Docket:	:	A.07-01-009 et al.
Exhibit Number	:	
Commissioner	:	Dian Grueneich
Admin. Law Judge	:	Regina DeAngelis
DRA Project Mgr.	:	Victor Chan
	:	

DIVISION OF RATEPAYER ADVOCATES
CALIFORNIA PUBLIC UTILITIES COMMISSION

REPORT ON THE RESULTS OF OPERATIONS OF GOLDEN STATE WATER COMPANY Region I CLEARLAKE DISTRICT for

Test Year 2008 and Escalation Years 2009 and 2010
Application 07-01-011
In Consolidated Proceeding A. 07-01-009 et al.

San Francisco, California
May 14, 2007

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MEMORANDUM

In this Report, the Division of Ratepayer Advocates (DRA) of the California Public Utilities Commission (Commission) presents its analyses, findings, and recommendations pertaining to the Golden State Water Company (GSWC), general rate case (GRC) Applications (A.) 07-01-011, the Clearlake District (Clearlake), Region 1. GSWC is requesting Commission authorization to increase rates in Clearlake for water service in 2008 by $214,200, an increase of 12.99% over present rates; in 2009 by $20,500, an increase of 1.10%; and in 2010 by $32,800, an increase of 1.72%.

The DRA Project Coordinator for this Report is Victor Chan. Cleveland Lee is DRA's Legal Counsel for this proceeding. The DRA witnesses' qualifications are set forth in Appendix B of this Report.

EXECUTIVE SUMMARY

A. INTRODUCTION

On January 5, 2007, Golden State Water Company (GSWC) filed general rate case (GRC) as applications A. 07-01-011, requesting authorization to increase water rates for Clearlake in 2008 by $214,200, an increase of 12.99% over present rates; in 2009 by $20,500, an increase of 1.10%; and in 2010 by $32,800, an increase of 1.72%. For Test Year 2008 and 2009, GSWC requests a return on equity of 11.25% and a return on rate base of 9.41%. Unless otherwise indicated, this Report pertains only to Clearlake.

Concurrently with this Report, DRA is submitting a Cost of Capital Report and a Regional and District Administrative Offices Report separately, which will present inter alia DRA's recommended rate of return as well as expenses and capital additions relating to its regional and district administrative offices in this proceeding.

B. SUMMARY OF RECOMMENDATIONS

DRA submits this Report as its prepared direct testimony in A.07-01-011, which is a part of the consolidated proceeding, A. 07-01-009 et al. DRA recommends an overall revenue requirement of $1,709,000 in Test Year 2008, an overall increase of $1.74% over present rates for GSWC's ratepayers, as stated in the table below entitled "Summary of Earnings."

Summary of Earnings

Test Year 2008

DRA Present	GSWC Present	DRA Recommended	GSWC's Request
$1,679,700	$1,649,300	$1,709,000	$1,886,300

An overview of DRA's key recommendations is presented in the following Chapters:

(a) Chapter 2- Customer, Consumption and Operating Revenue

For the Test Year 2008, the total average number of customers estimated by DRA and GSWC is 2,179 customers. DRA's estimated total water supply for the Test Year 2008 is 288,923 Ccf; GSWC's estimate is 341,282 Ccf due to different estimates for average usage in the metered commercial and flat rate private fire water customer classes. DRA also recommends a different factor for water loss.

At GSWC's present and proposed rates, DRA's calculated operating revenues for the Test Year 2008 are $1,679,700 and $1,919,800 while GSWC's are $1,649,300 and $1,886,300, respectively.

(b) Chapter 3-Expenses (O&M, A&G)

DRA recommends $777,700 in operating expenses for Test Year 2008. GSWC's proposed amount is $871,500. DRA's estimate is $93,800 lower than GSWC's proposal, because DRA used different escalation factors, assumptions, and methodologies to forecast these future expense amounts.

Table 3-1 compares DRA's recommended and GSWC's proposed estimates of operating expenses.

(c) Chapter 4-Plant In Service

GSWC requests plant additions of $424,800 for 2007; $413,300 for Test Year 2008; and $421,100 for Test Year 2009. DRA recommends plant additions of $211,200 in 2007; $356,400 in Test Year 2008; and $242,900 in Test Year 2009.

DRA will also present different recommendations concerning GSWC's partnership with engineering firm CH2MHill, GSWC's Overhead Rate, and GSWC's planned and unplanned project Contingency adder.

(d) Chapter 5- Depreciation Expenses and Reserve

GSWC's estimated depreciation for Test Year 2008 is $2,895,300 and $3,188,000 for Test Year 2009. DRA estimates $2,918,600 for Test Year 2008 and $3,196,600 for Test Year 2009. The difference between GSWC's and DRA's recommended accumulated depreciation and amortization is due to the differences in estimates of plant in service during the Test Years.

(e) Chapter 6-Rate Base

GSWC requests rate base of $4,670,600 for Test Year 2008 and $4,731,300 for Test Year 2009. DRA recommends $4,413,200 for Test Year 2008 and $4,365,100 for Test Year 2009. The parties differ regarding plant additions, Construction Work in Progress (CWIP), and Common Utility Allocation.

(f) Chapter 7-Taxes

DRA estimates higher income taxes for both State and Federal Income Taxes as shown in Table 7-1. GSWC and DRA present different revenue requirements, expenses, rate base, and taxes.

(g) Chapter 8-Policy Issues

DRA reviewed various water quality documents provided by GSWC and contacted DHS for information relating to the compliance history of the Clearlake Water System and found that these water systems have been in compliance with the drinking water standards during 2004 to 2006. DRA also learned through the Public Advisor's office that GSWC has generally been satisfactorily serving to the Clearlake customers.

(h) Chapter 9-Rate Design

GSWC's rate design is consistent with the method set forth in D.86-05-064. Approximately 50% of fixed costs are recovered through service charges, and the remaining costs are recovered through a single block commodity rate.

(i) Chapter 10- Escalation Years

DRA estimates $1,729,000 and $1,781,000 as the revenue requirements for Escalation Years 2009 and 2010, respectively. For the same respective Escalation Years, GSWC estimates $1,917,600 and $1,962,800.

List of Chapters and the Sponsoring DRA Witness

Chapter Number	Description	Witness
-	Executive Summary	Victor Chan
1	Summary of Earnings	Victor Chan
2	Customer, Consumption, Operating Revenue	Victor Moon
3	Expenses (O&M, A&G)	Eric Matsuoka
4	Plants in Service	Patricia Esule
5	Depreciated and Amortization Expenses	Patricia Esule
6	Rate Base	Patricia Esule
7	Taxes	Eric Matsuoka
8	Policy Issues	Victor Moon
9	Rate Design	Victor Chan
10	Escalations Years	Victor Chan
	Appendix A (Escalation Factors)	
	Appendix B (Qualifications and Prepared Testimony)	

CHAPTER 1 SUMMARY OF EARNINGS

A. INTRODUCTION

This Chapter presents DRA's recommendations in response to GSWC's general rate increase requests for the Clearlake District in Test Year 2008 and Escalation Years 2009 and 2010.

B. SUMMARY OF RECOMMENDATIONS

The GSWC Summary of Earnings shown in Table 1-1 in this Chapter compares the results of operations for the Test Year 2008, including revenues, expenses, taxes and rate base.

C. DISCUSSION

The total revenues requested by GSWC are as follows:

Year	Amount of Increase	Percent
Test Year 2008	$214,200	12.99%
Escalation Year 2009	$20,500	1.10%
Escalation Year 2010	$32,800	1.72%

GSWC estimates that its proposed rates will produce revenues providing the following returns for Test Year 2008:

Test Year	Return on Rate base	Return on Equity
2008	9.41%	11.25%

D. CONCLUSION

DRA recommends a revenue increase for Test Year 2008 as follows (Years 2009 and 2010 are discussed in Chapter 10:

Test Year	Amount of Increase	Percent
2008	$29,300	1.74%

The last general rate increase for GSWC was authorized by D.05-05-025 in A.04-08-042, resulting in a rate of return on rate base of 8.52% in 2005 and 7.94% in 2006. In this Report DRA used the most recent rates filed by AL-1233-W which became effective on January 1, 2007.

A comparison of DRA's and GSWC's estimates for rate of return on rate base for the Test Year 2008 at present rates is shown below:

	Rate of Return		
	2008		
	DRA	GSWC	Diff
Present Rates	8.43%	6.57%	1.86%

TABLE 1-1				
GOLDEN STATE WATER COMPANY				
Region I- Clearlake				
SUMMARY OF EARNINGS				
Test Year 2008				
	DRA	Utility	DRA	Utility
Item	Present	Present	Recommended	Requested
	(A)	(B)	(C)	(D)
	(Dollars in Thousands)			
Operating Revenues	1,679.7	1,649.3	1,709.0	1,886.3
Total Revenue	1,679.7	1,649.3	1,709.0	1,886.3
Expenses				
Operation & Maintenance	534.0	565.2	534.0	566.3
Admininistrative and General	243.7	305.0	243.7	305.0
Depreciation & Amortization	305.7	307.9	305.7	307.9
Taxes Other Than Income	49.1	50.1	49.1	50.1
CCFT	30.0	18.1	32.6	38.9
FIT	145.2	95.8	155.4	178.4
Total Expenses	1,307.7	1,342.1	1,320.5	1,446.6
Net Income	372.0	307.0	388.5	439.7
Rate base	4,413.3	4,670.6	4,413.3	4,670.6
Rate of Return	8.43%	6.57%	8.80%	9.41%

CHAPTER 2 CUSTOMER, CONSUMPTION, OPERATING REVENUE

A. INTRODUCTION

This chapter sets forth DRA's analysis and recommendations regarding the number of customers, water consumption, and operating revenues in the Test Year 2008 for GSWC's Clearlake CSA, in Lake County.

B. SUMMARY OF RECOMMENDATIONS

Tables 2-3 through 2-6 at the end of this chapter show DRA's recommendations; GSWC's updated estimates as of February 15, 2007; and the Parties' differing estimates of the average number of customers, water consumption, and operating revenues. For the Test Year 2008, the total average number of customers estimated by DRA and GSWC is 2,179 customers. For the Test Year 2008, DRA's estimates for the total water supply is 288,923 Ccf and water sales 186,818 Ccf; compared to GSWC's 341,282 Ccf and 179,231 Ccf, respectively.

At the present and GSWC's proposed rates, DRA's calculated operating revenues for the Test Year 2008 are $1,679,700 and $1,919,800 while GSWC's are $1,649,300 and $1,886,300, respectively.

C. DISCUSSION

D.04-06-018 sets forth the revised Rate Case Plan (RCP) standards and procedures for Class A water utilities filing a GRC application. That decision advocates the applicant utility to forecast customer growth using a five-year average of the change in the number of customers by customer class. The utility and DRA must use the "New Committee Method" to forecast per customer usage for the residential and small commercial customer classes in GRC cases, based on the Standard Practice No. U-2 and "Supplement to Standard Practice No. U-25" with the following improvements adopted by D.04-06-018:

- Use monthly data for 10 years, if available;

- Use 30-year average for forecast values for temperature and rain; and
- Remove periods from the historical data in which sales restrictions were imposed or the Commission provided the utility with sales adjustment compensation, but replace with additional historical data to obtain 10 years of monthly data, if available.[1]

Water sales for classes of service other than residential and small commercial (such as irrigation, industrial, reclaimed, public authority, and other) should be forecasted based on total consumption by class using the best available data.[2] The "New Committee Method" is not applicable to any other classes other than the residential and commercial classes.

1. Customers

DRA concurs with GSWC's methodology for estimating its customer growth based on the last recorded 5-year average of 2002 through 2006, of which the total number of customers estimated for test year 2008 is 2,179 customers.

2. Average Consumption

With the exception of metered commercial and flat rate private fire water uses, DRA concurs with GSWC's updated water uses forecasted for the other customer classifications, which used the methodology to calculate water uses based on the last 5-year average from 2002 through 2006. For the Test Year 2008, DRA's forecasted total water sales amount is 186,817 Ccf while GSWC's is 179,231 Ccf.

For metered residential and commercial water use, DRA forecasted 85.9 Ccf per customer per year for the Test Year 2008 as opposed to GSWC's 82.4 Ccf. GSWC has a single volumetric tariff which is charged to both residential and

[1] D.04-06-018, memo, at App. At 6-7.

[2] (D) 04-06-018, at App. 6-7, sec. IV (1) ©, subsec. "Results of Operation."

commercial customers. The difference in water use forecast is due to the different methodologies used by both parties. DRA's regression model incorporates the time variable while GSWC's does not. Time is an essential factor for forecasting water use because it trends specifically for the designated time period for the Test Year. DRA's R^2 value calculated for the regression model indicated a higher correlation showing 83.1% compared to GSWC's 82.7%. DRA's forecasted metered residential and commercial water use more reasonably reflects the future pattern of water use than GSWC's because DRA incorporates the time variable in its regression model. For the Test Year 2008, DRA's forecasted total residential and commercial water sales amount is 186,726 Ccf while GSWC's is 179,142 Ccf.

For the private fire water use, DRA estimated 0.6 Ccf per customer per year whereas GSWC estimated 0.0 Ccf. The difference is due to DRA using the 5-year average while GSWC used the last recorded usage. DRA calculated the private fire usage for the Test Year 2008, by dividing the 3 Ccf of water used in 2004 by 5 years, which equated 0.6 Ccf for the Test Year. There are 4 private fire service connections in the Clearlake CSA. For the Test Year 2008, DRA's forecasted private fire water sales amount is 2.4 Ccf while GSWC's is 0 Ccf.

3. Water Loss

Water loss is the amount of water lost through operations plus unaccounted-for water due to leakage. Water used in operation covers water used in flushing the system whereas unaccounted-for water is determined to be the difference between the total amounts of water produced and the total amount of potable water recorded for sales.

Table 2-1 shows DRA's computations for the Clearlake CSA water loss.

1 Table 2-1 Clearlake CSA Water Loss

Recorded		Used in Operation:	Unaccounted For :	Water Loss
		% :	% :	%
2002		1.65	14.99	16.65
2003		4.73	23.92	28.65
2004		14.98	26.78	41.76
2005		12.83	31.75	44.58
	(the latest recorded figure):			
2006	GSWC	14.73	32.75	47.48
5-yr Avg.		9.78	26.04	35.82
Correction Factor:	0.9868			
Correction Factor *5-yr Avg.: DRA used		9.65	25.69	35.35

Calculation of Correction Factor:

2007 Capital Budget

Budget Group:		Description:	Budget, $:	Replacem,Ft.:	Reference
53	Project	Marin Main Replacement	170,000	800	Region I, Clear Lake
B-01	Blanket	Meters	9,700		Workpapers,
B-02	Blanket	Services	19,300		Vol. 2, P.75
B-06	Blanket	Minor Main Replacement	6,800		et seq.
	Equivalent linear footage:$150 per ft.		35,800	239	

2008 Capital Budget

53	Project	Sunset MainReplacement	312,000	1,400	Region I, Clear Lake
B-01	Blanket	Meters	5,100		Workpapers
B-02	Blanket	Services	10,100		Vol. 2, P.76
B-06	Blanket	Minor Main Replacement	5,100		et seq.
	Equivalent linear footage:$150 per ft.		20,300	135	

Total Replacement, Ft.:	2,574
Existing Distribution Main, Ft.:	194,303

Total Replacement/Existing Distribution Main:	0.0132
Correction Factor:(1-Tot Replac/ExistDistrMain)	0.9868

For the Test Year 2008, DRA's calculated water loss for the Clearlake CSA is 35.35% compared to GSWC's 47.48%. The 12.13% difference is due to the different methodologies used to arrive at the respective figures. At first, DRA calculated the 5-year average of the last recorded unaccounted water used in operation and unaccounted for water due to leakage, then adjusted these figures with a correction factor by considering the utility's future budgeted projects and blanket items of work to take place in 2007 and 2008. The detailed calculations are described in said Table 2-1 above. GSWC used the 2006 recorded water loss of 47.48%. DRA is troubled by the high unaccounted water loss being experienced by GSWC in its Clearlake district which is unreasonably high compared to the American Water Works Association industry recommended benchmark of 10%.[3] Also, the trend in the unaccounted water has been worsening over time. Unaccounted water has increased from 14.99% in 2002 to 32.75% in 2006.

Through GSWC's response, DRA has found the following historical information regarding GSWC's effort in dealing with Clearlake CSA's water loss:

(a) GSWC planned to bring in a leak detection crew in the late '90's but determined that the dollars could be better spent on replacing waterlines already identified as needing replacement. The number of leaks that surfaced and made themselves known to GSWC were more than could be addressed, thus performing additional leak detection services was deemed unnecessary.

(b) GSWC has planned to reduce the amount of leakages by implementing

[3] AWWA Leak Detection and Water Accountability Committee, " Committee Report: Water Accountability." Journal AWWA (July 1996): 108-111.

a main replacement program that was funded annually to replace deteriorated waterlines and meters. The large amount of capital and potential rate impact it will have on its ratepayers has limited the acceleration of this program. For the last several years, GSWC has been allocating almost half of the entire capital budget to the main replacement program due to significant increase in materials and construction costs —installing 1,500 to 2,000 feet per year in the '90's, and approximately 1,000 feet in '00's.

(c) GSWC has sought outside grants on two separate occasions to assist its main replacement program.

c-1) GSWC approached the Clearlake Fire Department and attempted to strike a deal that would have the fire department sponsor the grant application with GSWC providing the staff and technical services necessary to prepare the grant application. The fire department was initially interested in this proposal but ultimately abandoned it.

c-2) GSWC applied for a grant from the State Revolving Fund for the main replacement. However, the application review committee had chosen other water systems based on their sizes and locations.

(d) The Clearlake CSA's main replacements for the last 5 years, are shown in Table 2-2 below.

Table 2-2 Clearlake CSA Main Replacement

	Location	**Length of**	
	Oak	900	
	Konocti Rd.	20	
	Country Club	703	
	Marin (estimated)	800	
	Sunset (proposed)	1,400	
	Lakeshore	500	

(e) The high percentage of water loss is due to a combination of (1) an

increase in the number of non-surfacing waterline leaks due to the deterioration of waterlines and (2) an increase in the flow rate of the non-surfacing waterline leaks. GSWC has performed meter calibration for all large meters (customer and production meters) and continues to change out defective meters in accordance with Commission requirements.

Based on the above findings, DRA recommends that GSWC should implement a main replacement program that will reduce its water loss to an acceptable level. Funding of such a program may be requested through a special application, or through requests in its next GRC.

GSWC estimated that it would require approximately $27.8 million (at a rate of $150 per foot) to replace all of the aging steel, polyethylene, and asbestos cement mains in the Clearlake CSA system. At this time, GSWC is focusing on replacing steel mains. Assuming, GSWC had to make this level of investment to reduce its unaccounted water loss, the increase in rates for a customer using an average of 7 Ccf of water per monthly will increase from $63.04 to $226.35 (an increase of $163.31 or 259%) at the present tariff rate. Clearly, this level of increase in rates will make water service unaffordable for a majority of the Clear Lake customers. DRA believes that reducing the unaccounted water loss should be done on a gradual basis to minimize any rate shock over time. DRA recommends that the GSWC submit in a separate application a long-term main replacement plan indicating timelines, prioritizing replacements, cost/benefit analysis and expected reductions in unaccounted water loss. In addition, DRA encourages GSWC to evaluate as an option for funding the needed capital expenditures in its Clearlake district the Rate Support Fund adopted for California Water Service's Lucerne service district.[4]

[4] See D.06-08-011, p. 7.

4. Total Water Supply

The total water supply represents the sum of water sales, and water loss. Water sales are calculated by the product of the number of customers and water use. DRA's total water supply estimated for the Test Year 2008 is 288,923 Ccf compared to GSWC's 341,282 Ccf.

GSWC's higher amount of the total water supply is due to its higher water loss estimated for the Test Year 2008 than DRA's.

5. Operating Revenue

Operating revenue is calculated by multiplying the number of customers to applicable water use and to the current tariff rates for the present revenue; and to the proposed rates for the proposed revenue.

DRA's operating revenues are higher than GSWC's because DRA's total water sales amount is higher than GSWC's.

D. CONCLUSION

Upon investigating and analyzing GSWC's requests for the number of customers, water consumption, and revenues, DRA's estimates are just and reasonable for the reasons discussed above. The Commission should adopt DRA's recommendations.

TABLE 2-3				
GOLDEN STATE WATER COMPANY				
Region I- Clearlake				
AVERAGE SERVICES				
2008				
	DRA	Utility	DRA Exceeded GSWC	
Item	Analysis	Estimated	Diff	Percent
	(A)	(B)		
Metered Service:				
Commercial	2,173	2,173	0	0.00%
Industrial	0	0	0	0.00%
Public Authority	2	2	0	0.00%
Irrigation	0	0	0	0.00%
Resale	0	0	0	0.00%
Contract	0	0	0	0.00%
Other	0	0	0	0.00%
Total Metered	2,175	2,175	0	0.00%
Flat Rate				
Commercial	0	0	0	0.00%
Public Authority	0	0	0	0.00%
Private Fire	4	4	0	0.00%
Total Flat Rate	4	4	0	0.00%
Total Average Customers	2,179	2,179	0	0.00%

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TABLE 2-4				
GOLDEN STATE WATER COMPANY				
Region I- Clearlake				
Average consumption per customer				
2008				
	DRA	Utility	DRA Exceeded GSWC	
Item	Analysis	Estimated	Diff	Percent
	(A)	(B)		
Metered Service:				
Commercial	85.9	82.4	3.5	4.25%
Industrial	0.0	0.0	0.0	0.00%
Public Authority	44.6	44.6	0.0	0.00%
Irrigation	0.0	0.0	0.0	0.00%
Resale	0.0	0.0	0.0	0.00%
Contract	0.0	0.0	0.0	0.00%
Other	0.0	0.0	0.0	0.00%
Flat Rate				
Commercial	0.0	0.0	0.0	0.00%
Public Authority	0.0	0.0	0.0	0.00%
Private Fire	0.0	0.0	0.0	0.00%

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TABLE 2-5				
GOLDEN STATE WATER COMPANY				
Region I- Clearlake				
OPERATING REVENUES				
Test Year 2008				
(at Present Rates)				
Item	DRA	GSWC	DRA Exceeded GSWC	
	(A)	(B)	Diff.	%
	(Dollars in Thousands)			
Metered Service:				
Commercial	1,672.6	1,642.1	31	1.86%
Industrial	0.0	0.0	0	0.00%
Public Authority	1.2	1.2	0	0.00%
Irrigation	0.0	0.0	0	0.00%
Resale	0.0	0.0	0	0.00%
Contract	0.0	0.0	0	0.00%
Other	0.0	0.0	0	0.00%
Total Metered	1,673.8	1,643.3	31	1.86%
Flat Rate				
Commercial	0.0	0.0	0	0.00%
Public Authority	0.0	0.0	0	0.00%
Private Fire	1.3	1.3	0	0.00%
Total Flat Rate	1.3	1.3	0	0.00%
Public Fire				
Miscellaneous				
Misc. Service	4.5	4.5	0	0.00%
Rent	0.0	0.0	0	0.00%
Other	0.1	0.1	0	0.00%
Revenue Accrued	0.0	0.0	0	0.00%
Supply Bal. Accts	0.0	0.0	0	0.00%
Total Misc.	4.6	4.6	0	0.00%
Total Operating Revenue	1,679.7	1,649.2	31	1.85%

Table 2-6				
GOLDEN STATE WATER COMPANY				
Region I- Clearlake				
TOTAL CONSUMPTION AND SUPPLY				
(CCF PER YEAR - 2008)				
	DRA	Utility	DRA Exceeded GSWC	
Item			Amount	Percent
	(A)	(B)		
Metered Service Sales:				
Commercial	186,725.9	179,142.1	7,583.8	4.23%
Industrial	0.0	0.0	0.0	0.00%
Public Authority	89.2	89.2	0.0	0.00%
Irrigation	0.0	0.0	0.0	0.00%
Resale	0.0	0.0	0.0	0.00%
Contract	0.0	0.0	0.0	0.00%
Other	0.0	0.0	0.0	0.00%
Total Metered	186,815.1	179,231.3	7,583.8	4.23%
Flat Rate Sales				
Commercial	0.0	0.0	0.0	0.00%
Public Authority	0.0	0.0	0.0	0.00%
Private Fire	2.4	0.0	2.4	
Total Sales	186,817.5	179,231.3	7,586.2	4.23%
Unacct For (% of supp	74,224.0	111,783.1	-37,559.1	-33.60%
Used in Operations	27,881.0	50,267.2	-22,386.2	-44.53%
Total Supply Forecast	288,922.5	341,281.6	-52,359.1	-15.34%

CHAPTER 3 EXPENSES

A. INTRODUCTION

This Chapter sets forth the analyses and recommendations of DRA for operating expenses. DRA's review is based on GSWC's application, testimonies, work papers, Region I Headquarter and District Office, interviews of GSWC employees, and GSWC data responses.

B. SUMMARY OF RECOMMENDATIONS

DRA recommends $777,700 in operating expenses for Test Year 2008. GSWC's proposed amount is $871,500. DRA's estimate is $93,800 less, because DRA applied escalation rates, assumptions, and methodologies that are different from GSWC's.

Table 3-1 of this chapter compares DRA's recommended and GSWC's proposed estimates of operating expenses.

C. DISCUSSION

Table 3-1 shows line item expenses recommended by DRA and compare them with those requested by GSWC. Following this is the discussion of each expense estimate listed.

Table 3-1		
Region 1 Clearlake		
Test Year 2008		
(Dollars in Thousands)		
	DRA	GSWC
Purchased Water	$ 24.7	$ 30.3
Purchased Power	78.2	92.4
Chemicals	36.1	43.2
Allocated Common Cust Acct-GO	9.9	14.6
Uncollectibles 0.460%	7.9	8.7
Operation Labor	207.9	207.9
Other Operation Expenses	89.7	89.7
Total Operation Expenses	454.4	486.8
Maintenance Labor	35.8	35.8
Other Maintenance Expenses	43.8	43.8
Total Maintenance Expenses	79.6	79.6
Office Supplies & Expenses	39.6	39.6
Injuries and Damages	0.1	0.1
Pension and Benefits	4.2	4.2
Business Meals	0.3	0.3
Regulatory Expenses	8.1	9.7
Outside Services	2.2	2.2
Miscellaneous	0.6	0.6
Allocated General Office	110.6	162.1
Allocated Region Office	32.3	35.7
Allocated District Office	15.2	20.1
Other Maint. Of Gen. Plt	1.6	1.6
Rent	12.4	12.4
A&G Labor	16.5	16.5
Total A&G Expenses	243.7	305.1
Total O&M & A&G	$ 777.7	$ 871.5

1. Escalation Factors

GSWC used the escalation factors established by the DRA Energy Cost of Service Branch memorandum dated the October 31, 2006. GSWC applied other factors to determine the future amounts of labor expenses. GSWC also applied a customer growth escalation factor to forecast certain Test Year expenses.

DRA recommends using the most recent escalation factors provided in the DRA Energy Cost of Service Branch, Escalation Memorandum dated February 28,

2007, which is reflected in DRA's estimates. Below DRA analyzes and recommends amounts different than those proposed by GSWC. DRA also applied a customer growth escalation factor to forecast Test Year expenses.

2. Operation Expenses

a) Purchased Water

DRA recommends $24,700 and GSWC requests $30,300 for purchased water expenses in Test Year 2008. DRA's estimate is $5,600 lower than GSWC proposal, due to a lower level of water supply and sales numbers provided by DRA revenue witness. The water supply and sales number are found at Chapter 2 in this report.

DRA and GSWC applied the same rate for purchased water to determine their estimate for purchased water expenses.

b) Purchased Power

DRA recommends $78,200 and GSWC requests $92,400 for purchased power expenses in Test Year 2008. DRA's estimate is $14,200 lower than GSWC proposal, due to a lower total production quantity numbers provided by DRA revenue witness. The total production numbers are found at Chapter 2 in this report.

Both DRA and GSWC used the same unit of kilowatt hours per production and the same cost per kilowatt hours.

c) Chemicals

DRA recommends $36,100 and GSWC requests $43,200 for chemicals expenses in Test Year 2008. DRA's estimate is $7,100 lower than GSWC proposal, due to a lower total production quantity numbers provided by DRA revenue witness and difference in unit cost per acre foot. The total production numbers are found at Chapter 2 in this report.

GSWC requested a $55.12 per acre foot unit cost. GSWC uses an inflated adjusted five-year average unit cost to 2006 dollars and applied an escalation

factor to the adjusted average number to develop the unit cost for 2007; and applied the escalation factor to the unit cost of 2007 to develop its estimate for Test Year 2008.

DRA uses the same methodology to develop its unit cost estimate of $54.40 per acre foot for Test Year 2008. It appears that the different publication of the escalation factors may attribute to the differences in estimates.

d) Various Allocated Expenses

The data for the various allocated expenses stated below are provided in a separate report and discussed by the DRA Regional witness:

- The Allocated Common Customer Accounts-General Office;
- The Allocated General Office Expenses;
- The Allocated Regional Office Expenses; and
- The Allocated District Office Expenses.

e) Uncollectible

DRA recommends the same percentage rate of 0.46% requested by GSWC for uncollectible expenses.

f) Operation Labor Expenses

The discussion below analyzes the labor expenses in Operation, Maintenance, and Administrative and General.

DRA recommends the same level of expenses of $207,900 requested by GSWC for operation labor in Test Year 2008.

DRA recommends the same level of expenses of $35,800 requested by GSWC for maintenance labor in Test Year 2008.

DRA recommends the same level of expenses of $16,500 requested by GSWC for administrative and general labor in Test Year 2008.

g) Other Operation Expenses

DRA recommends the same level of expenses of $89,700 requested by GSWC for other operation in Test Year 2008.

3. Maintenance Expenses

a) Maintenance Labor

Refer to Paragraph 2 Operation Expense, (f) Operation Labor above for discussion on labor expenses.

b) Other Maintenance Expenses

DRA recommends the same level of expenses of $43,800 requested by GSWC for other maintenance in Test Year 2008.

4. Administrative and General Expenses

a) Office Supplies and Expenses

DRA recommends the same level of expenses of $39,600 requested by GSWC for office supplies and expenses in Test Year 2008.

b) Injuries and Damages

DRA recommends the same level of expenses of $100 requested by GSWC for injuries and damages in Test Year 2008.

c) Pension and Benefits

DRA recommends the same level of expenses of $4,200 requested by GSWC for pension and benefits in Test Year 2008.

d) Business Meals

DRA recommends the same level of expenses of $300 requested by GSWC for business meals in Test Year 2008.

e) Regulatory Commission Expense

DRA recommends $24,300 or a yearly amortized amount of $8,100 for three years in regulatory commission expense. GSWC requests $29,100 or a yearly amortized amount of $9,700 for three years in regulatory commission expense. DRA recommendation makes a reduction of $4,800 or a yearly amount of $1,600 from GSWC's proposed amount. Table 3-2 depicts the expense activity for the last general rate case, which DRA uses to forecast Test Year 2008 expenses.

Table 3-2
Region I Clearlake CSA
Test Year 2008
(Dollars in Thousands)

		2005	2006	2007	DRA	GSWC
D.05-05-025	Adopted	$ 11.8	12.0	12.3		
	Recorded	1.1	2.6	12.3		
	Total Regulatory Expense				24.2	29.1
	Yearly Expense-3 years				8.1	$ 9.7

GSWC uses its last general rate case expenses for Region II, A.06-02-023, as a proxy to estimate Region I's regulatory commission expense for Test Year 2008. As of date, the Commission has not issued a final decision on A.06-02-023. It is to be noted that A.06-02-023 also addressed GSWC's General Office request to increase its revenue requirements.

DRA uses an inflated adjusted sum of recorded expenses for three years to 2007 dollars, assuming that GSWC will record the same amount of expenses adopted for 2007; applied an escalation factor to the adjusted sum number to develop the estimate for 2008; and added the estimated expenses for mailing cost, publishing cost, and miscellaneous expenses to the 2008 expenses to develop the expenses for Test Year 2008. DRA has increased the postage rate from 39 cents to 42 cents for mailing cost in anticipation of an increase in May 2007.

f) Outside Services

DRA recommends the same level of expenses of $2,200 requested by GSWC for outside services in Test Year 2008.

g) Miscellaneous

DRA recommends the same level of expenses of $600 requested by GSWC for miscellaneous in Test Year 2008.

h) Other Maintenance-General Plant

DRA recommends the same level of expenses of $1,600 requested by GSWC for other maintenance-general plant labor in Test Year 2008.

i) Rent

DRA recommends the same level of expenses of $12,400 requested by GSWC for rent in Test Year 2008.

j) Administrative and General Labor Expense

Refer to Paragraph 2 Operation Expense, (f) Operation Labor above for discussion on labor expenses.

CHAPTER 4 PLANT IN SERVICE

A. INTRODUCTION

This Chapter sets forth the analyses and recommendations of DRA for Plant in Service in the Clearlake CSA with approximately 2,124 customers. DRA's recommendations are based on GSWC's application, testimonies, supporting work papers, discussions with GSWC employees, e-mail from GSWC, and GSWC data responses.

B. SUMMARY

GSWC requests plant additions of $424,800 for 2007, $413,300 for Test Year 2008 and $421,100 for Test Year 2009, whereas DRA recommends plant additions of $211,200 in 2007, $356,400 in Test Year 2008 and 242,900 in Test Year 2009.

In addition to differences in plant additions, DRA will present different recommendations concerning GSWC's partnership with engineering firm CH2MHill, GSWC's Overhead Rate, and GSWC's planned and unplanned project Contingency adder.

C. DISCUSSION

1. Clearlake CSA Plant Additions

For the purposes of this report, DRA presents its analysis and recommendations for 2007, Test Year 2008 and Test Year 2009 separately.

2. 2007 Capital Additions

The following table illustrates GSWC's requested plant additions for 2007 and DRA's recommendation. DRA has performed its own independent analysis of all proposed projects and estimated funding requested by GSWC. Capital projects and project estimates that have been accepted by DRA are so indicated in the table. DRA will not offer discussion of those projects and estimates in this report. Discussion concerning projects for which DRA recommends a different result or Capital Projects that DRA recommends the Commission disallow will follow the

Table 4-1.

Clearlake Capital Budget for 2007

DESCRIPTION	GSWC	DRA	DIFFERENCE	% DIFFERENCE
Major Projects				
Misc. Bowl Replacement	11,000	0	-11,000	-100%
Misc Street Improvements	5,000	0	-5,000	0%
Marin - Main between 3671 Marin and 3891 Marin	170,000	143,000	-27,000	-16%
Master Plan	159,000	0	-159,000	-100%
SCADA	21,000	18,000	-3,000	-14%
Contingency	5,000	2,000	-3,000	-60%
New Business Funded by GSWC	5,000	5,000	0	0%
Total Major Projects	$376,000	$168,000	-208,000	-55%
Blanket Projects				
Meters	9,700	8,500	-1,200	-12%
Services	19,300	17,100	-2,200	-11%
Minor Main Replacement	6,800	6,000	-800	-12%
Minor Pumping Plant Equipment	1,900	1,700	-200	-11%
Minor Purification Equip/Structures	1,000	900	-100	-10%
Replace Turbidimeter (2)	5,300	4,700	-600	-11%
Office Furniture and Equipment	4,800	4,300	-500	-10%
Misc. Tools and Safety Equipment	0	0	0	0%
Total Blanket Projects	$48,800	$43,200	-5,600	-11%
Total Capital Budget	**$424,800**	**$211,200**	**-213,600**	**-50%**

**All estimates include DRA's recommended Contingency and Overhead Rate which are lower than GSWC's request. DRA's discussion of the Contingency and Overhead Rate is presented at the end of this chapter.*

1) Miscellaneous Bowl Replacements

GSWC requests $11,000 in 2007 for Miscellaneous Bowl Replacements. According to GSWC, this is for the emergency replacement of pumps and motors as well as column extension, which may routinely occur. GSWC's witness Ernest Gisler states that GSWC's estimate was derived by trending past expenditures for this type of project.

DRA recommends a different amount of $0. DRA's estimate is based on GSWC's historical expenditure for this category. In DRA's Master Data Request submitted to GSWC, DRA requested GSWC's five-year authorized budget and

recorded expenditures for all major and routine plant items. GSWC responded to DRA's request by providing the company authorized budgeted amount for just three years, 2000 through 2002. According to GSWC, budget amounts for 2003 through 2006 were not available because the company was not afforded a full rate case proceeding in 2004[5]. Although GSWC was not afforded the full benefit of a GRC in 2004, the company did receive an adjustment in rates. DRA is also troubled that the company management failed to prepare a capital budget in 6 years, a common best management practice for running any business. According to GSWC's Budget Monitoring record, funds budgeted for years 2001 and 2002 were deferred to other projects. In response to a subsequent data request, GSWC did provide DRA with the recorded expenditures for 2003 through 2006. The following table illustrates the budgeted amounts compared to the actual expenditures for the past seven-year period.

[5] GSWC filed a Notice of Intent to increase rates in January 2004. While the NOI was pending, the Commission issued R03-09-005 that deferred the filing of SCWC's Region I GRC from January 2004 to a later date to be determined. Subsequently, the Commission issued D04-06-018 which adopted the New Rate Case Plan requiring each Class A utility to submit its GRC applications according to a specified schedule. That schedule deferred SCWC's next GRC filing for Region I from January 2004 to January 2007. However, to lessen any hardship caused by the deferral the Commission ordered ORA and SCWC to devise and implement a mutually agreeable rate adjustment plan to transition Region I to the new rate case plan schedule. Decision 05-05-025 was issued in May 2005, which resulted in rate increases for SCWC's Region I. Bay Point's rates were increased 1.9% in 2005, 2.5% in 2006, and 2.5% for 2007.

Table 4-2

Miscellaneous Bowl Replacements[6]

Year	Budgeted Amt.	Year	Recorded
2000	$0	2000	$0
2001	$5,000	2001	$0
2002	$5,000	2002	$0
2003	Not available	2003	$0
2004	Not available	2004	$0
2005	Not available	2005	$0
2006	Not available	2006	$0
		5-yr Avg.	$0

It is clear that GSWC has not used budgeted funds for the purpose intended nor has the company experienced the need for "emergency" replacement of these facilities. Based on the information provided it is evident that GSWC has not found the need to make replacements of the equipment and facilities included in this budget group. GSWC claims that the methodology used to determine its estimate was trending of past expenditures. However, GSWC has not provided any support for the estimate.

3. Miscellaneous Street Improvements

GSWC requests $5,000 in 2007 for Miscellaneous Street Improvements. The projects that come under this category are routine in nature. The purpose of this budget item is to replace valve boxes and other water appurtenances associated with City or County roadway widening, drainage improvement and other projects where utility facilities are in the City or County right-of-way. GSWC claims that its estimate was determined by trending past expenditures.

DRA recommends $0 for this project. As shown in the following table, GSWC has not budgeted funds for this project category nor has it expended any funds for this project within the past 7-years. . Based on the information provided, it is evident that GSWC has not been required to replace equipment and

[6] GSWC response to DRA Data Request PXS 021, PXS 021-S

facilities included in this budget group. GSWC claims that the methodology used to determine its request was by trending of past expenditures. However, GSWC has not provided any support for the estimate.

Table 4-3

Miscellaneous Street Improvements

Year	Budgeted Amt.	Year	Recorded
2000	$0	2000	$0
2001	$0	2001	$0
2002	$0	2002	$0
2003	Not available	2003	$0
2004	Not available	2004	$0
2005	Not available	2005	$0
2006	Not available	2006	$0
		5-yr Avg.	$0

4 Marin Street – Main Replacement

GSWC requests $170,000 in 2007 to install 800-feet of 8-inch pipe to replace an old, leaky, 2-inch steel main. DRA performed its own analysis and recommends $143,000. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

5. Master Plan

In 2007, GSWC requests recovery of $159,000 in expenses for developing its Master Plan GSWC contracted with engineering firm CH2MHILL to complete Master Plans for all Region I service areas. GSWC represents that the Master Plans require a highly detailed analysis of the system, including water supply reliability, distribution, storage, and water quality as it relates to anticipated demands within the system. According to GSWC's plant witness, Ernest Gisler,

> The analysis will include the utilization of our existing extended period hydraulic model of the system as a means to identify hydraulic constraints and potential areas in which water aging may lead to water quality issues. The Master Plan will project out ten years into the future and will identify and prioritize improvement projects to ensure continued water quality and service. The Master Plan will be the road map we will use as

> the basis for future capital budgets and it will be updated periodically to ensure system trends are being addressed.[7]

DRA maintains that GSWC's engineering and operations staff should have a thorough, first-hand knowledge of the water system and any needs or deficiencies that may exist since the act of running the system on a day to day basis would automatically provide such knowledge. GSWC's engineering staff has performed a detailed analysis of the system in the past. The most recent Master Plan completed in 1999 was done in-house.

In discussions between DRA and the utility, the company stressed that the Master Plan is a living document upon which future Master Plan(s) may rely. DRA agrees and consequently, GSWC should have little, if any, problem in developing a new Plan, such as by utilizing the existing 1999 Master Plan as the basis for appropriate updates or changes.

GSWC has provided no proof justifying the need to hire an outside consultant as reasonable. While admittedly that during the last 10-years some regulatory requirements may have changed requiring additional analysis and consideration, GSWC has not shown that its own engineering staff were not informed of these changes and could not incorporate them into the 1999 or subsequent Master Plans. Presumably, a Class A water utility such as GSWC should have the expertise and resources to project future needs and to prepare the necessary models.

In GSWC's General Rate Case application for Region III, A. 05-02-004, GSWC made a similar claim that an outside consultant (CH2MHill) was needed to prepare its Urban Water Management Plan. DRA opposed that request for the same reasons that DRA now opposes this request concerning the Master Plan. As in A. 06-02-023, GSWC also in this matter fails to prove that it lacks the ability

[7] Golden State Water Company, Prepared Testimony of Ernest A. Gisler, p. 16.

and/or resources to develop its Master Plan in-house. In D06-01-025, the Commission denied GSWC's request and should also reject this similarly unjustified and unreasonable request.[8]

6. SCADA – Wonderware

GSWC requests $21,000 in 2007 to purchase and install SCADA software to replace existing software that is no longer supported. DRA recommends $18,000. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

7. Blanket Budget

GSWC's Blanket Budget includes routine items necessary to operate and maintain the water system; such as replacement of meters due to age or operational deficiencies, services, minor main replacement, miscellaneous tools and equipment, and replacement of service vehicles.

GSWC requests a total $48,800 in 2007 for the Blanket Budget. DRA has performed its own analysis and recommends $43,200. DRA's recommendation includes DRA's lower Overhead Rate.

8. Contingency for Blanket Projects

In 2007, GSWC requests 10% as Contingency for both major stand-alone projects and the Blanket Projects. In its work papers, GSWC specifically noted the contingency amount for its Blanket Projects and identified the contingency for Blanket Projects separately in the Capital Budget. The amount requested for Blanket Projects in 2007 is $5,000.

DRA recommends $2,000. DRA disagrees with GSWC on the 10% contingency rate and instead recommends a 5% contingency for both the major stand-along projects and the Blanket Budget items. GSWC has not provided any support for its estimate of 10% for Contingency. DRA objected to GSWC's

[8] D.06-01-025, Section 5.7, concerning GSWC's request for an outside consultant to prepare its Urban Water Management Plan.

request for 10% Contingency in GSWC's GRC for Region III. In D06-01-025, the Commission agreed that the company failed to provide support for its request of 10% Contingency. For example, GSWC does not appear to have used preventative maintenance to eliminate or reduce the number of emergency repairs. Nor has GSWC demonstrated any cost management procedures that would render more accurate project management and cost estimations. Further, as in A. 05-02-004, GSWC's GRC for Region III, when GSWC failed to justify its request for 10% Contingency, in this matter GSWC also fails show that typical cost overruns or unanticipated projects amount to 10% or more of the Capital Budget.

a. 2008 Capital Additions

For Test Year 2008, GSWC request a total Capital Budget of $413,300, whereas DRA recommends a total Capital Budget of $356,400. The following table illustrates GSWC's requested Capital Budget and DRA's recommended Capital Budget. Capital Projects and project estimates that have been accepted by DRA are so indicated and DRA will not offer discussion of those projects and estimates in this report. Discussion concerning projects for which DRA recommends a different result or Capital Projects that DRA recommends the Commission disallow will follow the Table 4-4.

Table 4-4

Clearlake Capital Budget for Test Year 2008

DESCRIPTION	GSWC	DRA	DIFFERENCE	% DIFFERENCE
Major Projects				
Sonoma WTP Replace Air Compressor	28,000	25,000	-3,000	-11%
Sonoma WTP Replace Air Dryer	28,000	25,000	-3,000	-11%
Misc Bowl Replacement	6,000	0	-6,000	-100%
Misc Street Improvements	6,000	0	-6,000	-100%
Sunset Ave b/w West 40th and Davis	312,000	277,000	-35,000	-11%
Contingency	3,000	1,000	-2,000	-67%
New Business Funded by GSWC	5,000	5,000	0	0%
Total Major Projects	$388,000	$333,000	-55,000	-14%
Blanket Projects				
Meters	5,100	4,700	-400	-8%
Services	10,100	9,400	-700	-7%
Minor Main Replacement	5,100	4,700	-400	-8%
Minor Pumping Plant Equipment	2,000	1,900	-100	-5%
Minor Purification Structures	1,000	900	-100	-10%
Office Furniture and Equipment	1,000	900	-100	-10%
Misc. Tools and Safety Equipment	1,000	900	-100	-10%
Total Blanket Projects	$25,300	$23,400	-1,900	-8%
Total Capital Budget	**$413,300**	**$356,400**	**-56,900**	**-14%**

**All estimates include DRA's recommended Contingency and Overhead Rate which are lower than GSWCs request. DRA's discussion of the Contingency and Overhead Rate is presented at the end of this chapter.*

1) Sonoma Water Treatment Plant – Replace Air Compressor

In Test Year 2008, GSWC requests $28,000 to replace an existing air compressor with a large volume air compressor to provide air supply required to operate and manipulate pneumatically controlled valves. DRA has preformed its own analysis and recommends $25,000. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

2) Sonoma Water Treatment Plant – Replace Air Dryer

For Test Year 2008, GSWC requests $28,000 to replace the air dryer required to remove water from compressed air to prevent the accumulation of water in airlines and pneumatic controllers which could damage the equipment.

DRA has preformed its own analysis and recommends $25,000. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

3) Misc Bowl Replacements

For Test Year 2008, GSWC requests $6,000 for this project category. DRA recommends a different amount of $0. As indicated in the previous section for 2007, DRA's analysis of GSWC's budget and expenditures for this budget category shows that GSWC has budgeted and spent zero dollars on projects of this nature. GSWC claims that its estimate was based on trending past expenditures. GSWC has provided no support for its estimate.

4) Misc. Street Improvements

For Test Year 2008, GSWC requests $6,000 for this routine category. DRA recommends $0. As indicated in the previous section concerning 2007, DRA's analysis of GSWC's budget and expenditures for this budget category shows that GSWC has budgeted and spent zero dollars on projects of this nature. GSWC claims that its estimate was based on trending past expenditures. GSWC has provided no support for its estimate.

5) Sunset Ave - Main Replacement

GSWC requests $312,000 in Test Year 2008 to replace 1,400 feet of leaky main. Due to the high number of leaks in this main, the age of the main and the high water loss within this CSA, DRA recommends that this project be authorized. However, DRA recommends $277,000. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

6) Blanket Budget

GSWC requests $25,300 in Test Year 2008 to cover the routine plant operation and maintenance projects including; replacement of meters, services, minor main replacement, office furniture, and miscellaneous tools and equipment. DRA has performed its own analysis and recommends $23,400. DRA's recommendation includes DRA's lower Overhead Rate.

7) Contingency for Blanket Projects

GSWC requests $3,000 or 10% of its Blanket Budget for Test Year 2008, as Contingency to fund unforeseen cost overruns or unanticipated projects.

DRA recommends a 5% Contingency or $1,000 for Blanket Budget projects. Again, GSWC has not provided any support for its estimate of 10% for Contingency. DRA objected to GSWC's request for 10% Contingency in GSWC's GRC for Region III. In D06-01-025, the Commission agreed that the company failed to provide support for its request of 10% Contingency. For example, GSWC does not appear to have used preventative maintenance to eliminate or reduce the number of emergency repairs. Nor has GSWC demonstrated any cost management procedures that would render more accurate project management and cost estimations. Further, as in A. 05-02-004, GSWC's GRC for Region III, when GSWC failed to justify its request for 10% Contingency, in this matter GSWC also fails show that typical cost overruns or unanticipated projects amount to 10% or more of the Capital Budget.

Since there is no support for the use of a 10% adder, DRA recommends that the Contingency adder be consistent with that that was approved in D.06-01-025 for GSWC's Region III.

c. 2009 Capital Additions

For Test Year 2009, GSWC requests a total Capital Budget of $421,100, whereas DRA recommends a total Capital Budget of $242,900. The following table illustrates GSWC's requested Capital Budget and DRA's recommendation. Capital Projects and project estimates that have been accepted by DRA are so indicated in the table and DRA will not offer discussion of those projects and estimates in this report. Discussion concerning projects for which DRA recommends a different result will follow the Table 4-5.

Table 4-5

Clearlake Capital Budget for Test Year 2009

DESCRIPTION	GSWC	DRA	DIFFERENCE	% DIFFERENCE
Major Projects				
Lakeshore Plant - Intake Strainer	117,000	0	-117,000	-100%
Sonoma WTP - GAC Changeout	47,000	41,000	-6,000	-13%
Miscellaneous Bowl Replacement	12,000	0	-12,000	-100%
Misc Street Improvements	12,000	0	-12,000	-100%
Lakeshore Drive Main Replacement	117,000	101,000	-16,000	-14%
Contingency	11,000	5,000	-6,000	-55%
New Business Funded by GSWC	5,000	5,000	0	0%
Total Major Projects	$321,000	$152,000	-169,000	
Blanket Projects				
Meters	10,700	9,700	-1,000	-9%
Services	16,000	14,500	-1,500	-9%
Minor Main Replacement	21,300	19,300	-2,000	-9%
Minor Pumping Plant Equipment	2,100	1,900	-200	-10%
Minor Purification Structures	1,100	1,100	0	0%
Office Furniture & Equipment	5,300	4,800	-500	-9%
Vehicle Replacement	41,500	37,700	-3,800	-9%
Miscellaneous Tools and Equipment	2,100	1,900	-200	-10%
Total Blanket Projects	$100,100	$90,900	-9,200	-9%
Total Capital Budget	**$421,100**	**$242,900**	**-178,200**	**-42%**

**All estimates include DRA's recommended Contingency and Overhead Rate which are lower than GSWC's request. DRA's discussion of the Contingency and Overhead Rate is presented at the end of this chapter.*

1) Lakeshore Plant – Intake Strainer

GSWC requests $117,000 in Test Year 2009 to install an intake strainer at its Lakeshore Plant. At the Lakeshore Plant, GSWC uses booster pumps to covey raw water to the Sonoma Water Treatment Plant for treatment and distribution to customers. According to GSWC, the raw water pumps are fitted with stainless steel debris screens which are approximately six feet below the normal water surface of Clear Lake. The intake strainer would be used to provide a self cleaning process to prevent plants, debris, and algae from clogging the booster pump screens and then reaching the treatment plant. According to GSWC, the problem with debris and algae reaching the Sonoma plant through the booster pumps has increased over time and is an ongoing operational problem. GSWC's

witness, Ernest Gisler, states in his testimony;" Operators are now required to shut down the Lake Shore Plant and Sonoma WTP to manually clean the intake screens."[9]

DRA recommends that this project be disallowed. DRA visited the Lakeshore Plant intake and Sonoma Treatment Plant in February 2007. DRA did not view any excessive debris or algae at either the point of intake or at the Sonoma WTP. During DRA's field visit, DRA asked the company's representatives how often GSWC is required to clean the intake screens and whether any analysis had been done to determine whether there would be any savings in the treatment of water with installation of the self-cleaning intake strainer. GSWC's representative stated that the screens are not being cleaned and no analysis was done to determine whether any savings would be achieved.

In an attempt to reconcile Mr. Gisler's testimony that operators are required to shut down the plant to manually clean the intake screens with the answer received during the field visit, DRA sent data request PXS-018 on March 9, 2007, wherein DRA requested a record of any scheduled or unscheduled events when it was necessary to shut down the plant in order to clean the existing intake screens.[10] GSWC's response was that the intake screen size was changed to a larger mesh size in 1992 in order to prevent clogging or plugging.[11] After the change in screen mesh size in 1992, there is no record of plant shut down due to plugging or clogging of the intake screen. According to GSWC's response to DRA's Data Request, the only issue that remained after the mesh size was changed is that algae and small solids can still get through the screens and reach the treatment plant. DRA argues that GSWC's claim of debris plugging the intake screens is not supported as revealed in GSWC's response to DRA data request

[9] Prepared Testimony of Ernest Gisler, p. 51.

[10] DRA data request PXS-018.

[11] GSWC response to Data Request PXS 018, dated March 10, 3007.

PXS-018. GSWC has not proved that algae and small debris which may reach the treatment plant where the raw water is treated is a critical problem. Any algae and debris that reaches the treatment plant should continue to be removed through the treatment processes already in place. The addition of plant projects to resolve potential problems that are currently being addressed by methods already in place unnecessarily increases the burden on rate payers.

2) Sonoma Water Treatment Plant – GAC Change out

GSWC request $47,000 in Test Year 2009 to replace Granular Activated Carbon (GAC) that will be at the end of its useful life in 2009. DRA has performed its own analysis and recommends $41,000. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

3) Miscellaneous Bowl Replacements

For Test Year 2009, GSWC requests $12,000 for this project category. DRA recommends a different of $0. As indicated in the previous section for 2007, DRA's analysis of GSWC's budget and expenditures for this budget category shows that GSWC has budgeted and spent zero dollars on projects of this nature. GSWC claims that its estimate was derived by trending past expenditures. GSWC has provided no support for its estimate.

4) Misc. Street Improvements

For Test Year 2009, GSWC requests $12,000 for this routine category. DRA recommends a different amount of $0. As indicated in the previous section for 2007, DRA's analysis of GSWC's budget and expenditures for this budget category shows that GSWC has budgeted and spent zero dollars on projects of this nature. GSWC claims that its estimate was derived by trending past expenditures. GSWC has provided no support for its estimate.

5) Blanket Budget

GSWC requests $100,100 in Test Year 2009 to cover the routine plant operation and maintenance projects including; meters, services, minor main replacement, furniture and equipment, and miscellaneous tools and safety equipment.

DRA has performed its own analysis and recommends $90,900. DRA's recommendation includes DRA's lower contingency and Overhead Rate.

6) Contingency

GSWC requests $11,000 or 10% of the Blanket Budget as Contingency in Test Year 2009, for unexpected capital expenditures and to fund unforeseen cost overruns.

DRA recommends 5% contingency or $5,000. GSWC has not provided any support for its estimate of 10% for Contingency. DRA objected to GSWC's request for 10% Contingency in GSWC's GRC for Region III. In D06-01-025, the Commission agreed that the company failed to provide support for its request of 10% Contingency. For example, GSWC does not appear to have used preventative maintenance to eliminate or reduce the number of emergency repairs. Nor has GSWC demonstrated any cost management procedures that would render more accurate project management and cost estimations. Further, as in A. 05-02-004, GSWC's GRC for Region III, when GSWC failed to justify its request for 10% Contingency, in this matter GSWC also fails show that typical cost overruns or unanticipated projects amount to 10% or more of the Capital Budget.

CH2MHILL PARTNERSHIP[12]

DRA is opposed to GSWC ongoing partnership with CH2MHIll. In this rate case, GSWC has formed a partnership with this firm to develop and prepare

[12] DRA testimony concerning CH2M Hill partnership was prepared jointly by Mehboob Aslam
(continued on next page)

its Master Plans for all of its Northern and Coastal District CSA's, perform design and design-build tasks for all of the major Water Supply and Distribution projects, and develop project costs for all projects excluding pipeline projects within its application. According to GSWC's witness, Ernest Gisler, GSWC will likely retain CH2MHILLto continue assisting in the implementation of its 2008 and 2009 capital projects.[13]

Upon reviewing GSWC's testimony, DRA has serious reservations about the justification provided by the company that this partnership will alleviate the backlog of capital projects company-wide, provide the needed resources necessary to handle the engineering workload and provide efficiency in the form of cost savings to ratepayers. DRA request the Commission to review the synergy of this partnership carefully as it not only will have deep financial implication on Region I capital projects, but also on other capital projects in the company's Region I and Region II service territories.

Following is a list of the issues regarding this partnership:

- **Need for the Partnership with CH2MHILL:** In DRA's Data Request, AMX-32, GSWC provided a historical background of forming such partnership with CH2M Hill. In doing so, GSWC re-submitted the excerpts of the testimony of David Chang, Engineering and Planning Manager of Region II, in the previous Region II GRC proceedings, A.06-02-023. In that proceeding, Mr. Chang justified the need for such a partnership based on the following reasons:

- **Heavy Workload:** In addition to $30 million of capital improvements each year, there have been higher volumes of new

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and Patricia Esule.

business projects (budget Group 60)...The total number of new business projects applications totaled more than 164 from January 2003 through September 2005. That is an increase of 52% when compare to the total of new business project applications of 108 form 2000 to 2002.

- **Stringent local permit requirement:** Many local cities are imposing more stringent Conditional Use Permit requirements on local projects. These requirements have prolonged permitting process, caused delay or stoppage of projects, and caused significant cost increases.

- **Increase in construction costs:** Due to the expansion in construction sector in the US and overseas, specifically in China and India, there have been significant increases in construction material costs and construction labor cost. There has been global shortage of construction raw material such as concrete and steel…these increase in construction costs ahs caused project budget overruns and deferral of projects.

- **Staff Shortage:** Despite its aggressive recruiting efforts GSWC had difficulty in hiring qualified engineering staff…staff shortage has further increased the need to rely on outside engineering resources to complete projects.

Upon reviewing GSWC's justification, DRA disagrees with each of the above reasons. GSWC's so called heavy workload is attributed mainly to an increase in new business applications. Since new businesses' capitals are generally

(continued from previous page)
[13] Prepared Testimony of Ernest Gisler, A 06-01-009 thru A-06-01-015, pgs 3-5.

funded by the contractors or developers in the form of contributions and advances, which are considered revenue neutral, DRA believes that the hiring of CH2MHILLshould also be revenue neutral and should not burden the existing ratepayers. However, this is not the case in this partnership. DRA finds that CH2MHILLis intimately involved with each of the company-funded capital projects that have an impact on the revenue, which eventually have to be shouldered by GSWC's ratepayers.

GSWC's second claim that such partnership is needed to meet the ever stringent local permitting requirement. DRA finds it to be baseless. DRA believes that the same permitting requirement on GSWC is equally applicable to any outside consultant such as CH2M HILL. Hiring CH2MHILL is not likely to bypass or shortcut the permitting process required by the local agency. Rather, DRA believes that better time management and planning should help the company to deliver its projects in a more timely fashion. In addition, these permits are also required for new business applications and once again any planning to deal with them should not affect ratepayers.

DRA finds GSWC's third justification that there have been significant increases in construction material cost and construction labor cost as lacking in support. The increase in construction cost affects everyone in the construction business, including CH2MHILL DRA finds it difficult to see the hiring of CH2MHILL could provide cost savings on construction costs. On the contrary, DRA finds that the extra layer of CH2MHILL has increased the cost of a typical capital project. For example, CH2MHILL adds at least 10% of the total cost of capital projects as its profit and an additional 10% is applied for CH2MHILL's contingencies. DRA believes that GSWC can mitigate its cost overruns by improving its cost estimation techniques and employing cost management planning. For example, utilization of real-time cost data and maintaining a company-wide cost data base coupled with management accountability would be a good place to start.

GSWC's final justification that there is staff shortage is also unsupported. On more than one occasion, the Commission noticed that the GSWC is operating under "Top Heavy" organization structure and that it carries "Corporate Fat". For example, in the Commission's decision, D.06-01-025, the presiding Administrative Law Judge made the following statement commenting on the GSWC's enormous overhead rate:

> The record shows that private engineering businesses assess overhead rates of about 15%. In fact, SCWC's own "overhead" rate in 1990 was only 12%, and that included its direct billings, as shown by the contract with the Department of Corrections for facilities to serve the prison discussed in detail below.
>
> The vendor rates differ substantially from SCWC's current rate because they include the vendor company's profit, as well as administration and management. SCWC's overhead rates do not include profit. This difference strongly suggests that SCWC's overhead expenses are high, a conclusion also supported by SCWC's 1990 rate, and giving credibility to customers' allegations of corporate "fat."

GSWC's past restructuring efforts had contributed to this "corporate fat". For example, prior to 1994, GSWC's water operations were organized into 16 Districts and the Company's General Office housed most of the water quality and engineering staff. In 1994, GSWC consolidated the district operations into three large operating regions: Region I, Region II, and Region III, and decentralized its oversight for engineering and water quality needs, thus creating the current organizational structure that is consisted of at least four layers: 1) General Office, 2) Regional Headquarters, 3) District Offices, and 4) Local CSAs.

Each of these layers has its own engineering and water quality staff. For example, each Regional Headquarter has the position of Engineering and Planning Manager, Water Quality Manager, a couple of Engineers, Senior Civil Engineers, and Engineer CAD Technicians. Similarly, each District Office has its own position of District Engineer, Water Quality Engineer, Engineering Technicians,

Electrician, and Water Quality Technician. While each CSA has it own Operations Superintendent, Water Supply Operators, and Water Distribution Operators.

This decentralization in 1994 resulted in a temporary reduction of the number of staff in the Company's General Office. However, DRA finds that this reduction in the General Office was short-lived. With the exception of a brief reduction over a few years after 1994, number of staff has been steadily on the rise. In 1994, there were 128 employees in Company's General Office. After the decentralization, the number was reduced to 87 in 1997. Since then, the number of employees in the General Office had increased to 102 in 2005. In the last General Office proceeding, A.06-02-023, GSWC requested the recovery of its payroll expense for a total of 139 employees. Thus, the company now not only has more employees in its General Office but has an enlarged staff in its Regional offices since the decentralization. Despite such increase in staff, GSWC continues to request for more positions in each subsequent GRC.

DRA would like to point out that among the newly added positions in its General Office, GSWC has a position of the Senior Vice President-Operations who is in part responsible for Company's Infrastructure Replacement and Investment needs. GSWC also formed a new department, Operations Department in its General Office and hired a Capital Projects Manager. GSWC justified that the Capital Projects Manager is needed in order to bring organization and cohesiveness to its capital program that currently lacks central oversight.

There is little merit in the company's claim of staff shortage. Ratepayers are already supporting an elaborate team of centralized (General Office) and decentralized (Regional) engineering staff. Based on its Region II GRC, the combined salary is $3,880,311 for the staff from Engineering, Water Quality, and Operation Department who participates in the capital budgets pertaining to water distribution and water supply function of the company. . As such, DRA believes that GSWC is adequately staff and should be able to carry out its capital projects on its own.

DRA recommends that GSWC utilize other less costly and available alternatives, such as improving internal procedures to coordinate, schedule and track capital projects. GSWC has a staff of well qualified engineers that should be able to manage more than just the day to day operation. GSWC's situation is not unique. Allowing GSWC to contract out the engineering duties associated with construction of major plant projects adds to the costs of construction projects, further burdening ratepayers whose rates already support the company's engineering salaries.

b. Bidding Process In Hiring CH2MHILL: **As discussed in details above that the need for the current partnership between GSWC and CH2MHILLis unjustified, so is the process of hiring and awarding the contract to CH2MHILL. Based upon the information provided by the Company[14], DRA finds that the original Request For Proposals (RFP) was first issued in year 2004, for the specific purpose as described below:**

> American States Water Company d.b.a. Southern California Water Company within California is seeking a relationship with a first-rate engineering firm or firms for the purpose of 1) Performing planning and design, design-build, and construction management of a major portion of our 2005 water distribution projects; and, 2) Performing planning and design, design-build, and construction management of a major portion of our 2005 water supply projects.

It is evident that the RFP was strictly for the purpose of completing portion of GSWC's 2005 capital projects. However, once hired, CH2MHILLhas been retained and continued to perform capital projects beyond 2005 without further competitive bid. In fact, GSWC's work papers reveal that CH2MHILLwill perform capital projects scheduled for as far out as 2009 and there is no reason to believe that it won't go beyond that time.

[14] GSWC's response to DRA's Data Request AMX-32

DRA finds troubling that there were no new RFPs being issued for the work beyond 2005. The continued retention of CH2MHILL amounts to a "no-bid" contract. More troubling is the fact that in the "Proposal Evaluation" section of the RFPs, GSWC assigned only a 10% weight for the "Fee Schedule" as criteria for evaluating a bid, indicating how little importance it placed in the overall cost of the project.

c. Conflict Of Interest: **The fact that CH2MHILLplays such an integral role in the development and construction of major plant projects presents what may be a conflict of interest between CH2MHILL and GSWC. CH2MHILL performs analysis of the water system by preparing the Master Plan which results in the roadmap for future construction projects. Then GSWC hires CH2MHILLto participate in the construction of those projects by preparing the designs and obtaining necessary permits for those same projects. GSWC has not justified abdicating many of its own engineering duties and responsibilities to CH2MHILL.**

For reasons discussed above, DRA strongly opposes GSWC's partnership with CH2MHILL and recommends that the Commission remove the 10% profit factor along with its 10% contingencies from all projects involving

CH2MHILLOverhead Rate

GSWC requests overhead rates of 18.47%, 25.83% and 32.67% for 2007, 2008, and 2009, respectively for its capital projects in Region whereas DRA recommends 6.61%, 17.74%, and 20.82% for those same years.

DRA believes that when compared with other Class-A water companies, GSWC's overhead rates are too high. For example, California Water Service Company has a constant overhead rate of approximately 8% year after year. Therefore, GSWC's enormous overhead rates are indicative of an unreasonable increase in the indirect/supervisory/support function in the company's day-to-day operations. The Commission was aware of this problem and in its decision, D.06-01-025; the presiding Administrative Law Judge noted the following:

> The record shows that private engineering businesses assess overhead rates of about 15%. In fact, SCWC's own "overhead" rate in 1990 was only 12%, and that included its direct billings, as shown by the contract with the Department of Corrections for facilities to serve the prison discussed in detail below.
>
> The vendor rates differ substantially from SCWC's current rate because they include the vendor company's profit, as well as administration and management. SCWC's overhead rates do not include profit. This difference strongly suggests that SCWC's overhead expenses are high, a conclusion also supported by SCWC's 1990 rate, and giving credibility to customers' allegations of corporate "fat."

On the other hand, current accounting methodologies used to record and track these indirect costs are also of concern for DRA, because these methodologies tend to distort the amount of actual indirect costs in various operating regions of the company.

GSWC's O&M and A&G expenses are capitalized into two categories throughout the operational areas. They are either capitalized directly to a specific capital project and become a part of the capital project itself, or they can be of an indirect nature and cannot be assigned to a specific capital project, which in this case, they would be booked into a company wide Overhead Pool Account. The amount of this account would later be allocated to all of the capital projects through the use of Overhead Rate.

Currently, GSWC requests to book related capitalized expenses from various operational areas of its organization, which consists of Regions I, II, III, Bear Valley Electric Division (BVE), and General Office into its company-wide Overhead Pool Account. Overhead rates are then determined by dividing indirect cost booked in the Overhead Pool Account by the amount of proposed capital projects.

DRA has found that the capitalized amount in the Overhead Pool Account remains relatively constant over the years. For example, GSWC work papers show

that the indirect expenses being booked into company-wide Overhead Pool Account for 2006 were $12,225,525. GSWC forecasts these expenses to be $12,898,918, $13,294,657, and $13,676,962 in 2007, 2008, and 2009 respectively.

However, other Class-A water companies are not booking such enormous indirect costs. For example, on average, California Water Service Company, the largest Class A water company in the state, books its indirect costs at about $7,000,000 per year. Such striking difference between the two companies leads DRA to conclude that GSWC is trying to maximize the capitalization of its O&M and A&G costs in order to earn a higher rate of return.

In addition, the practice of booking indirect costs into a company-wide Overhead Pool Account creates a disconnect between the actual indirect costs incurred in one operating region of the company and the corresponding capital investment in the same region. This would result in unrealistic assignment of indirect costs to the capital projects in that region that is in violation of this Commission's rule.

The Commission's Uniform System of Accounts for Water Utilities clearly states the following when describing the application of Overhead Construction Costs:

> 6. Overhead Construction Costs
>
> All overheads construction costs, such as engineering, supervision, general office salaries and expenses, construction engineering and supervision by others that the accounting utility, law expenses, insurance, injuries and damages, relief and pensions, taxes and interest, shall be charged to particular jobs or units on the basis of the amount of such overheads reasonably applicable thereto, to the end that each job or unit shall bear its equitable proportion of such costs and that the entire cost of the unit, both direct and overhead, shall be deducted from the utility plant account at the unit of property is retired.
>
> The instruction contained herein shall not be interpreted as permitting the addition to utility plant

> accounts of arbitrary percentages or amounts to cover assumed overhead costs, but as requiring the assignment to particular jobs and accounts of actual and reasonable overheads costs.
>
> The records supporting the entries for overheads construction costs shall be so kept as to show the total amount of each overhead for each year, the nature and amount of each overhead expenditure charged to each construction work order and to each utility plant account, and the bases of distribution of such costs.[Emphasis added.]

According to the above, the overhead costs should not be an arbitrary percentage but should be an actual and reasonable cost. By lumping all of its indirect costs into a single company-wide Overhead Pool Account, GSWC removes the possibility of assigning the actual indirect costs incurred in a specific operating region to only those capital projects of that operating region. For example, inclusion of indirect costs from its Electric Division, BVE into the company-wide Overhead Pool insures that no matter what actual indirect costs are booked from BVE, the capital projects in BVE will always have a large base of indirect costs available to fulfill the assignment of overhead rate that is based upon an arbitrary percentage.

If the indirect costs from BVE operating area were accounted separately, and as discussed above that they should be relatively constant from year to year, a large capital project in BVE operating area in a particular year should result in a lower overhead rate. However, by lumping indirect costs from all of the operating regions in one Single Company-wide Pool Account, GSWC could generate an overhead rate that does not reflected accurately the indirect costs of the BVE operating area, i.e.: it could cause the overhead rate higher that it would have been.

In addition, GSWC has historically not been able to zero-out its company-wide Overhead Pool Account. DRA believes that this situation has rendered this Overhead Pool Account a “bottom-less” pit where the relationship between indirect costs and capital projects in a particular operating region ceases to exist.

No matter how large or small an amount of capital project gets in a year, the indirect expenses from the subsequent years will be used to sustain a presubscribed arbitrary overhead rate.

For example, GSWC's work papers[15] indicate a year-end balance of negative $4,349,866 in 2004 in its Overhead Pool Account. Simply put, close to four and half million dollars were applied to capital projects in the name of indirect capitalized expenses that were not yet incurred. GSWC's records show that in the following year i.e. 2005, another load of $14,127,089 was being booked into company-wide Overhead Pool Account where the year-end balance was a positive $5,588,750. This surplus amount indicates that in 2005, there were more O&M and A&G expenses being capitalized than the amount that was being applied to capital projects as overhead.

In this application, GSWC's work papers indicate that it is trying to zero out its company-wide Overhead Pool Account at the end of year by charging the excess balance of the account to various capital projects throughout the company. DRA objects to this methodology and believes that the proper method of eliminating the excess amount is to return the capitalized expenses back to O&M and A&G areas where they can be properly expensed rather than capitalized.

In addition, GSWC books its entire employee related insurances, health benefits, and vacation expenses into its General Office. GSWC then designates 21% of these expenses as capitalized expenses. GSWC also estimates that approximately 64% of these 21% expenses should be booked into the company-wide Overhead Pool Account as an indirect capitalized labor. Once again, the true costs are distorted by this practice. For employees' pension, GSWC has historically booked the entire 21% of this expense as indirect capitalized expense into the company-wide Overhead Account. Upon DRA's objection in its last rate case proceedings, GSWC now books 64% of this 21% of employees' pension

[15] MSExcel File, Titled: Overhead-R1 V07 02-08-07 Update

expenses as indirect capitalized labor. However, there is no need to pool employee related costs for insurance, health benefits, pension, and vacation into General Office. These costs should be directly assigned to each employee working in his or her operating region. In addition, by lumping these costs in the company-wide Overhead Pool Account, the true overhead costs for capital projects in GSWC's specific operating regions are distorted.

In order to end the current abuse of overhead rate, DRA recommends the following steps:

(i) GSWC must separate its specific capitalized costs at each operating region level so that only true and real costs are passed on to the related capital projects in each operating region. DRA argues that GSWC should track the capitalized expense which it books into the Company-wide Overhead Pool Account for each operating region separately. Therefore, there will be no company-wide Overhead Pool Account; instead each operating region will have its own Overhead Pool Account. This will give more control and added transparency to the entire process of measuring overhead rates and facilitate the accountability for the managers responsible for specific operating regions.

(ii) GSWC must bring down the amount of its annual indirect capital expenses so that they are in-line with the other Class-A water utilities. In general, a smaller size company should have lower indirect capital expenses compare to a larger size company. As discussed earlier, this is not the case with GSWC. California Water Service Company with approximately 500,000 customers and serves 28 different districts is booking half of the indirect capital costs as GSWC, which serves approximately 275,000 customers in 16 districts. DRA believes that one contributing factor is related to GSWC's top-heavy organizational structure. Another factor is the lack of oversight and accountability. GSWC could bring down its indirect costs and achieve a lower comparable overhead rate for its capital projects by implementing cost cutting techniques, managing the overhead costs at various operating region levels, and properly and directly tracking various overhead costs into the specific operating regions,.

(iii) DRA disagrees with the method employed by GSWC in order to "Zero-out" the company-wide Overhead Pool Account. As

> discussed earlier, in order to have a better control and managerial accountability, GSWC should eliminate the company-wide Overhead Pool Account. In addition, GSWC should not "zero-out" excess year-end balance in overhead accounts by simply assigning these amounts to capital projects in the year or the capital projects in the subsequent future years. Instead, GSWC should transfer the excess balance back to the O&M and A&G expenses where they can be properly expensed. For the subsequent future years, GSWC will then have to diligently estimate the indirect costs so that there is no shortage or excess in overhead pools. Any excess should also be investigated and the responsible managers in each operating region should be held accountable.

For this proceeding, DRA is using the following methodology to calculate applicable overhead rate for GSWC's capital projects in Region I for 2007, 2008, and 2009:

Since the data regarding company-wide Overhead Pool Account in 2006 is the latest recorded data available, DRA begins its analysis from the beginning of 2006. GSWC records show that there is a positive balance of $5,588,750 in the company-wide Overhead Pool at the beginning of 2006, indicating an excess of expenses being drawn out of O&M and A&G for the purpose of capitalization in 2005. Similarly, 2006 year-end balance is a positive $1,019,917. Once again this balance indicates an excess during 2006. However, during the DRA's discovery, GSWC stated that the $1,019,917 was deliberately left in the company-wide Overhead Pool Account for the purpose of recalculation of its overhead rate per Commission's decision: D.06-11-020. DRA agrees that there is a need for such adjustment; however, DRA disagrees with the amount and recommends $72,152 instead. Therefore, there is a total of $5,660,902[16] in excess in 2006.

[16] $5,588,750 + $72,152

In addition, GSWC work papers[17] show that in 2006 it allocated an additional $4,835,138 in order to "zero out" the company-wide Overhead Pool in 2006. It should also be noted that in GSWC's work papers[18] the adjustment for the purpose of clearing company-wide Overhead Pool Account is listed as $9,661,219 instead of $4,835,138. Upon DRA's inquiry, GSWC's staff failed to present any plausible reason for this discrepancy and insisted that the adjustment amount for zeroing-out its company-wide Overhead Pool Account was $4,835,138. Nevertheless, DRA chose to proceed with its analysis by accepting the value of $4,835,138.

As discussed earlier, DRA disagrees with the method employed by GSWC for the purpose of clearing its company-wide Overhead Pool Account, and instead believes that the excess monies should be transferred back to O&M and A&G expenses. Therefore, the total excess amount in 2006 is then moved up to $10,496,040.[19]

DRA's objective is to determine a reasonable overhead rate for GSWC's capital projects in Region I. Since the indirect costs are being booked in a company-wide Overhead Pool Account, DRA needs to know that how much of these costs can be attributed to Region I and General Office. Upon DRA's request[20], GSWC provided a breakdown of these costs among its operating regions: General Office, Region I, Region II, Region III, and its Bear Valley Electric. GSWC's data shows that in 2006 it booked a total of $12,257,441 indirect costs into the company-wide Overhead Pool Account, of which $4,072,759 and $2,301,517 were contribution from General Office and Region I,

[17] GSWC response to DRA's Data Request AMX-59, And GSWC's Work papers: MSExcel File, Overhead –R1 V07 02-08-07 Update

[18] GSWC response to DRA's Data Request AMX-59, And GSWC's Work papers: MSExcel File, Overhead –R1 V07 02-08-07 Update

[19] $5,660,902 + $4,835,138

[20] DRA's data Request AMX-03

respectively. These amounts translate into allocation rates of 33.22% and 18.78% for General Office and Region I, respectively.

Using these rates, DRA then calculates $585,258 and $330,729 as the indirect expenses for General Office and Region I. These amounts should be booked into the company-wide Overhead Pool Account to offset a portion of the excess amount of $10,490,040. In addition, using GSWC's historical allocation rate of 16.62% for its General Office Expenses to Region I, DRA calculates $97,270[21] as the indirect expenses contributed from General Office to Region-I. This means that $427,999[22] of indirect cost should be contributed from Region-I into the company-wide Overhead Pool Account during 2006.

Once the reasonable contribution of Region-I indirect costs that are adjusted for the excess amount are known, DRA moved to separate the portion of these indirect costs that maybe used for New Businesses in 2006. New Businesses are those capital projects that are funded by outside contributors and normally are not included in the rate base for the rate making purposes. In its response to DRA's data request, AMX-03, GSWC indicated that the capital investment for New Businesses in 2006 was $2,622,634. Historically, GSWC uses 13% as its overhead rate New Businesses. However, for Region I overhead rate, DRA cannot relied on this historical 13% overhead rate and instead uses the ratio of company-funded capital projects to that of New Businesses in Region I in 2006 to separate the amount of indirect expenses that can be attributed to company-funded region I capital projects in 2006.

GSWC's response to DRA Data Request AMX-03 revealed that it spent $13,005,156 toward company-funded projects in 2006. Therefore, the amount spent for New Businesses was 20.15 %[23] of the amount spent for company-funded

[21] $585,258 * 16.62%

[22] $97,270 + $330,729

[23] $2,622,634 / $13,005,156

capital projects. Using the ratio of 20.15%, DRA then calculates $341,688[24] as indirect cost that can be attributed to company-funded capital projects in 2006. Using $341,688 as the base and by applying the appropriate escalation factors, DRA derives $438,699, $449,052, and $459,021as the indirect costs in Region I for 2007, 2008, and 2009, respectively. However, as these indirect costs are based upon 2006 recorded capital budget, an adjustment is needed to reflect the recommended capital budget in the year 2007, 2008, and 2009, which are relatively lower than the one recorded in year 2006. In general, most of the management oversight costs decrease as the volume of the capital budget is reduced thus provides the rational for a downward adjustment of indirect cost. Therefore, DRA downwardly adjusts the indirect costs relative to the decrease in the recommended capital budget vis-à-vis the capital budget in year 2006 to the value of $224,437, $274,753, and $297,058, for the year 2007, 2008, and 2009 respectively. In the end overhead rate was calculated by dividing respective indirect cost by the recommended budget in a particular year.

Capital Budget Contingency Rate

GSWC requested a contingency rate of 10%. The rate is being applied to both stand-alone major capital projects and the blanket projects. However, in its work papers, GSWC specifically noted the contingency amount for its blanket projects. The contingency amounts for stand alone projects are embedded in their respective cost estimates. Based on discussion below, DRA disagrees with GSWC on the 10% contingency rate and instead recommends it to be 5%.

GSWC states[25] that the contingency budget is used for unexpected capital expenditures or to fund overruns on known projects. DRA believes that both of these reasons are indicative of poor management planning. The emergency breakdown should be avoided by implementing an effective preventive

[24] $427,999 * (1-0.2017)

[25] Ernest Gisler's testimony, page -64

maintenance plan throughout the operation areas. The preventive maintenance planning not only decreases the occurrence of emergency breakdowns; it also saves costly emergency fixes.

Similarly, cost overruns are also an indication that GSWC does not have an effective cost management plan. It shows that GSWC is performing poorly on both cost estimations and project management. DRA would like to emphasize that the issue of cost overrun is very serious as it directly affects the rate base which in turn would increase the revenue requirement. In addition, unlike the increase in O&M and A&G expenses, the increase in rate base allows the Company to earn a rate of return. Therefore, there is an inherent advantage for the Company to inflate its capital expenditure needs. Hence an increase in the rate base should be carefully examined by the Commission. DRA recommends that the Commission places added emphasis on cost estimations so that they are fully supported and that proper project management oversight and cost management plans are in place.

In addition, GSWC has not provided any supporting documentation to justify the 10% contingency rate. This Commission previously noticed that GSWC's contingency request was not supported, yet the Company chose not to provide support for its request once again. For example, the assigned Administrative Law Judge made the following remarks in the Commission's decision D.06-01-025, concerning GSWC's GRC for Region III:

> *"SCWC included a 10% adder in its capital budgets for "contingency." ORA opposed adding this amount because SCWC had not provided ORA with sufficient justification.*
>
> *In rebuttal, SCWC explained that the contingency budget is used where actual costs exceed budgeted costs for a capital project. On cross-examination, SCWC's witness explained that in addition to cost overruns, the contingency budget is used for unanticipated projects. SCWC also stated that in 2004, actual capital expenditures were $29.1 million, while the budgeted amount was only $20.7 million, including the contingency budget. SCWC pointed out that this line item had been in its capital budgets for at least 20 years.*

The record in this proceeding shows that SCWC often overruns its budget for a capital project. As one example, the actual costs for the Calipatria Niland Upgrade project increased by 7% from the time SCWC filed its application to the filing of rebuttal testimony. SCWC also appears to have a practice of hiring vendors on a time and materials basis. Accurate budgeting and cost containment are critical management functions that require additional attention from SCWC management. We are concerned that the contingency budget may play a role in "cushioning" SCWC from the consequences of insufficient attention.

We are also aware that unanticipated capital projects may require immediate attention. The record, however, shows no historical analysis of SCWC's contingency budget expenditures on unanticipated projects. Such an analysis could be readily prepared because the general work order approval forms included in Exhibit 29 disclose when a project is funded by the contingency budget. SCWC did not do such an analysis, even after ORA recommended a disallowance. SCWC has provided us no breakdown between budget overruns and unanticipated projects that have used this fund in the past, so we will simply assume it was divided evenly between the two uses.

We will allow SCWC to include a contingency budget for unanticipated projects in test years 2006 and 2007.[26] *We will set SCWC's contingency budget based on unanticipated projects only, which we will assume to be 5% of the total capital budget. Our objective is to do away with the cushion for poor budgeting. Therefore, we will allow SCWC to include in its 2006 and 2007 capital budgets a contingency adder equal to 5% of the total approved capital budget."*

DRA argues that nothing has changed since the Commission's last decision. The concerns for the "cushion" of rate base are still valid and the Company failed to support its request.

Based upon the fact and findings discussed above, DRA recommends allowing a contingency rate of 5%.

[26] SCWC included a 10% contingency adder on all forecasted 2005 projects. As discussed elsewhere in today's decision, the Commission's practice is to use last recorded plant accounts (2004) as the basis for the test years. Forecasted but not complete projects in the intervening year (2005) are not included. Accordingly, no contingency amount will be included for 2005.

D. Conclusion

The following table reflects Plant in Service as requested by GSWC and recommended by DRA.

Table 4-6

PLANT IN SERVICE
Test Year 2008 and Escalation year 2009

Item	DRA EY 2007 (A)	Utility (B)	DRA TY 2008 (C)	Utility (D)	DRA TY 2009 (E)	Utility (F)
			(Dollars in Thousands)			
Plant in Service-BOY	7,626.0	7,626.0	8,245.8	8,435.6	8,607.0	8,847.3
Additions:						
Utility Funded	211.2	424.8	356.4	413.3	242.9	421.1
Advances	32.8	32.8	32.8	32.8	32.8	32.8
Contributions	17.2	17.2	17.2	17.2	17.2	17.2
CWIP	436.2	436.2		-		-
Gross Additions	697.4	911.0	406.4	463.3	292.9	471.1
Less:						
Retirements	(77.6)	(101.4)	(45.2)	(51.5)	(32.6)	(52.4)
Transfer & Adjustment	-					
Plant-in-Service (EOY)	8,245.8	8,435.6	8,607.0	8,847.3	8,867.3	9,266.0
Weighting Factor	50.00%	50.00%	50.00%	50.00%	50.00%	50.00%
Wtd. Avg. Plant in Service	7,935.9	8,030.8	8,426.4	8,641.4	8,737.2	9,056.7

CHAPTER 5 DEPRECIATION AND AMORTIZATION

A. INTRODUCTION

This Chapter presents DRA's analysis and recommendation on depreciation. The following table shows the weighted average accumulated depreciation and amortization for Test Years 2008 and 2009.

B. SUMMARY OF RECOMMENDATIONS

GSWC's estimated depreciation for Test Year 2008 is $2,895,300 and $3,168,400 for Test Year 2009. DRA estimates $2,918,600 for Test Year 2008 and $3,196,500 for Test Year 2009. The difference between GSWC and DRA recommended accumulated depreciation and amortization is due to the differences in estimates of plant in service during the Test Years. The following Table 5-1 illustrates GSWC and DRA estimates for depreciation.

C. DISCUSSION

According to GSWC's witness, Jenny Darney-Lane, in this rate case, GSWC has agreed to no longer track the cost of small tools through a clearing account that was then applied as an "overhead" to labor costs. Through a settlement agreement with DRA in A.06-02-023, GSWC agreed with DRA that starting in 2007 the company would begin to expense the cost of small tools. Therefore, GSWC will no longer book the depreciation for small tools to the small tools clearing account and will include the amount as part of the depreciation expense. GSWC has also provided a depreciation study specific to the administrative offices.

DRA has reviewed the company's analysis and accepts GSWC's methodology to arrive at the accumulated depreciation and amortization accrual for Region I. The following table reflects GSWC's estimated Depreciation and DRA's recommendation.

Table 5-1

ACCUMULATED DEPRECIATION AND EXPENSE
Test Year 2008 and Escalation year 2009

Item	DRA (A)	Utility EY 2007 (B)	DRA (C)	Utility TY 2008 (D)	DRA (E)	Utility TY 2009 (F)
			(Dollars in Thousands)			
Accum. Depreciation (BOY)	2,577.7	2,577.7	2,786.2	2,762.5	3,050.9	3,028.1
Accruals During Year:						
Clearing Account	2.5	2.5	2.5	2.5	2.5	2.5
Contributions	6.1	6.1	6.8	6.8	7.4	7.4
Depreciaton Expense	277.5	277.5	300.7	307.9	313.9	323.1
Total Accruals	286.1	286.1	310.0	317.2	323.8	333.0
Less:						
Net Retirements	-77.6	-101.4	-45.2	-51.5	-32.6	-52.4
Adjustments	0.0	0.0		0.0		0.0
Accum. Depreciation (EOY)	2,786.2	2,762.5	3,051.0	3,028.1	3,342.1	3,308.7
Weighting Factor	50%	50%	50%	50%	50%	50%
Avg. Accumulated Deprec.	2,682.0	2,670.1	2,918.6	2,895.3	3,196.5	3,168.4

CHAPTER 6 RATE BASE

A. INTRODUCTION

This Chapter presents DRA's analysis and recommendation on rate base. The following table compares DRA and GSWC's estimates of rate base for Test Years 2008 and 2009.

B. SUMMARY OF RECOMMENDATIONS

GSWC requests rate base of $4,670,600 for Test Year 2008 and $4,731,300 for Test Year 2009. DRA recommends $4,413,200 for Test Year 2008 and $4,365,100 for Test Year 2009. Differences in rate base are due to differences in plant additions and Common Utility Allocations.

C. DISCUSSION

1. Common Utility Allocation

Common Utility Allocation is the allocation of Company's General Office weighted average rate base to each of the Customer Service Areas of the Region I. The amount also includes the rate base allocations from the Region I Headquarters and Northern/Coastal District Office. For the discussion regarding the Region I Headquarters, and Northern/Coastal District Office, please refer to the DRA report on "Region I Administrative Offices and Low Income Ratepayers Assistance Program".

For its General Office, the Company requested the amount of $73,400, $84,900, and $96,300 in year 2007, 2008, and 2009 respectively whereas DRA recommends $51,804, $47,824 and $51,804.

The Company's previous General Rate Application (GRC), A.06-02-023 included its General Office's operations. The Commission's decision is still pending regarding these proceedings. However, the Company's weighted average rate base allocations from its General Office to the Region I's Customer Service Areas, are based on the stipulated rate base, and assume that all contested issues are resolved in the Company's favor. The difference is due to the fact that DRA's

recommended allocations are based on the stipulated amount and the assumption that all contested issues presented in A.02-02-023 are resolved in DRA's favor.

2. Working Cash

GSWC's estimate of working cash for Test Years 2008 and 2009 is $10,000. DRA performed its own independent analysis of working cash requirement and lead/lag days. In determining working cash, DRA followed the guidelines set by Standard Practice U-16-W in determining the expense lag days. DRA arrived at a similar result as GSWC. Therefore DRA accepts the company's estimate of $10,000.

3. Construction Work in Progress (CWIP)

Although DRA does not recommend a difference in recorded or forecasted CWIP at this time, GSWC's approach to the CWIP amount is in need of Commission review and oversight. The CWIP account is traditionally used to track capital projects that are in progress but not yet completed. The Commission allows water utilities to earn a rate of return on the CWIP dollars. The rationale for this is that typically water utilities' capital projects are comparatively simple and are therefore expected to be completed within one year, and then placed into service as used and useful. For the most part, this process has worked for most Class A water companies.

However, this is not the case with GSWC; DRA has observed in this rate case and prior rate cases for Region II and III that many of GSWC's projects are not completed in one year and therefore, remain in the CWIP account for more than a year and some cases several years. This practice potentially turns the Company's CWIP account into a "gold mine" because the Commission allows CWIP to earn a rate of return. When projects remain in CWIP year after year, rates are developed based upon many of the same projects over and over again prior to projects becoming used and useful. In some cases, by the time projects

are completed the cost to complete the project has increased well beyond the approved or authorized budget.

Because of the potential impact on rates to rate payers caused by projects remaining in CWIP beyond one year, a thorough examination is required to examine which projects are included in CWIP that have carried over from prior rate cases, why the projects were not completed within the expected timeframe, whether funds were deferred from authorized projects to other projects and whether those other "non-authorized" projects were reasonable.

In the Clearlake CSA, there were approximately 20 projects in the CWIP account. General Work Orders for these projects were issued from 2002 through 2006. DRA's review of this CSA CWIP account did not find the number of aged projects it found in other CSA's. However, in keeping with DRA's position in the other CSA's in the Northern and Coastal Districts DRA recommends that the Commission give serious consideration into whether it is proper to continue allowing GSWC to continue using CWIP for projects that can not or will not be completed within a years' time. Under the existing parameters, GSWC is able to book any and all projects into CWIP and there is little oversight into the reasonableness of many of the projects and almost no control over increasing costs for delayed projects. Therefore, DRA recommends that projects which GSWC can not complete within one year be allowed to earn Allowance for Funds Used during Construction, or AFUDC which will allow the company to only earn interest while the project is pending completion without earning rate of return. DRA also recommends that the Commission perform a detailed audit in GSWC's CWIP and its accounting practices.

In this rate case, GSWC requests forecasted CWIP costs in the amount of $436,200 in 2007, to complete pending projects included in the CWIP account. These projects were initiated prior to the close of 2006 but have not been completed. DRA has reviewed the projects included in the forecasted CWIP and

recommends funding of $436,200 to complete projects pending completion in 2007.

4. Conclusion

The following Table 6-1 illustrates GSWC's requested rate base and DRA's recommendation.

Table 6-1

WEIGHTED AVERAGE DEPRECIATED RATEBASE

Item	DRA (A)	Utility EY 2007 (B)	DRA (C)	Utility TY 2008 (D)	DRA (E)	Utility TY 2009 (F)
			(Dollars in Thousands)			
Wt. Avg. Plant in Service	7,935.9	8,030.8	8,426.4	8,641.4	8,737.2	9,056.7
Utility Plant Under Construction	153.9	153.9	0.0	0.0	0.0	0.0
Acquisition Adjustment	0.0	0.0	0.0	0.0	0.0	0.0
Total Utility Plant	8,089.8	8,184.7	8,426.4	8,641.4	8,737.2	9,056.7
Depreciation Reserve	-2,682.0	-2,670.1	-2,918.6	-2,895.3	-3,196.5	-3,168.4
Net Utility Plant	5,407.8	5,514.6	5,507.8	5,746.2	5,540.7	5,888.3
Materials and Supplies	20.2	20.2	20.2	20.2	20.2	20.2
Advances	-79.0	-79.0	-108.8	-108.8	-137.4	-137.4
Contributions	-131.8	-131.8	-142.5	-142.5	-152.7	-152.7
Rate Base Before Adjustment	5,217.2	5,324.0	5,276.7	5,515.1	5,270.8	5,618.4
Deferred F.I.T. Items	-929.6	-940.4	-983.1	-1,007.5	-1,016.3	-1,052.5
Deferred Revenues	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Invest. In Other Water Co.		0.0		0.0		0.0
Deferred Rate Case Expense		0.0		0.0		0.0
Allowance for Working Cash	10.0	10.0	10.0	10.0	10.0	10.0
Common Utility Allocation	125.8	149.9	110.1	153.4	101.1	155.7
Weighted Average Rate Base	4,423.0	4,543.2	4,413.3	4,670.6	4,365.2	4,731.3

CHAPTER 7 TAXES

A. INTRODUCTION

This Chapter sets forth the analysis and recommendations of DRA regarding taxes other than income and income taxes. Tables 7-1 and 7-2 show DRA's and GSWC's estimates of taxes other than income and income taxes for Test Year 2008.

B. SUMMARY OF RECOMMENDATION

DRA estimates higher income taxes for both State and Federal Income Taxes as shown in Table 7-1. The difference between GSWC's and DRA's estimates is due to different estimates in revenue requirement, expenses, rate base and other tax issues.

C. DISCUSSION

1. Ad Valorem Tax (Property Tax)

DRA recommends $28,000 for ad valorem taxes for Test Year 2008. GSWC requested $29,100 for ad valorem taxes. The amount of $1,100 differs from GSWC's due to DRA's different plant estimates, discussed in Chapter 5 of this report.

2. Payroll Taxes

Payroll taxes include Social Security tax, Federal Insurance Contribution Act (FICA) tax consisting of Old Age Benefits and Medicare, Federal Unemployment Tax Assessment (FUTA), and State Unemployment Tax Assessment (SUTA).

DRA and GSWC recommend an estimate of $21,100 for payroll taxes in Test Year 2008.

3. Local Taxes

DRA and GSWC recommend an estimate of $100 for local taxes in Test Year 2008.

4. Tax Depreciation

DRA calculated tax depreciation for state and federal income tax purposes by applying the ratio of DRA's estimate of net plant to GSWC's estimate of net plant to GSWC's tax depreciation estimate.

5. Interest Deduction

To calculate the interest deduction, DRA used its recommended rate base, discussed by DRA's plant witness, multiplied by DRA's recommended weighted cost of debt.

6. Income Taxes

The differences in income taxes estimated for Test Year 2008 between DRA and GSWC are due to the differences in revenues, expenses, and rate base.

7. Conclusion

As per discussion above, DRA recommends the Commission to adopt its estimates for Taxes Other Than Income and Income Taxes for Test Year 2008.

Table 7-1		
GOLDEN STATE WATER COMPANY		
Region I- Clearlake District		
TAXES OTHER THAN INCOME (2008)		
	@ Proposed Rates	
	2008	
	DRA	Utility
Item	Analysis	Estimated
	(A)	(B)
Ad Valorem Tax	28.0	29.1
Payroll Taxes	21.0	21.0
Local Franchise Tax	0.1	0.1
Total Taxes other than income	49.1	50.2

TABLE 7-2				
GOLDEN STATE WATER COMPANY				
Region I- Santa Maria District				
Income Tax				
2008				
	ORA	Utility	ORA	Utility
Item	Present Rates		Recommended Rates	
	(A)	(B)	(E)	(F)
	(Dollars in Thousands)			
Operating Revenues:	1,679.7	1,649.3	1,709.0	1,886.3
Expenses:				
Oper. & Maint. & A&G	1,078.4	1,178.2	1,078.4	1,179.3
Taxes Other than Income	49.1	50.1	49.1	50.1
Depreciation & Amortization				
Book Depreciation- District	(300.7)	(307.9)	(300.7)	(307.9)
Book Depreciation- G.O.	(5.0)	(9.0)	(5.0)	(9.0)
Interest	160.2	169.1	160.2	169.1
Expense Before Taxes	982.0	1,080.5	982.0	1,081.6
CCFT				
Tax Depreciation- State	(365.7)	(374.5)	(365.7)	(374.5)
Other Schedule M Items	7.9	10.2	7.9	10.2
State Taxable Income	339.9	204.5	369.2	440.5
CCFT (8.84%)	30.0	18.1	32.6	38.9
FIT				
Excess Tax Depreciation	36.9	27.1	36.9	27.1
Book Depreciation- District	(300.7)	(307.9)	(300.7)	(307.9)
Book Depreciation- G.O.	(5.0)	(9.0)	(5.0)	(9.0)
State Tax	(25.1)	(18.1)	(25.1)	(18.1)
Other Scheduled M Items	6.4	8.5	6.4	8.5
Def. Rev. Amort.- Contrib.	4.5	4.5	4.5	4.5
Federal Taxable Income	414.7	273.9	444.0	509.8
FIT (35%)	145.2	95.8	155.4	178.4

CHAPTER 8 CHAPTER POLICY ISSUES

A. INTRODUCTION

This Chapter provides DRA's comments regarding GSWC's water quality and customer service in the Clearlake CSA.

B. SUMMARY OF RECOMMENDATIONS

DRA reviewed various water quality documents provided by GSWC and contacted DHS for information relating to the compliance history of the Clearlake Water System and found that these water systems have been in compliance with the drinking water standards during 2004 to 2006. DRA also learned through the Public Advisor's office that GSWC has generally been satisfactorily serving the Clearlake customers.

C. DISCUSSION

1. Water Quality

DRA performed a review of GSWC's water supply and quality documents. DRA also contacted DHS to obtain the compliance history of GSWC's water systems from 2004 to 2006 in the Clearlake service territory. As informed by DHS, the Clearlake water systems generally were in compliance with the drinking water standards between 2004 and 2006.

The last DHS inspection was in 2000. During this inspection, DHS identified two major issues and required GSWC to address two critical issues in its Comprehensive Master Plan to be submitted in 2007: (1) Clearlake is located in an area that experiences frequent power outages and should have a generator available to ensure a reliable supply of water to consumers; and (2) DHS is concerned that Clearlake is rapidly approaching its maximum day demand for source capacity.

2. Customer Complaints

DRA, through the Commission Public Advisor's Office, has received no protest to the proposed increase in rates and addressing various related cost issues such as memorandum accounts, service, compensation, water quality, and management of the water system.

The Consumer Affairs Branch has received four informal complaints involving rates, billing, installation, service for the period January 1, 2004 through December 31, 2006. There were no formal complaints filed against GSWC during this period.

CHAPTER 9 RATE DESIGN

This chapter sets forth the analysis of DRA on the rate design. GSWC currently provides water service to its customers under the following tariffs:

Schedule No. CL-1, GENERAL METERED SERVICE

Schedule No. 4, PRIVATE FIRE SERVICE

Schedule No. UF, SURCHARGE TO FUND PUBLIC UTILITIES COMMISSION REIMBURSEMENT FEE

GSWC's rate design is consistent with the method set forth in D.86-05-064. Approximately 50% of fixed costs are recovered through the service charge, and the remaining costs are recovered through a single block commodity rate.

The Commission has issued Order Instituting Investigation I.07-01-022 regarding conservation rate designs. At this time, the Commission should continue to apply the current rate design methodology until the Commission issues its final decision on the conservation rates for GSWC.

CHAPTER 10 ESCALATION YEARS

Table 10-1 below shows the Summaries of Earnings for Escalation Years 1 and 2. To obtain the increases in these years, D.04-06-018 requires water utilities to file an Advice Letter 45 days prior to the start of the year showing all calculations supporting their requested increases.

The revenues shown in the table are for illustration purposes and the actual increases would be authorized only after approval of the utility's escalation year advice letters for 2009 and 2010.

TABLE 10-1

GOLDEN STATE WATER COMPANY
Region I- Clearlake
SUMMARY OF EARNINGS (Escalation Years)

Item	DRA 2009 (A)	@ proposed	DRA 2010 (C)
	(Dollars in Thousands)		
Operating Revenues	1,729.0		1,781.0
Total Revenue	1,729.0		1,781.0
Expenses			
Operation & Maintenance	544.9		582.4
Admininistrative and General	249.2		254.6
Depreciation & Amortization	319.0		332.3
Taxes Other Than Income	51.0		52.7
CCFT	31.6		31.0
FIT	149.8		149.2
Total Expenses	1,345.5		1,402.2
Net Income	383.5		378.8
Ratebase	4,365.1		4,316.8
Rate of Return	8.79%		8.78%

APPENDIX A: ESCALATION FACTORS

State of California — PublicUtilities Commission
San Francisco

M E M O R A N D U M

Date: February 28, 2007

To: D. Sanchez, Program Manager, DRA; K. Coughlan, Director, Water Division

From: Martin G. Lyons, Program Supervisor, DRA Energy Cost of Service Branch

File No. : S-2559

Subject: DRA February 2007 Summary of Compensation Per Hour

The following data are provided to Commission water utilities staff to enable them to utilize DRA's composite non-labor escalation methodology. The numbers are to be used in conjunction with the non-labor factors provided in DRA's monthly escalation memorandum to bring historic dollars to base year dollars and to inflate recorded dollars to test year levels. More specifically, the annual change in Compensation per Hour is applicable to contracted services, while the non-labor factor is related to material and supply purchases. In accordance with a 1991 agreement between the CPUC Water Division and the California Water Association (CWA), the monthly non-labor rate is to be weighted by 60 percent and the Compensation per Hour Index weighted 40 percent. If you have any questions regarding the application of these factors, please contact me.

COMPENSATION PER HOUR

Annual Rate of Change
Non-farm Business Sector, Seasonally Adjusted

Year	Annual Change
1997	3.6%
1998	5.3%
1999	4.4%
2000	6.9%
2001	2.7%
2002	2.8%
2003	4.0%
2004	4.5%
2005	4.4%
2006	5.4%
2007	3.7%
2008	3.5%
2009	3.9%
2010	4.1%
2011	4.2%

Source: Global Insight February 2007 U.S. Economic Outlook

State of California Public Utilities Commission
San Francisco

M E M O R A N D U M

Date : February 28, 2007

To : Division of Ratepayer Advocates and Water Division

From : M. G. Lyons, Program Supervisor
DRA Energy Cost of Service Branch

File No.: S-2559

Subject: Division of Ratepayer Advocates: Estimates of Non-labor and Wage Escalation Rates for 2007 through 2011 from the February 2007 Global Insight U.S. Economic Outlook

The purpose of the monthly Escalation Memorandum is to inform division management of the trends in the general price level of utility non-labor expenses and wage contracts. Data are provided for 12 years, which include seven historic years, the estimated current year, and four forecasted years.

The following table summarizes the major changes in forecasted labor and non-labor inflation for years 2007 through 2011. Data for 2006 are provided as benchmarks. The factors for January 2007 are presented for comparison. Near-term lagged CPI is expected to run over 3% due to petroleum price increases and fall to the 2% range by 2008. Non-labor inflation for 2007-11 is effectively checked by continued structural changes in the economy such as globalization and improved operating efficiencies. Global Insight's forecast of rising non-labor rates for 2006 is the result of temporary price increases in petroleum, chemicals/allied products, metals/metal products, and machinery. Labor escalation continues to be constrained by changes in the labor market due to corporate structural change, outsourcing, and high labor productivity.

FORECASTED INFLATION

	Labor		Non-labor	
	01/07	02/07	01/07	02/07
2006	3.4%	3.4%	5.5%	5.5%
2007	3.2%	3.2%	2.1%	1.7%
2008	1.8%	1.5%	1.3%	1.6%
2009	2.1%	2.3%	0.8%	1.1%
2010	1.9%	2.1%	0.5%	0.7%
2011	1.9%	1.9%	0.5%	0.7%
Compounded	15.2%	15.3%	11.1%	11.8%

A more extensive explanation of the derivation and use of the above factors and a complete presentation of the escalation factors from 2000 through 2011 are provided in the attached appendix.

The recommended NON-LABOR ESCALATION RATES for 2007 through 2011 are presented in Table A. The values for 2000 through 2006 are provided for comparison.

TABLE A

Year	Non-Labor Inflation Rate*
2000	3.5%
2001	0.0%
2002	0.0%
2003	2.5%
2004	5.8%
2005	5.5%
2006	5.5%
2007	1.7%
2008	1.6%
2009	1.1%
2010	0.7%
2011	0.7%

* Revised 07/17/97 based on 1995 re-weighted purchases. [Source: BLS, Supplement to Producer Price Indexes, 1995, Table 12]

These escalation rates represent the calendar year average, or alternatively stated, the 12-month-ended spot rate at mid-year. These price factors have not been adjusted for real growth of expensed materials and services. The escalation factors are generated from a composite index of 10 Wholesale Price Indexes (WPI) for materials and supplies expenses and the CPI-U weighted 5% for services and consumer-related items. **These non-labor rates are not applicable to plant, contracted services, loans, insurance, rents, and pensions and other utility employee benefits. Escalation of these expenses is addressed on pages 10-15 of D.04-06-018/R.03-09-005 (Water Rate Case Plan).**

The WAGE ESCALATION RATES in Table B are based on recorded utility labor settlements for 2000 through 2006 and Global Insight projections of the U.S. CPI for All Urban Consumers (CPI-U) for 2007 through 2011.

TABLE B

Year	Wage Increases 1/ 2/
2000	3.00%/3.50%/3.00%- PG&E/SCE/SoCal
2001	3.00%/3.50%/3.00%- PG&E/SCE/SoCal
2002	3.00%/3.50%/3.00%- PG&E/SCE/SoCal
2003	4.00%/3.25%/3.00%- PG&E/SCE/SoCal
2004	4.00%/3.50%/3.50%- PG&E/SCE/SoCal
2005	4.00%/3.50% /3.50%- PG&E/SCE/SoCal
2006	3.75%/3.75%/3.50%- PG&E/SCE/SoCal
2007	3.2% -CPI 3/
2008	1.5% -CPI 3/
2009	2.3% -CPI 3/
2010	2.1% -CPI 3/
2011	1.9% -CPI 3/

1/ Wage increases are not adjusted for changes in hours worked or the number of employees. The labor requirement is a separate issue related to the calculation of total payroll.

2/ If the proposed increase is reasonable, witnesses should use the particular utility's actual settlement on the date it becomes effective. The above recorded wage increases are for benchmark purposes only.

3/ CPI-U lagged one year to be consistent with union contracts.

The generally accepted method in labor contracts is to peg a wage increase to the rate of increase in the CPI-U for the previous year. Consequently, these wage escalation rates are based on the previous year's CPI escalation. If the utility is using an index other than U.S. CPI-U, please contact me for directions. The witnesses should familiarize themselves with the actual wage contracts for 2000 through 2011 to ascertain the correct wage formulas, reasonableness, and the effective date of increase for the particular proceeding. The annualized wage increase should reflect the percentage changes in wages weighted by the number of months individual wage rates were in effect.

Other non-labor and labor indices may be used if a witness has more specific knowledge of any particular account. **Those individuals who plan to use their own inflation factors are expressly requested to contact me for approval and direction**.

These forecasts are updated monthly. Please call me if you have any questions relating to these projections.

cc: M. Pocta D. Sanchez F. Curry
M. Enderby K. Coughlan

APPENDIX B: QUALIFICATIONS OF DRA STAFF MEMBERS

Victor Chan, P.E.

- Senior Utilities Engineer
- Registered Professional Engineer in California
- Employed by the P.U.C. since 1996
- Employed in DRA Water Branch since 2004
- Sponsoring Sections:
    - Chapter 1 (Summary of Earnings)
    - Chapter 8 (Policy Issues)
    - Chapter 10 (Escalation Years)

Eric Matsuoka

- Public Utilities Regulatory Analyst
- Employed by the P.U.C. since 1974
- Employed in DRA Water Branch since 1998
- Sponsoring Sections:
    - Chapter 3 (Expenses, O&M, A&G)
    - Chapter 7 (Taxes)

Patricia Esule

- Public Regulatory Analyst
- Employed by the P.U.C. since 1989
- Employed in DRA Water Branch since 2002
- Sponsoring Sections:
    - Chapter 4 (Plant in Service)
    - Chapter 5 (Depreciation and Amortization Expenses)
    - Chapter 6 (Ratebase)

Victor Moon

- Utilities Engineer
- Registered Professional Engineer in California
- Employed by the P.U.C. since 1977
- Employed in DRA/Water Branch since 1984
- Sponsoring Sections:
    - Chapter 2 (Customer, Consumption, Operating Revenue)
    - Chapter 8 (Rate design)