Rental of Building / Real Property		
34	642.2	Rental of Equipment		
35	650.2	Transportation Expenses		
36	656.2	Insurance - Vehicle		
37	657.2	Insurance - General Liability		
38	658.2	Insurance - Workman's Compensation		
39	659.2	Insurance - Other		
40	667.2	Regulatory Commission Expenses		
41	675.2	Miscellaneous Expense		
42		Total Maintenance		
43		Total Source of Supply Expenses		

WATER OPERATING EXPENSES				
Line No.	Acct. No.	Account	Total System	Total Arkansas
II. WATER TREATMENT EXPENSES				
Operations				
44	601.3	Salaries and Wages - Employees		
45	603.3	Salaries and Wages - Officers, Directors and Majority Stockholders		
46	604.3	Employee Pensions and Benefits		
47	615.3	Purchased Power		
48	616.3	Fuel for Power Production		
49	618.3	Chemicals		
50	620.3	Materials and Supplies		
51	631.3	Contractual Services - Engineering		
52	632.3	Contractual Services - Accounting		
53	633.3	Contractual Services - Legal		
54	634.3	Contractual Services - Management Fees		
55	635.3	Contractual Services - Other		
56	641.3	Rental of Building / Real Property		
57	642.3	Rental of Equipment		
58	650.3	Transportation Expenses		
59	656.3	Insurance - Vehicle		
60	657.3	Insurance - General Liability		
61	658.3	Insurance - Workman's Compensation		
62	659.3	Insurance - Other		
63	667.3	Regulatory Commission Expenses		
64	675.3	Miscellaneous Expense		
65		Total Operations		
Maintenance				
66	601.4	Salaries and Wages - Employees		
67	603.4	Salaries and Wages - Officers, Directors and Majority Stockholders		
68	604.4	Employee Pensions and Benefits		
69	618.4	Chemicals		
70	620.4	Materials and Supplies		
71	631.4	Contractual Services - Engineering		
72	632.4	Contractual Services - Accounting		
73	633.4	Contractual Services - Legal		
74	634.4	Contractual Services - Management Fees		
75	635.4	Contractual Services - Other		
76	641.4	Rental of Building / Real Property		
77	642.4	Rental of Equipment		
78	650.4	Transportation Expenses		
79	656.4	Insurance - Vehicle		
80	657.4	Insurance - General Liability		
81	658.4	Insurance - Workman's Compensation		
82	659.4	Insurance - Other		
83	667.4	Regulatory Commission Expenses		
84	675.4	Miscellaneous Expense		
85		Total Maintenance		
86		Total Water Treatment Expenses		

WATER OPERATING EXPENSES				
Line No.	Acct. No.	Account	Total System	Total Arkansas
		III. TRANSMISSION & DISTRIBUTION EXPENSES		
		Operations		
87	601.5	Salaries and Wages - Employees		
88	603.5	Salaries and Wages - Officers, Directors and Majority Stockholders		
89	604.5	Employee Pensions and Benefits		
90	615.5	Purchased Power		
91	616.5	Fuel for Power Production		
92	618.5	Chemicals		
93	620.5	Materials and Supplies		
94	631.5	Contractual Services - Engineering		
95	632.5	Contractual Services - Accounting		
96	633.5	Contractual Services - Legal		
97	634.5	Contractual Services - Management Fees		
98	635.5	Contractual Services - Other		
99	641.5	Rental of Building / Real Property		
100	642.5	Rental of Equipment		
101	650.5	Transportation Expenses		
102	656.5	Insurance - Vehicle		
103	657.5	Insurance - General Liability		
104	658.5	Insurance - Workman's Compensation		
105	659.5	Insurance - Other		
106	667.5	Regulatory Commission Expenses		
107	675.5	Miscellaneous Expense		
108		Total Operations		
		Maintenance		
109	601.6	Salaries and Wages - Employees		
110	603.6	Salaries and Wages - Officers, Directors and Majority Stockholders		
111	604.6	Employee Pensions and Benefits		
112	618.6	Chemicals		
113	620.6	Materials and Supplies		
114	631.6	Contractual Services - Engineering		
115	632.6	Contractual Services - Accounting		
116	633.6	Contractual Services - Legal		
117	634.6	Contractual Services - Management Fees		
118	635.6	Contractual Services - Other		
119	641.6	Rental of Building / Real Property		
120	642.6	Rental of Equipment		
121	650.6	Transportation Expenses		
122	656.6	Insurance - Vehicle		
123	657.6	Insurance - General Liability		
124	658.6	Insurance - Workman's Compensation		
125	659.6	Insurance - Other		
126	667.6	Regulatory Commission Expenses		
127	675.6	Miscellaneous Expense		
128		Total Maintenance		
129		Total Transmission & Distribution Expenses		

WATER OPERATING EXPENSES				
Line No.	Acct. No.	Account	Total System	Total Arkansas
IV. CUSTOMER ACCOUNTS EXPENSE				
130	601.7	Salaries and Wages - Employees		
131	603.7	Salaries and Wages - Officers, Directors and Majority Stockholders		
132	604.7	Employee Pensions and Benefits		
133	615.7	Purchased Power		
134	616.7	Fuel for Power Production		
135	620.7	Materials and Supplies		
136	631.7	Contractual Services - Engineering		
137	632.7	Contractual Services - Accounting		
138	633.7	Contractual Services - Legal		
139	634.7	Contractual Services - Management Fees		
140	635.7	Contractual Services - Other		
141	641.7	Rental of Building / Real Property		
142	642.7	Rental of Equipment		
143	650.7	Transportation Expenses		
144	656.7	Insurance - Vehicle		
145	657.7	Insurance - General Liability		
146	658.7	Insurance - Workman's Compensation		
147	659.7	Insurance - Other		
148	667.7	Regulatory Commission Expenses		
149	670.7	Bad Debt Expense		
150	675.7	Miscellaneous Expense		
151		Total Customer Accounts Expenses		
V. ADMINISTRATION & GENERAL EXPENSES				
152	601.8	Salaries and Wages - Employees		
153	603.8	Salaries and Wages - Officers, Directors and Majority Stockholders		
154	604.8	Employee Pensions and Benefits		
155	615.8	Purchased Power		
156	616.8	Fuel for Power Production		
157	620.8	Materials and Supplies		
158	631.8	Contractual Services - Engineering		
159	632.8	Contractual Services - Accounting		
160	633.8	Contractual Services - Legal		
161	634.8	Contractual Services - Management Fees		
162	635.8	Contractual Services - Other		
163	641.8	Rental of Building / Real Property		
164	642.8	Rental of Equipment		
165	650.8	Transportation Expenses		
166	656.8	Insurance - Vehicle		
167	657.8	Insurance - General Liability		
168	658.8	Insurance - Workman's Compensation		
169	659.8	Insurance - Other		
170	660.8	Advertising Expense		
171	666.8	Regulatory Commission Expenses - Amort. Of Rate Case Expense		
172	667.8	Regulatory Commission Expenses		
173	675.8	Miscellaneous Expense		
174		Total Administration & General Expenses		

WATER OPERATING EXPENSES				
Line No.	Acct. No.	Account	Total System	Total Arkansas
		VI. DEPRECIATION AND AMORTIZATION EXPENSES		
175	403	Depreciation Expense		
176	406	Amort. of Utility Plant Acquisition Adjustments		
177	407	Amortization Expense		
178	407.1	Amort. of Limited-term Plant		
179	407.2	Amort. of Property Losses		
180	407.3	Amort. of Other Utility Plant		
181		Total Depreciation and Amortization Expenses		
182		TOTAL OPERATING EXPENSES BEFORE TAXES (Ref. P. W-18)		

WATER OPERATING REVENUES - ARKANSAS						
Line No.	Acct. No.	Account	Ref. Page	Average Number of Customers	Number of M. Gallons Sold	Revenues
		WATER SALES				
1	461	Metered Water Revenue				
2	461.1	Metered Sales to Residential Customers				
3	461.2	Metered Sales to Commercial Customers				
4	461.3	Metered Sales to Industrial Customers				
5	461.4	Metered Sales to Public Authorities				
6	461.5	Metered Sales to Multiple Family Dwellings				
7		Total				
8	460	Unmetered Water Revenue				
9	462	Fire Protection Revenue				
10	462.1	Public Fire Protection				
11	462.2	Private Fire Protection				
12	464	Other Sales to Public Authorities				
13	465	Sales to Irrigation Customers				
14	466	Sales for Resale				
15	467	Interdepartmental Sales				
16		Total				
17		Total Water Sales				
		OTHER WATER REVENUES				
18	657.1	Forfeited Discounts				
19	658.1	Misc. Service Revenues				
20	659.1	Rent from Water Property				
21	667.1	Interdepartmental Rents				
22	675.1	Other Water Revenues				
23		Total				
24		TOTAL WATER OPERATING REVENUES	W-18			

WATER OPERATING REVENUES - SYSTEM							
Line No.	Acct. No.	Account	Ref. Page	Average Number of Customers	Number of M. Gallons Sold	Revenues	
WATER SALES							
1	461	Metered Water Revenue					
2	461.1	Metered Sales to Residential Customers					
3	461.2	Metered Sales to Commercial Customers					
4	461.3	Metered Sales to Industrial Customers					
5	461.4	Metered Sales to Public Authorities					
6	461.5	Metered Sales to Multiple Family Dwellings					
7		Total					
8	460	Unmetered Water Revenue					
9	462	Fire Protection Revenue					
10	462.1	Public Fire Protection					
11	462.2	Private Fire Protection					
12	464	Other Sales to Public Authorities					
13	465	Sales to Irrigation Customers					
14	466	Sales for Resale					
15	467	Interdepartmental Sales					
16		Total					
17		Total Water Sales					
OTHER WATER REVENUES							
18	657.1	Forfeited Discounts					
19	658.1	Misc. Service Revenues					
20	659.1	Rent from Water Property					
21	667.1	Interdepartmental Rents					
22	675.1	Other Water Revenues					
23		Total					
24		TOTAL WATER OPERATING REVENUES	W-18				

WATERWORKS ANNUAL OPERATING REPORT & STATISTICS

Show the particulars called for below. Where space is insufficient for a complete response, continue the item(s) on the continuation sheet provided on page W-33 and identify by page number.

ITEM NO.	ITEM	RESPONSE
1	Name and Location of Community Served	
2	Population of Community Served	
3	Type of Community Served a. Residential only b. Residential with Light Commercial c. Residential with Commercial, Institutional & Industrial	
4	Source of Water Supply a. Wells (List number, diameter, depth, & proven dependable gpm of each pump) b. Stream without Impoundage (Name stream and list number and capacity in gpm of each pump) c. Lake or Impoundage (Name lake and list number and capacity in gpm capacity of each pump) d. Spare pumps (List number of installed spare source pumps and the gpm capacity of each pump) e. Springs (List number of springs used and capacity in gpm of each pump)	

WATERWORKS ANNUAL OPERATING REPORT & STATISTICS

Show the particulars called for below. Where space is insufficient for a complete response, continue the item(s) on the continuation sheet provided on page W-33 and identify by page number.

- 5 Treatment of Water (List those items below which most nearly describe treatment used)
- a. Aeration
 - b. Chemical treatment (Briefly describe type)
 - c. Disinfection:
 - i. Chlorination
 - ii. Chlorination and ammonia
 - iii. Hypochlorination
 - iv. Ozone
 - v. Other
 - d. Filtration
 - e. Water Stabilization
 - f. Sedimentation

- 6 Domestic Water Demand
- a. Annual average, month, 1000 gallons
 - b. Season, max. day, 1000 gallons
 - c. Month, max., 1000 gallons
 - d. Day, max., 1000 gallons
 - e. Hour, 4-hr. max., 1000 gallons

- 7 Fire Hydrant Service
- a. Fire water service not provided
 - b. Fire water service provided
 - c. Fire Flow Test (Include copy of latest fire flow test and report of Insurance Service Office of Arkansas)

WATERWORKS ANNUAL OPERATING REPORT & STATISTICS

Show the particulars called for below. Where space is insufficient for a complete response, continue the item(s) on the continuation sheet provided on page W-33 and identify by page number.

- 8 Finished Water Storage (List number, materials of construction and capacity in gallons of each finished water storage tank)
- a. Below ground tanks
 - b. Standpipes or tanks at ground level
 - c. Elevated Tanks

- 9 Distribution System Pressure
- a. Lowest normal pressure in system
 - b. Highest normal pressure in system
 - c. Average normal system pressure

- 10 Purity of Water Supplied
- a. Number of water samples submitted to Health Department each month
 - b. Number of water samples submitted during year which did not meet Health Department standards
 - c. Free chlorine residual (in milligrams per liter) maintained at plant and at extremities of distribution system

- 11 Customer Complaints
- a. Total number of customer complaints received
 - b. Number of customer complaints concerning purity, wholesomeness, potability, odor or taste of water

WATERWORKS ANNUAL OPERATING REPORT & STATISTICS

Show the particulars called for below. Where space is insufficient for a complete response, continue the item(s) on the continuation sheet provided on page W-33 and identify by page number.

12	Interruptions of Service a. Number of times and total hours service was intentionally interrupted for required service, maintenance of system or extensions b. Number of times and total hours service was interrupted due to emergencies (loss of power, main breakage, severe storms, etc.)	
13	Service Meters by Customer Class (No. of Meters) a. Residential b. Commercial c. Institutional (or public) d. Industrial	
14	Extent of Supply and Distribution System (List by size and the materials of construction total lineal feet of pipe in the supply and distribution system)	
15	Water Operator's License a. Class of Operator's License required by Department of Health b. Name and job title of Company employee(s) holding required Operator's License	
16	Electrical Supply a. Electricity purchased from b. Kilowatt-hours consumed c. Identity of rate schedule d. Total cost of electricity consumed	

WATERWORKS ANNUAL OPERATING REPORT & STATISTICS

Show the particulars called for below. Where space is insufficient for a complete response, continue the item(s) on the continuation sheet provided on page W-33 and identify by page number.

17	Production and Sales for Year a. Total amount of water pumped b. Total amount of water purchased c. Total d. Water sold to consumers e. Water used by fire hydrants and street cleaning f. Water used by respondent g. Total h. Water lost and unaccounted for	
18	Maintenance and Distribution System a. Number of dead-end mains in system, 4-inch dia. or larger b. Frequency of flushing above dead-end mains c. Frequency entire distribution system is flushed and all valves and fire hydrants checked for operation d. Frequency treatment plant and all storage tanks are checked for needed cleaning or repairs	
19	Adequacy of Waterworks a. In last five years, has there been any shortage of water supply or any bottlenecks in the plant which required any curtailment or restrictions on use of water? If so, describe fully the particulars.	

WATERWORKS ANNUAL OPERATING REPORT & STATISTICS

CONTINUATION SHEET

REPORT TO ARKANSAS PUBLIC SERVICE COMMISSION

CHECK LIST

Company Name _____

Instructions: In the space provided, please enter the appropriate amounts from the Annual Report to the APSC. Any discrepancies should be fully explained. Any differences between ending figures from last year's annual report and beginning balances in this year's annual report should be fully explained.

Description	Page W-1 Amount	Page W-5 Amount
Utility Plant in Service	-	-
Utility Plant Leased to Others	-	-
Property Held for Future Use	-	-
Utility Plant Purchased or Sold	-	-
Construction Work in Progress	-	-
Completed Construction Not Classified	-	-
Utility Plant Acquisition Adjustment	-	-
Description	Page W-1 Amount	Page W-10 Amount
Nonutility Property	-	-
Accum. Depr. of Nonutility Property		
Investments in Associated Companies		
Utility Investments		
Other Investments		
Sinking Funds		
Other Special Funds		
Description	Page W-1 Amount	Page W-9 Amount
Accum. Depr. - Utility Plant in Service	-	-
Description	Page W-2 Amount	Page W-11 Amount
Unamortized Debt Discount and Expense		
Other Deferred Debits		

REPORT TO ARKANSAS PUBLIC SERVICE COMMISSION

CHECK LIST

Company Name _____

Instructions: In the space provided, please enter the appropriate amounts from the Annual Report to the APSC. Any discrepancies should be fully explained. Any differences between ending figures from last year's annual report and beginning balances in this year's annual report should be fully explained.

Description	Page W-3 Amount	Page W-12 Amount
Common Stock Issued	-	-
Premium on Capital Stock	-	-
Reacquired Capital Stock	-	-
Description	Page W-3 Amount	Page W-13 Amount
Bonds	-	
Reacquired Bonds	-	
Advances from Associated Companies	-	
Other Long-Term Debt	-	
Total Long Term Debt		
Notes Payable	-	-
Notes Payable to Associated Companies	-	-
Description	Page W-3 Amount	Page W-14 Amount
Taxes Other than Income	-	
Income Taxes	-	
Interest Accrued on Other Liabilities	-	-
Description	Page W-3 Amount	Page W-15 Amount
Customer Deposits	-	-
Description	Page W-3 Amount	Page W-19 Amount
Unappropriated Retained Earnings	-	-

CHECK LIST

Company Name _____

Instructions: In the space provided, please enter the appropriate amounts from the Annual Report to the APSC. Any discrepancies should be fully explained. Any differences between ending figures from last year's annual report and beginning balances in this year's annual report should be fully explained.

Description	Page W-4 Amount	Page W-14 Amount
Other Deferred Credits	-	-
Description	Page W-4 Amount	Page W-15 Amount
Contributions in Aid of Construction	-	-
Customer Advances for Construction	-	-
Description	Page W-4 Amount	Page W-16 Amount
Accum. Deferred Investment Tax Credits	-	-
Accum. Deferred Income Taxes - Accel. Amort.	-	-
Accum. Deferred Income Taxes - Other Property	-	-
Accum. Deferred Income Taxes - Other	-	-
Total Accum Def Inc Taxes	-	-
Description	Page W-18 Amount	Page W-19 Amount
Balance Transfer to Earned Surplus	-	-
Description	Page W-18 Amount	Page W-26 Amount
Operating Revenues	-	-
Description	Page W-18 Amount	Page W-24 Amount
Operating Expenses	-	-

STATEMENT OF ACCURACY

I do hereby state that the amounts contained in this report are true and accurate, schedules have been cross-referenced by use of the attached check list, and that the accuracy of all totals has been verified by me or under my supervision. Should I or anyone under my supervision become aware of any error in or omission from this report, I will take steps to notify the Arkansas Public Service Commission of such error or omission and provide corrected schedules as soon as possible.

President/General Manager

REPORT TO ARKANSAS PUBLIC SERVICE COMMISSION

COMPANY CONTACTS

Company Information	
Company Name	
dba	
Official Mailing Address	

AREA	PERSON TO CONTACT	PHONE #	FAX #	E-MAIL
Annual Report				
Fuel Adjustment Report				
Cost of Debt Report				
Tariffs				
Accounting				
Rates				
Engineering				
Finance				
Income Taxes				
Property Taxes				
Gas Supply				
Legal				
Data Processing				

Please list the number of utility employees located in Arkansas _____.