



California American Water Company

303 H Street, Suite 250, Chula Vista, California 91910 (619) 409-7700 Fax (619) 409-7701

July 31, 2006

Via E-Mail

Jonathan P. Tom
Water Division
California Public Utilities Commission
505 Van Ness Ave.
San Francisco, CA 94102

Re: Comments on Water Action Plan and Rate Case Plan

Dear Mr. Tom

By this letter California-American Water Company (“California American Water”) responds to the July 7, 2006 letter from Kevin Coughlan, Director of the California Public Utilities Commission Water Division, requesting comments from Class A water utilities on methods to implement the Water Action Plan and improve the Rate Case Plan. California American Water welcomes the opportunity to share its experiences with the current Rate Case Plan and its suggestions for ways to advance the objectives of the Water Action Plan.

California American Water has thoroughly reviewed the current Rate Case Plan and the results of its general rate case applications over the last several rate cycles. While certain aspects of the current Rate Case Plan have simplified general rate case application preparation and review, there are still changes that could be made to make the rate case application process less adversarial, more effective, and more cost efficient. In addition, since the Water Action Plan was not part of the scope of the Rate Case Plan, there are changes that could be made to implement the objectives of the Water Action Plan.

California American Water’s suggestions below are divided into two main categories. The first category consists of general suggestions to simplify and improve the Rate Case Plan. The second category consists of suggestions to implement the specific Water Action Plan objectives.

GENERAL RATE CASE PLAN IMPROVEMENT SUGGESTIONS

1. Single Rate Case Applications for Multi-District Companies

Each Class A water company with multiple districts should file a single rate case application for all districts. A single rate case application for each Class A water company, including multi-district companies, will eliminate many of the concerns of multi-district utilities regarding the applicability of rate of return and allowances for



general office. Additionally, because all of the records for each company will be filed in a single rate case application, it will allow the Division of Ratepayer Advocates (“DRA”) the opportunity to undertake a more thorough analysis of the entire company’s books and records.

2. Four and Half Year Rate Case Application Schedule

To address the increased administrative burden associated with the preparation and review of a single rate case application for multi-district companies, California American Water recommends that each Class A water utility should file a rate case application once every four and a half years – not three as in the current Rate Case Plan. Implementation of this plan would require shuffling the current schedule and must include revenue protection safeguards for companies or districts that will go beyond the three-year effective period of the previous rate case.

Because they would require the most time and resources for preparation and review, the three large multi-district water companies (Golden State, California American Water and California Water Service) should file cases one and a half years apart. The remaining Class A water companies (Park, Suburban, San Gabriel, San Jose, Valencia and Great Oaks) would be distributed equally into the six remaining slots between the three large multi-district companies. Attached to this letter is a proposed schedule.

Under California American Water’s proposal, rate cases would cover alternating four and five year periods. All rates would be effective January 1 and interim rates allowing retroactive rates back to January 1 would be required for all mid-year filings.

3. Eighteen Month Processing Time for Rate Case Applications

In addition to lengthening the time between rate case filings, California American Water proposes that the Commission lengthen the schedule for processing each case to eighteen months. Under this schedule, a company would file its proposed application six months before the actual filing date. Service and notice of the proposed application would be similar to that currently required of the final application. DRA and intervenors would have six months to review the proposed application and issue data requests. With this six-month review and discovery period, the Master Data Request could be reduced because the parties would have more time to review the proposed application and submit specific data requests for information that they actually need. After the six-month period, the company would file the final application.



After the final application is filed, there would be a two-month period for meet and confer sessions before DRA and intervenors issue their reports and testimony in month three. The company would file formal rebuttal testimony within three weeks of reports and testimony from DRA and intervenors. Month four would be devoted to settlement negotiations, which receive a short shrift under the current Rate Case Plan. The Commission should encourage the use of alternate dispute resolution in general rate cases. Before hearings, which would take place during month five, the parties could file a full or partial settlement as well as a complete comparison exhibit setting forth all open issues to be determined in the hearing. A proposed decision should be issued around the end of month nine allowing plenty of time for comments on the decision and alternates to be issued, if necessary.

WATER ACTION PLAN OBJECTIVE IMPLEMENTATION SUGGESTIONS

1. Maintain Highest Standards of Water Quality

To achieve the Water Action Plan objective of maintaining the highest standards of water quality, California American Water recommends that the Commission require all Class A water utilities to meet at least annually with the Department of Health Services (“DHS”) to discuss all current and potential water quality issues. A full report of these annual meetings since the last general rate case should be included in each Class A water company application.

Each general rate case application should also include water quality data, including historical data since the last case and projections of contamination plumes based on hydrological data. This data could be used to support proposed projects as well as emergency projects needed for water quality. The Commission should also allow water quality memorandum accounts for all water companies to track all costs, including the return on and of plant required for emergency water quality remediation.

Finally, the Commission should provide incentives for larger companies to assist or acquire smaller troubled water companies. In rate of return determinations (discussed in more detail below) the Commission should give consideration to companies that work to solve water quality issues for smaller companies. This could be through low or no interest loans, partnerships or acquisition.

2. Strengthen Water Conservation Programs to a Level Comparable to Energy Utilities

All Class A water utilities should have a plan to meter all current un-metered connections. The plan should include a schedule to complete the conversion and a detailed estimate of the costs for the conversion. Companies should strive to complete the transition within a two rate case cycle. Additionally, the



Commission should require water companies to actively participate in joint sessions with energy utilities to assess the effectiveness of conservation programs. A report of these meetings and a report on the estimated savings should be included in each company's proposed application.

The Commission should strongly encourage water company participation in the California Urban Water Conservation Council ("CUWCC") and costs applicable to participation in the CUWCC should be recovered as part of a conservation memorandum account. Companies should also be able to track in a conservation memorandum account the costs of external conservation personnel, if necessary.

The Commission should implement a rebuttable presumption in favor of conservation rate design. A company choosing not to implement a conservation rate design should be required to make a showing in its rate case application why a conservation rate design is not appropriate due to specific circumstances.

The conservation rate designs approved by the Commission should include a Water Revenue Adjustment Mechanism ("WRAM") account to track revenue variations due to the rate design and track revenue losses that occur due to decreased consumption. The conservation rate designs should increase the revenue collection in the variable cost component, and in doing so, provide water companies with fixed cost recovery protection. This will remove disincentives for water companies to promote conservation.

Finally, the Commission should consider positive return on equity adjustments for water companies that fully utilize conservation measures, and negative adjustments could be considered in cases where utilities do not promote conservation.

3. Promote Water Infrastructure Investment

In their proposed and final applications all water companies should include ten-year investment plans to support capital investments. Companies should develop these plans using water quality action plans, water conservation plans and comprehensive planning studies. Included in the plans should be a long-range plan to replace aging distribution infrastructure.

The Commission should allow companies to fund replacement plant via two infrastructure system replacement surcharges ("ISRS") capped at an annual percent of the revenue requirement. The first ISRS would be for distribution system needs and a balancing of current and future needs to reduce future spikes. A second ISRS should be allowed for normal and recurring source of supply, pumping and water treatment plant.



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The Commission should also allow each water company an annual company-wide discretionary investment amount based on historical construction expenditures. All capital investment needs above the discretionary amount would be recovered in rates via annual advice letters. The Commission should allow AFUDC (allowance for funds used during construction) on all of these projects until they are put in rates.

Finally, the Commission should allow each water company to establish memorandum accounts to allow for emergency development and construction of water treatment plant and other emergency replacements.

4. Assist Low Income Ratepayers

The Commission should establish a generic low income program for all water companies. If possible, this program should include the participation of the local electric utilities for distribution of the low-income credits directly to customers. This process would allow distribution of low income assistance to water users who are not the customers, such as those who reside in multi-family dwellings. The generic low income program should include a set amount or percentage discount and should be funded through a state-wide pool.

Additionally, the Commission should promote the installation of meters for all dwelling units, including those in multi-family units. This could be accomplished by sub-metering with radio read meters.

5. Streamline CPUC Regulatory Decision Making

California American Water believes that the suggestions made in the first section of this letter will generally streamline the Commission's regulatory process. This section includes additional recommendations for streamlining the Commission's regulatory process that are directly tied to the Commission's Water Action Plan.

First, California American Water recommends that the Commission institute a single annual generic rate of return case. This case would decide the return on equity for all companies in general. As part of the general rate case, each company would put on a showing to determine capital structure, debt cost and company specific return on equity adjustments that balance that company's specific cost of capital (including differences in capital structure). Each utility would change its cost of capital annually to adjust for its actual embedded current debt costs.

Second, the Commission should structure purchased power and purchased water reserve accounts to allow full cost recovery in each successive rate case as long as a company can show that it maintained efficient methods of use. This will ensure that customers are protected when consumption is reduced, because the marginal cost of water and power is normally higher than the embedded average cost in



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rates. Additionally, the number of annual advice letters could be reduced if this account is reviewed only during the rate case.

Third, the Commission should encourage parties to develop interim rates through settlement, rather than using just an inflation rate, especially in cases of large requested increases. This may become less necessary, however, if more and more plant is added via ISRS and annual advice letters.

6. Set Rates that Balance Investment, Conservation, and Affordability

The Commission should allow plant development costs in rates on an annual basis, which would result in less capitalization of engineering costs. Similarly, the Commission should authorize a surcharge mechanism for direct reimbursement of Construction Work In Progress prior to plant start-up. Such mechanisms would help the Commission and the companies balance investment and affordability.

California American Water appreciates this opportunity share its suggestions for ways to improve the Rate Case Plan while advancing the objectives of the Water Action Plan. In addition to the reply comments to be provided on August 11, 2006, California American Water believes that a series of workshops would be beneficial to further discuss and refine the suggestions made by itself and other participating parties.

Very truly yours,

David P. Stephenson
California-American Water Company

cc: Kevin Coughlan
Parties that Received July 7, 2006 Letter



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CALIFORNIA PUBLIC UTILITIES COMMISSION					
WATER UTILITY GENERAL RATE CASE FILING SCHEDULE BASED ON 4 ½ YEAR CYCLE					
Filing Date	Districts	Utility	Filing Date	Districts	Utility
Year 1					
January		California Water	July		Valencia
Year 2					
January		Great Oaks	July		Golden State
Year 3					
January		Park	July		San Jose
Year 4					
January		California American	July		San Gabriel
Year 5					
January		Suburban	July		California Water
Year 6					
January		Valencia	July		Great Oaks
Year 7					
January		Golden State	July		Park
Year 8					
January		San Jose	July		California American
Year 9					
January		San Gabriel	July		Suburban