STATE OF CALIFORNIA EDMUND Governor

PUBLIC UTILITIES COMMISSION
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TO PARTIES OF RECORD IN APPLICATION 12-01-003:

This is the proposed decision of Administrative Law Judge Wilson. Until and unless the Commission hears the item and votes to approve it, the proposed decision has no legal effect. This item may be heard, at the earliest, at the Commission's August 14, 2014 Business Meeting. To confirm when the item will be heard, please see the Business Meeting agenda, which is posted on the Commission's website 10 days before each Business Meeting.

Parties of record may file comments on the proposed decision as provided in Rule 14.3 of the Commission's Rules of Practice and Procedure.

/s/ TIMOTHY J. SULLIVAN
Timothy J. Sullivan,
Chief Administrative Law Judge (Acting)

TJS:dc3

Attachment

Decision **PROPOSED DECISION OF ALJ WILSON** (Mailed 7/11/14)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of San Jose Water Company (U168W) for an Order authorizing it to increase rates charged for water service by $47,394,000 or 21.51% in 2013, by $12,963,000 or 4.87% in 2014, and by $34,797,000 or 12.59% in 2015.	Application 12-01-003 (Filed January 3, 2012)

DECISION RESOLVING GENERAL RATE CASE OF SAN JOSE WATER COMPANY

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DECISION RESOLVING GENERAL RATE CASE OF SAN JOSE WATER COMPANY

1. Summary

San Jose Water Company (SJWC) is authorized to increase rates by amounts designed to increase revenue by $22,063,000 or 9.79% in its test year 2013, $11,579,000 or 4.72% in 2014, and $15,356,000 or 6.02% in 2015. As a result of the revenue increase granted by this decision, the monthly bill for the average SJWC residential customers using 1500 cubic feet (CCF)[1] of water with a 5/8" by 3/4" meter would increase by $7.96 or 20.8% to $46.20 from $38.24 for the test year 2013.

2. Background

San Jose Water Company (SJWC) provides public utility water service to approximately 226,000 residential and industrial customers within its 140 square-mile Santa Clara County service territory. Its service territory encompasses parts of Cupertino, San Jose, and Santa Clara, and in Campbell, Los Gatos, Monte Sereno, and Saratoga, as well as portions of unincorporated Santa Clara County.

SJWC is a wholly owned subsidiary of San Jose Water Corporation. SJWC's last general rate case (GRC) was for a 2010 test year, which was resolved by Decision (D.) 09-11-032.

On January 3, 2012, SJWC filed the above-captioned application to increase rates charged for water service within its service territory by $47,394,000 or

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[1] CCF means hundred cubic feet.

21.51% in 2013, by $12,963,000 or 4.87% in 2014, and by $34,797,000 or 12.59% in 2015.

Notices of the application were provided to the public through postings in offices, newspaper publications, and by mailings to each customer and to all cities and public agencies in the service territory.

On January 12, 2012, Resolution ALJ-176-3287 preliminarily determined that this proceeding was ratesetting and that hearings would be necessary. On February 6, 2012, the Office of Ratepayer Advocates (ORA) filed a protest.[2] On January 30, 2012, the assigned Administrative Law Judge (ALJ) issued a ruling setting a Prehearing Conference (PHC) for February 13, 2012.

On February 13, 2012, the PHC took place in San Francisco to establish the service list for the proceeding, discuss the oral motion for party status and to late-file a protest, discuss the scope of the proceeding, and develop a procedural timetable for the management of the proceeding. The Six Mutual Water Companies (Mutuals)[3] provided a verbal motion at the PHC for party status and for leave to late-file a protest to the current application. The assigned ALJ granted the motion for party status as well as the motion for leave to late-file a protest to the current proceeding.

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[2] During the progress of this proceeding, the Division of Ratepayer Advocates changed its name to the Office of Ratepayer Advocates (ORA). The Commission therefore refers to this party as Office of Ratepayer Advocates or ORA for the remainder of this decision.

[3] The Six Mutual Water Companies consists of Bid Redwood Park Mutual Water Co., Brush & Old Well Rd Mutual Water Co., Mountain Summit Mutual Water Co., Oakmont Mutual Water Co., Ridge Mutual Water Company, and Villa Del Monte Mutual Water Co.

On March 15, 2012, the assigned Commissioner issued her *Assigned Commissioner's Scoping Memo and Ruling* (Scoping Memo), which set forth the procedural schedule, assigned the presiding officer, and addressed the scope of this proceeding and other procedural matters following the PHC.

A public participation hearing was held in San Jose on May 21, 2012. Approximately 13 of the 60 or so people who attended the meeting spoke against any rate increase. The primary concern of the customers that spoke was the level of SJWC's requested rate increase.

On June 4, 5, 6, and 11, 2012, Evidentiary Hearings (EH) were held. Both SJWC and ORA presented witnesses in support of their respective testimonies. On June 5, 2012, SJWC and the Mutuals filed a joint motion requesting adoption of a settlement which resolved all outstanding issues raised by the Mutuals in their testimony.

On October 24, 2012, the assigned ALJ issued a ruling granting SJWC's motion in which it requested interim rate relief. Her ruling also granted SJWC's request to track in a memorandum account the difference between interim rates and final rates for subsequent recovery or refund, consistent with the final rates adopted by the California Public Utilities Commission (Commission) in the pending GRC.

On March 4, 2013, the assigned Commissioner issued an Amended Scoping Memo, which identifies this proceeding to consider new evidence regarding security and safety issues and revise the schedule.

Opening and reply briefs were filed on July 20, 2012 and August 7, 2012, respectively, by SJWC and ORA.

In determining the various components of San Jose's authorized revenue requirement, we do not use a one-size-fits- all approach. Doing so would ignore the uniqueness of events and circumstances that affect each component of the revenue requirement determination. By, for example, just using a five-year average to estimate the base upon which a forecasted expense is determined, we would ignore an expert's estimate based on intimate knowledge of the utility or recent events. What if the increases over those five years grew to a greater extent in more recent years? An average would result in a lower growth factor that recent history indicated as the trend. Therefore, we consider all options presented by parties for estimating forecasted revenue requirement elements, using the method which most appropriately fits the circumstances of each element.

3. Joint Comparison Exhibit

At the PHC, the assigned ALJ reminded all active parties to participate in settlement discussions subsequent to the tendering of interested parties' testimony and prior to the start of an EH.[4] At the EH, it was reported that the mediation process resulted in one partial settlement agreement between SJWC and the Six Mutual water companies, but no settlement with ORA. Therefore, all contested issues between SJWC and ORA remained outstanding and were the topic of EH, further exhibits, and briefs.

The Joint Comparison Exhibits filed jointly on June 5, 2012 by SJWC and ORA provide a comparison of test year 2013 results of operations to show the differences between SJWC and ORA. The Joint Comparison Exhibits were

[4] Active parties consisted of SJWC, the Commission's ORA, and the Mutuals.

identified and received into the record as Exhibits JCE-1 and JCE-2. Exhibit JCE-1 summarized the differences between SJWC and ORA with little detail (for example, for all Administrative and General (A&G) expenses), while Exhibit JCE-2 provided the detailed differences between SJWC's request and ORA's proposal (for example, broken out by A&G Rents, A&G Maintenance, etc.).

4. Settlement Agreement Between SJWC and the Mutuals

There was one settlement agreement in this proceeding regarding all outstanding issues raised by the Mutuals in their testimony.[5] This settlement, between SJWC and the Mutuals, was filed on June 5, 2012 resolves all issues contested by the Mutuals in this proceeding. This resolution strictly concerns rate design issues so does not affect SJWC's revenue requirement. The contested components of SJWC's Mountain District's rate design resolved by the Settlement Agreement relate to: (1) service charges; (2) quantity rates; (3) the daily usage allocation and the related Overuse Rate; and (4) the Elevation Charge. The Settlement Agreement describes the resolution of each settled issue and provides references to the testimony and exhibits of witnesses for the Settling Parties addressing the particular issue.

The Mutual's issues were resolved by the settlement as follows:

1. The service charges for Mountain District customers shall be the same service charges that are in effect for all of SJWC's remaining customers and are as reflected on SJWC's Schedule 1, General Metered Service.

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[5] http://docs.cpuc.ca.gov/SearchRes.aspx?DocFormat=ALL&DocID=61866

2. SJWC shall charge one service charge to each of its customers that is a mutual water company based on the size of the meter by which the mutual water company is served.
3. The mutual water companies that are SJWC customers in the Mountain District shall be charged the Quantity Rates applicable to non-residential customers ("All Other Customers") as specified in Tariff Schedule No. 1C for General Metered Service in the Mountain District, but subject to Special Condition 6 in that Schedule.
4. Current use restriction of 500 gallons per day, or 15,000 gallons per month, which is roughly equivalent to 20 CCF per month, shall remain in place for each water service.
    a. This use restriction is implemented by means of an Overuse Rate of $7.00 per CCF, which generally applies to each customer's monthly usage exceeding 20 CCF.
    b. Each SJWC customer in the Mountain District that is a mutual water company shall be entitled to a single quantity rate usage allocation per customer individually served by the mutual water company.
    c. The Overuse Rate will apply to a mutual water company's monthly use of SJWC service above that volume, which is calculated as the number of customers individually served by the mutual water company multiplied by 20 CCF.
5. The Elevation Charge specified in Special Condition 4 of Tariff Schedule No. 1C will be eliminated.
6. The rate design is reflected in the revised sample Schedule 1C for General Metered Service in the Mountain District, which is appended to this Settlement Agreement as Attachment A. Except as noted in items 1 through 5 above, the provisions of Schedule 1C will not be changed. Rates and charges set forth in the settlement agreement shall modified proportionately from the amounts stated therein in order to achieve the revenue requirement determined in accordance with the Commission's decision in this proceeding, except for the Overuse Rate, which the Settling

> Parties agree should be $7.00 per CCF. Revised rates are scheduled to become effective January 1, 2013, pending a timely Decision in this proceeding.

Upon careful analysis of the record and consideration of reasons for the parties' initial and revised estimates and rate design, we find that the partial rate design settlement agreement is a reasonable resolution of the issue, consistent with the law, and in the public interest. Pursuant to Rule 12.5 of the Commission's Rules of Practice and Procedure (Rules), the adoption of this settlement agreement does not constitute approval of any principle or issue in this proceeding and should not be cited as precedent in any future proceeding.

5. Overview of SJWC's and ORA's Positions

5.1. SJWC

In Application (A.) 12-01-003, SJWC requests an increase of $47,394,000 (21.51%) in 2013, $12,963,000 (4.87%) in 2014, and $34,797,000 (12.59%) in 2015, over currently authorized rates. After subsequent revisions during the pendency of this proceeding, SJWC's request for 2013 results in an increase in rates of 18.56%, slightly lower than in its original application. SJWC sees the main difference between it and ORA as the gap between long-term policy commitments and a short-term focus on minimizing costs. SJWC identifies the following as the key issues of contention:

1. State and Commission policies mandate water conservation, but limiting sales of a service that SJWC believes is heavily dependent on fixed cost investments necessarily means higher rates per unit sold. In forecasting sales, SJWC takes the water conservation policy into account, proposing aggressive new conservation programs and recycled water investments, and offering a three-tier conservation rate design tied to implementing a proposed Water Revenue Adjustment Mechanism (WRAM).

2. Another of what SJWC sees as a key Commission water policy is the wise investment in utility infrastructure. For SJWC, an almost 150 year old company with a stable service area, that policy translates into what it identifies as:
   a. A well-planned and prudent pipeline replacement program designed to maintain the replacement rate of 1% per year that the Commission authorized in SJWC's last GRC; and
   b. Plans to repair or replace aging tanks and reservoirs and to replace superannuated Motor Control Centers (MCCs) that are key components for several pumping stations.
3. SJWC's posits that it requires 23 new positions to implement public policies and mandates, such as: 1) application of water quality standards and conservation programs; 2) provision of high quality customer service, and safe and effective maintenance and operation of utility plant; and 3) response to other regulatory requirements and initiatives.

5.2. ORA

ORA recommends an increase of .05% in 2013, 3.73% in 2014, and 5.56% in 2015, over currently authorized rates. The following is a summary of ORA principal positions:

1. Approximately 75% or $222 million of SJWC's requested capital budget for the years 2012-2014 should be allowed in authorized rates.
2. Approximately 90% or $138 million of SJWC's estimated $153 million in operating, maintenance, administrative, and general expenses should be authorized in rates.
3. SJWC must not be allowed to carry forward tax losses to increase ratebase when the necessary offsetting entries that created the tax loss were never realized in rates.
4. Calculation of SJWC's ratebase must adhere to a reasonableness standard and therefore should incorporate

ORA's findings on working cash and depreciation reserves.

5. The extraordinary protection afforded by authorizing new memorandum accounts for potential recovery of SJWC's non-forecasted expenses is unwarranted and should be denied.
6. The significant and swift reduction in customer demand that has been achieved under SJWC's existing Monterey-Style WRAM invalidates the need for full decoupling.

6. Customers, Consumption, and Revenues

6.1. Operating Revenues

6.1.1. SJWC

SJWC estimates operating revenues at present rates for the years 2012 through 2015 based on the estimated average number of customer and estimated total water consumption and rates effective as of January 1, 2012.[6]

ORA argues that several adjustments must be made to accurately estimate test year revenues under present rates. These would include adjustments to: 1) all Contributions in Aid of Construction; 2) revenue collected from the "uplift charge" applied under the current Schedule 1C tariff; 3) revenue collected from the upsize meter charge; and 4) a service charge revenue increase collected under the Schedule 1C tariff.[7]

SJWC agrees with ORA's arguments on items (1), (3), and (4) above and has included these adjustments in the Test Year 2013 Present Rate Revenues included in the "SJWC Current" columns provided in the joint comparison exhibits. Even though SJWC disagrees with ORA regarding treatment of the

[6] Exhibit SJW-1, Chapter (ch.) 7 at 4.

[7] Exhibit ORA-1, ch. 2 at 4.

"elevation charge," because SJWC and Six Mutuals agreed to remove the elevation charge in their settlement agreement, SJWC believes this issue is moot.

6.1.2. ORA

To determine operating revenues, ORA used its recommended customer and consumption data and SJWC's existing authorized rates. ORA also made several adjustments to SJWC forecasts as discussed in detail below.

ORA posited that SJWC made a formula error in SJWC Workpaper 7-1E, by summing only a portion of the deferred revenues associated with Contributions in Aid of Construction. This adjustment would result in an increase in 2013 revenues under present rates of $212,902.

Because uplift charges of $0.7632/cubic feet (CCF) were not included by SJWC in its requested 2013 revenues, ORA added this figure, resulting in an increase to 2013 revenues at present rates of $70,091.

ORA also included the actual upsize meter charges that SJWC had excluded from test year revenue estimates. Based upon the existing tariffs authorized in Schedule 1B, test year revenues under present rates would increase by $83,330 in 2013.

ORA also recommends that the estimated service charge revenue for SJWC's Mountain District be consistent with SJWC's actual billing practices for the Mountain District. In particular, SJWC's authorized tariff Schedule 1C indicates that service charges for the Mountain District are based upon the number of ¾" meter customers that are individually served. In its adjustment, ORA replaced the two ¾" meter customers that SJWC had estimated for ratemaking purposes with the actual number of 446 ¾" meter customers that are individually served in this district. This adjustment would results in an increase to estimated revenues under present rates of $99,444.

6.1.3. Discussion

The Commission adopts ORA's recommendations regarding Contributions in Aid of Construction, revenue collected from the upsize meter charge, and increased service charge revenue collected under the Schedule 1C tariff, all of which SJWC agreed with. Because the Commission adopts herein the settlement between SJWC and the Mountain District, we find that ORA's concerns regarding the Mountain District's tariff (used by the Mutuals) are moot, and deny ORA's request regarding its recommended adjustment to the Mountain District tariff. The Commission therefore adopts Operating Revenues for 2013 of $250,377,000.

6.2. Consumption

6.2.1. SJWC

SJWC proposes that its estimates of water consumption recognize the policy of water conservation. As provided for in the Rate Case Plan for Class A Water Utilities, SJWC estimates water consumption for residential and business classes on a per customer basis utilizing the "New Committee Method." Following the Rate Case Plan guidelines for other sales categories, including Industrial, Public Authority, Resale, and Other classes, the calculated average annual sales by customer class were used to forecast future sales.[8] These sales estimates are then reduced by 1.5% a year based on SJWC's ongoing, and proposed, conservation measures as well as the Commission-ordered conservation goal of "a 1-2% annual reduction in consumption per service connection and customer class in CCF." SJWC states that its proposed adjusted

[8] Exhibit SJW-1, ch. 6 at 6.

sales forecasts is more accurate and reasonable than those proposed by ORA, and is based not only on a conservation adjustment, but also reflects a trend in sales due to continuing conservation, and thus SJWC's sales forecasts should be adopted.

ORA recommends removal of SJWC's proposed conservation adjustment from the water sales forecasts,[9] at 2, which SJWC posits is a result of inappropriate short term thinking that ignores both State of California requirements[10] and Commission policies,[11] both of which promote water conservation. SJWC posits that the current rate of conservation may be transitory, and may dissipate in the event an economic recovery or in the event that a plentiful water supply occurs. SJWC suggests that ORA would have to prove that SJWC could achieve the state and Commission's conservation goals without SJWC's proposed conservation program.[12]

SJWC goes on to state that its proposed conservation adjustment is not based solely on its requested expansion of its conservation program, but is also a result of its average trend in conservation over the last ten years, including environmental and legal requirements, local, regional, and statewide commitment to conservation, increased investment by SJWC in conservation activities starting in 2006 with its signing of the Memorandum of Understanding

[9] Exhibit ORA-1, ch. 2.

[10] http://www.swrcb.ca.gov/water_issues/hot_topics/20x2020/.

[11] http://www.cpuc.ca.gov/puc/hottopics/3water/051109_wateractionplan.htm.

[12] Exhibit SJW-10, ch. 4 at 2.

(MOU) with the California Urban Water Conservation Council (CUWCC), and increased conservation efforts from SJWC's water wholesaler.[13]

6.2.2. ORA

To forecast estimated water consumption, ORA used the same results achieved by SJWC's use of the "new committee method." However, ORA does not make an additional conservation adjustment to lower forecasted consumption, as SJWC does.

Where SJWC interprets the Commission's annual conservation goal of reducing consumption by 1%-2% as being additive to the State's goals, ORA believes that the 1%-2% percent annual reduction target set by the Commission is in place to meet California's 2020 goals. ORA also suggests that if water utilities have already achieved these goals and in recognition of the significant reductions in water consumption achieved by SJWC customers, further reductions in consumption would result in what ORA calls "rather illogical results."

Because ORA disagrees with SJWC's requested adjustment to consumption, ORA recommends consumption for 2013-2015 with no adjustment for further conservation. This results in an ORA recommendation of residential consumption of 174 CCF, 172 CCF, and 171 CCF for 2013, 2014, and 2015 respectively; and business consumption of 829 CCF, 819 CCF, and 809 CCF for 2013, 2014, and 2015 respectively.

6.2.3. Discussion

The Commission adopts SJWC's estimate of water consumption, and therefore SJWC's additional conservation adjustment to water sales. While

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13 Exhibit SJW-1, ch. 6 at 1 and 4.

further reductions in consumption are challenging, the Commission intends that conservation goals are critical to limited water resources and the adopted water consumption should recognize this purpose. The Commission therefore adopts an estimated water consumption of 53,202 MCF[14] for 2013.

6.3. Customers

6.3.1. SJWC

SJWC estimated customer additions for the Residential and Business classes using the three year (2009-2011) average increase and estimated the other customer additions using a three year (2010-2011) average increase. SJWC's Test Year 2013 customer forecasts are 196,962, 20,258, and 111 for the Residential, Business, and other customer classes respectively.[15]

ORA recommends the use of a five-year average to avoid having forecasts biased by the 2008-2009 economic recession and recommends a five-year average for the other customer class for consistency and to capture wider fluctuations in recorded data. ORA's Test Year 2013 customer forecasts are 197,345, 20,344, and 130 for the Residential, Business, and Other customer classes respectively.[16]

SJWC posits that by including the year 2007, ORA produces forecasts that are biased by the stronger economy prevalent before the 2008-2009 economic recession. Ben Bernanke, former Chairman of the Federal Reserve Bank, announced that he expects the Federal Reserve Bank to keep interest rates at their current low levels through to the end of 2014. Based on Chairman Bernanke's statement, SJWC believes that he expects an economic recovery to normal levels

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14 MCF stands for one-thousand cubic feet.

15 Exhibit SJW-2A at WP 7-3A and WP 7-12A.

16 Exhibit ORA-1, ch. 2 at 3.

will not occur through 2014. SJWC therefore recommends that its recommended three-year average percentage change from 2009-2011 provides a steadily increasing customer forecast that accounts for the slow economic recovery, which it sees as a more appropriate reflection of the underlying weakness of the economy.[17]

6.3.2. ORA

ORA disagrees with SJWC's use of two or three years of data to estimate customer growth in the current proceeding,[18] and recommends the use of a five-year average to determine future customer levels, in order to avoid having forecasts biased by the 2008-2009 economic recession. ORA recognizes that customer growth fluctuates from year to year, but believes that a consistent methodology should be used from rate case to rate case in order to avoid cherry picking of particular years for consideration in the forecast.

Based on its calculation of estimated growth, ORA forecasts total customers for 2013 of 223,000.[19]

6.3.3. Discussion

SJWC's use of a three-year average to project the number of customers are a useful indication of recent customer trends, while ORA's recommended use of

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[17] Exhibit SJW-10, ch. 5 at 7-8.

[18] In the current proceeding, SJWC estimated its customer growth for Residential and Business classes using a three year average increase (2009-2011) and estimated the its customer growth for Other Metered Services using a two year (2010-2011) average increase.

[19] The estimate of 223,000 customers consists of: Residential - 197,345; Business - 20,344; Industrial - 53; Public Authority - 1,283; Other - 130; Raw Water - 3; Recycled Water - 132; and Private Fire Service - 3,680.

a five-year average of the number of customers tends to capture economic changes over a longer period. In order to reflect the value of each methodology, the Commission adopts an average of both methods for estimating customers, except for recycled water customers, which we discuss separately below.

Accordingly, the Commission adopts the following customer estimates:

Residential	197,154
Business	20,301
Industrial	53
Public Authority	1,283
Resale	30
Other	112
Total Potable Metered Services	**218,933**
Raw Water	3
Recycled Water	132
Private Fire Service	3,624
Total Active Services	**222,692**

7. Recycled Water

7.1. Recycled Water Sales

7.1.1. SJWC

SJWC requests that its Recycled Water Program continue, which would result in an increase in total estimated recycled water usage from approximately

526,205 CCF in 2011 to 669,887 CCF in 2012, 942,911 CCF in 2013, 1,232,410 CCF in 2014, and 1,539,389 CCF in 2015.[20]

SJWC uses a simplifying assumption that there is a one-to-one offset between recycled and potable water. Under this methodology the estimated increase of recycled water sales to Business and Public Authority customers, from the 2011 recorded sales, is deducted as a one-to-one offset to the potable sales for these customers. So, if ORA's recommendations related to recycled water should be accepted, ORA's proposed deductions from 2013 through 2015 recycled sales forecasts should be 273,020 CCF, 562,520 CCF, and 869,500 CCF, respectively. Thus, in order to make the adjustment ORA recommends (in effect to set recycled water forecasts and potable sales offsets to 2012 levels) the deductions from Business and Public Authority potable sales (above the deductions for 2012) would need to be removed. Under this methodology, SJWC believes that the total sales (potable plus recycled) would stay the same whether or not ORA's recommendations are accepted, but the allocation of sales between potable and non-potable would need to be adjusted if SJWC's recycled program recommendations are not authorized for 2013 and 2014.[21]

7.1.2. ORA

Consistent with its recommendation to reduce the estimated number of service connections, ORA recommends that the Commission deny further investment by SJWC in its Recycled Water Program, including: 1) the removal of SJWC's reduction of 192,800 CCF in business class total sales; 2) the addition of

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[20] Exhibit SJW-1, ch. 20 at 21.

[21] Exhibit SJW-10, ch. 5at 8.

53 business customers forecasted to convert to recycled water customers in 2013; and 3) an increase in total sales to industrial customers by 48,900 CCF to reverse estimated recycled water substitutions in 2013.[22] SJWC agrees with ORA that if the Commission adopts ORA's recommendation to eliminate the Recycled Water Program after 2012, there will be a necessary offsetting adjustment to the potable sales estimates, but disagrees with the methodology proposed by ORA. The Commission therefore adopts Recycled Water Sales of 673 MCF for 2013.

7.1.3. Discussion

In recognition of the importance of recycled water as a low-cost alternative to potable water supply, the Commission adopts SJWC's request to continue its Recycled Water program. Although the Commission supports continuation of the Recycled Water Program, amounts adopted herein reflect ORA's reduced estimate of recycled water customers and consequently significantly reduced expense and plant by SJWC for recycled water due to uncertainties not yet resolved in the Commission's Rulemaking (R.) 10-11-014.

7.2. Recycled Water Plant and Expenses

7.2.1. SJWC

One of the most significant differences in this proceeding between SJWC and ORA is whether the Commission should approve certain recycled water projects including SJWC's proposed $31.55 million for water distribution mains over the years 2012 to 2014, and $15.9 million in operational and maintenance expenses for customer retrofits. The 2013 test year effect for the retrofit cost on conservation expense is $6,131,200.

[22] Exhibit ORA-1, ch. 2 at 4.

SJWC argues that its proposal is consistent with the Commission's encouragement of the increased use of recycled water and industry trends as reflected by the fact that water agencies in Santa Clara County are in development of recycled water infrastructure projects. SJWC points out that the Commission adopted three recycled water project alignments in D.09-11-032, SJWC's last GRC, for construction in 2009-2011. In this proceeding SJWC proposes to construct four alignments.

In previous years the South Bay Water Recycling Program (SBWR) provided funding for customer retrofitting of systems to accept recycled water. However as explained by SJWC[23] because water discharge requirements are being met, SBWR no longer funds this activity. In order to continue installation of these retrofits, SJWC requests that these unfunded retrofit costs be included in conservation expenses. SJWC argues that it is a common practice for recycled water retailers to pay such costs and that without the retrofits the remainder of the recycled water system may be stranded or underutilized.

7.2.2. ORA

ORA does not oppose recycled water construction or the addition of recycled water customers. However, ORA contends the 2010 Urban Water Management Plan (Plan) shows recycled water usage in 20 years equivalent to SJWC's proposed 2015 recycled water use and, according to ORA, four alignments will allow SJWC to meet its recycled water usage goals for 2015 as described in the Plan. In addition, ORA notes that the Commission in R.10-11-014 is developing the necessary criteria for evaluating recycled water

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[23] Exhibit SJW-1, chap. 20, at 11.

projects, and should not unnecessarily move forward on new projects until such criteria are developed.

In addition, ORA recommends against any funding by SJWC of the retrofit costs. ORA contends that an evaluation of other recycled water retailers indicates that the reasons for retailers funding customer retrofitting costs does not exist for SJWC.

7.2.3. Discussion

While the Commission fully supports the development and use of recycled water and has stated this policy in its adopted 2010 Water Action Plan, the Commission is also in the process of developing reasonable criteria for a policy framework, including cost allocation, for recycled water. As the Commission explained in R. 10-11-014,[24] one of the issues is "Determination of how costs of recycled water infrastructure should be allocated among stakeholders, including customers, investor-owned utilities (IOUs), and public agencies not regulated by the Commission." While SJWC's recycled water proposal indicates a furtherance of the Commission policy supporting the use of recycled water, at this time it is premature to allocate recycled water costs, or consideration of retrofit costs as SJWC proposes. Furthermore, it is uncertain whether the Commission will consider recycled water costs as a form of conservation, a reduction in potable water expense, or some other cost recognition mechanism. For these reasons, the Commission adopts ORA proposal to include the recycled water costs for the four alignments in this GRC. SJWC may request costs for other recycled water alignments and consideration of retrofit costs in a future GRC.

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[24] R.10-11-014 at 7.

Accordingly, the Commission adopts recycled plant amounts of $5,717,000 for 2012, and $0 for 2013 and 2014. Furthermore, as all recycled water expense estimates relate to operation and maintenance expenses for customer retrofits, and as the Commission is not adopting any customer retrofit costs at this time, no recycled water expenses are included in Test Year amounts.

8. Water Supply Portfolio

8.1. SJWC

SJWC's potable water supply portfolio consists of three sources - purchased water from SJWC's water wholesaler Santa Clara Valley Water District (SCVWD) pumped water from the groundwater basin (which is also managed by SCVWD), and treated surface water from SJWC's Montevina and Saratoga water treatment plants (WTPs).[25] SJWC forecasts the purchased water amount based on the purchased water take-or-pay contract with SCVWD and the surface supply amount based on historical surface supply production adjusted to account for reduced capacity of the Montevina WTP due to water quality restrictions and during planned upgrades to the facility. The pumped groundwater is then forecasted as the marginal source of supply making up the difference between total supply necessary (i.e., potable water sales plus unaccounted for water) and purchased water plus surface water.[26]

SJWC estimates that the total WTP capacity will be reduced by approximately 60% from 2013 through 2015 while upgrades to the Montevina

[25] Exhibit SJW-1, ch. 3 at 2.

[26] Exhibit SJW-1, ch. 7 at 4.

WTP are completed. This 60% reduction is accounted for in SJWC's surface supply estimate of 1,827 MCF in Test Year 2013.[27]

ORA agrees with SJWC's purchased water forecast, and agrees that pumped water should be the marginal supply. However, ORA makes two adjustments to SJWC's surface supply forecast: 1) correction of what ORA identifies as a "mathematical impossibility" in recorded surface water production in 2007; and 2) assuming a 49% capacity reduction to the Montevina WTP.[28] SJWC states that it did not make a mistake, but actually did produce only 1,051 million gallons (MG) from SJWC's surface supplies on the Los Gatos Creek and Saratoga Creek systems in 2007. SJWC's Montevina WTP also produced an additional 774 MG from the neighboring Lexington Reservoir, which is owned by SCVWD and was recorded as purchased water to accurately reflect the short-term contractual arrangement between SJWC and SCVWD during 2007. Because SJWC has no future contracts with SCVWD to purchase and produce surface water from Lexington Reservoir, and does not anticipate any production from Lexington Reservoir during 2012-2014, SJWC believes that the 1,051 MG figure for 2007 is the correct value for the total surface water production from SJWC's sources, and is appropriate to use for forecasting purposes.[29]

SJWC also posits that ORA used an inappropriate argument for available water treatment processing capability at the Montevina WTP when assuming that available processing capacity would be reduced by 49% of normal during construction. SJWC's estimated 60% reduction in annual production during

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[27] Exhibit SJW-1, ch. 7 at 4.

[28] Exhibit ORA-1, ch. 2 at 5.

[29] Exhibit SJW-10, ch. 3 at 3-2.

construction at the Montevina WTP is an estimate based on several conditions that will exist during construction of the plant improvements, including: 1) reduced hydraulic capacity by half; 2) loss of usable high turbidity water due to the repurposing of the off-spec water diversion basin (which allows temporary diversion of water) during construction; and 3) both short-term and full plant outages which will cause further production losses. Considering all of these factors, SJWC posits that a 60 % reduction in annual production during construction at the Montevina WTP is a correct and appropriate measure.[30]

8.2. ORA

Both ORA and SJWC estimate test year surface water production based upon the five-year average of recorded production. ORA has increased the forecast of surface water to reflect updated information provided by SJWC in the current proceeding. ORA increases the 2011 production amount, which had been estimated in SJWC's application to be consistent with the actual recorded production that SJWC provided in its updated work papers. This adjustment results in a 1% increase in forecasted surface water production.

ORA conceded during hearings that the additional surface water which ORA imputed for 2007 to arrive at its five-year average of surface water production was purchased from surface water, ORA stated that such water cost more than regular surface water that SJWC would have available.

ORA compared the recorded data on surface water supply that SJWC submitted in the current proceeding (1,051 MG/year) with data SJWC submitted in A.10-09-019 on the production of surface water (1,742 MG/year). ORA also

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30 Exhibit SJW-10, ch. 3 at 3.

discovered that production previously reported for just one of SJWC's two surface water treatment plants, the Montevina WTP, exceeded the entire amount of surface water that SJWC reported for 2007 in the current proceeding. To rectify what it identifies as an inconsistency, ORA proposes that the 2007 Montevina production be divided by the 10 year average Montevina WTP production as a percentage of total surface water production. This calculation results in 2007 surface water production of 1,909 MG/year, or a 5% increase in forecasted surface water production.

ORA also adjusted SJWC's estimate of surface water production based on the assumption that during construction at Montevina, capacity will be reduced. Due to these proposed facility upgrades, which are the subject of A.10-09-019, SJWC estimates that capacity will be reduced by approximately 60%, compared to ORA's recommended reduction of 49%. ORA states that its recommendation more closely aligns with SJWC's opening brief in A.10-09-019 where, in support of its requested ratemaking treatment, SJWC indicated that "the plant will, in fact, be operating throughout the time when water is available for processing through the plant, subject to occasional interruptions due to construction activity." ORA also states that its recommendation equates to Montevina being used and useful just slightly over a majority of the time. ORA posits that it would be an error to reduce total surface water production by the same percentage reduction that is estimated to impact only the Montevina WTP. This is because the remaining average 9% of surface water production would be unaffected by Montevina facility upgrades. Therefore, ORA recommends reduction to total surface water production of 44.5%.

In aggregate, ORA's corrections and recommended adjustments to SJWC estimates of water supplies would result in a decrease of approximately

$1,111,000 in expense due to the increased availability of lower-cost surface water forecasted in the test years.

8.3. Discussion

Although SJWC's explanation of the unusual surface water production in 2007 may be correct, as SJWC offers, this was an unusual event. Thus 2007 surface water production should not be used in forecasting surface water production for 2013. Therefore, a reasonable forecast should exclude 2007 from the estimated surface water production and use the remaining years of 2000-2010 for this forecast.

Neither SJWC's nor ORA's recommended forecasts of water production from the Montevina WTP are compelling. SJWC's statement in A.10-09-019 suggests occasional interruptions in production, but this is not supportive of a 60% reduction in capacity over a full year cycle. However, ORA's calculation of a 49% reduction does not reflect many of the construction outage events that contribute to the overall capacity reduction calculation. Therefore, the Commission adopts a 55% reduction in the Montevina WTP in its calculations of surface water production for Test Year 2013. In recognition that Montevina WTP produces 91% of the surface water production, the Commission also applies the additional 9% remainder to this calculation resulting in an overall reduction in surface water production of 50% due to the construction effects of the Montevina WTP. As a result, the Water Supply Portfolio for 2013 consists of: Purchased Water of 29,388 MCF; Surface Water of 2,794 MCF; and Well Production of 24,779 MCF.

9. Customer Growth and Escalation Factors on Expenses

As explained by SJWC, its estimating method includes a 0.3% per year customer growth rate as well as escalation factors in making expense estimates.

SJWC relies on the escalation discussion in D.07-05-062, Attachment A at A-19 for support in applying customer growth to expense estimates. However, a plain reading of D.07-05-062 shows that the Commission did not apply customer growth to test year expenses but instead applied the customer growth to expenses in escalation years following the test year. Therefore, the Commission has eliminated customer growth as a factor in all test year expenses.

10. Labor and Payroll

10.1. SJWC

SJWC estimated employee payroll for Test Year 2013 by indexing the beginning of year 2012 total annual payroll expense (includes 355 existing employees) by the union contract escalation rate of 3% for union employees and 5% for administrative employees and officers. The 355 current positions include four positions added to support SJWC's Capital Improvement Plan. An additional 23 positions are proposed for Test Year 2013.[31]

SJWC based its test year forecast of payroll expense on what it considers the most recent payroll information, and escalating by the union contract escalator for union employees[32] and a 5% factor for administrative employees and officers.

SJWC conducted a compensation study on wages and benefits provided by comparable utilities, which reflected that SJWC was paying union employees an average of 95.8% of what the average peer group was paid; paying

[31] Exhibit SJW-1, ch. 5 at 1-8.

[32] SJWC also noted that its union agreement provided for annual contract wage increases of 2%, 2%, and 3% respectively for the years 2011, 2012, and 2013, just slightly above the ORA Energy Cost of Service Branch forecast amounts of 1.6%, 1.6%, and 1.9%, respectively.

administrative employees an average of 90% of comparable averages without bonus and 92% with bonus; while the corresponding figures for officers were 88% and 103%, respectively. The study also showed that SJWC's officers were paid between the 50th and 75th percentile of the peer group after a cost of living factor was applied.[33]

SJWC disagrees with ORA's exclusion of officers' bonuses and "other compensation" from their recorded 2011 base salaries, stating that SJWC follows a philosophy of paying its officers based on their performance and without these bonus, annual salaries would have to be increased.

SJWC also challenged ORA's exclusion of temporary and part-time help from payroll expense, stating that temporary labor is provided for in its union contracts to provide relief during peak summer months and during extended absences and allows SJWC to complete preventative maintenance projects during peak periods at much lower cost than that of full-time employees in terms of both wages and benefits. SJWC states that it has historically included forecasted expense for part-time and temporary help in its GRCs and consistently has been authorized some level of recovery for such costs. SJWC requests that the $192,000 included in SJWC's Test Year 2013 payroll estimate for temporary and part-time labor should be allowed.

SJWC also believes temporary vacancies that occur due to the bid process required by the union contract, which allows existing union employees to try-out for a new or vacant position, impact the need for additional positions. If the try out is unsuccessful, the employee returns to his or her prior position and the bid process may have to be repeated several times. SJWC posits that any short-term

[33] Exhibit SJW-10, ch. 8 at 8-1 to 8-3.

savings associated with vacant positions are offset by the cost of new positions. SJWC' witness testified that ORA's exclusion of $286,000 of 2011 labor expense related to Non-tariffed Products and Services (NTP&S) from the base for forecasting test year payroll cost was not in compliance with the applicable Affiliate Transaction Rules (ATRs),[34] and that SJWC states that it would incur these labor costs with or without provision of NTP&S.

In addition to the four new positions added as of 2012, SJWC proposes addition of 23 more new positions in Test Year 2013. ORA recommends allowing only three of the 27 new positions -fewer than SJWC already has added as of 2012, by applying SJWC's customer growth rate of 0.3% per year to SJWC's 351 employees as of 2011 to recommend adding three new positions through 2015.[35] SJWC posits that this is not a sound basis for decision in this case, because the referenced settlement agreement was expressly non-precedential with respect to any disputed matter of fact or law.[36] SJWC believes that the four positions not presently authorized were added out of great need and one of those positions, the new Electrical Engineer, has already produced significant cost savings.[37]

SJWC posits that its request for 23 new positions is driven primarily due to "increasing regulatory requirements in multiple areas, growing infrastructure and capital replacement needs, technological advances, the implementation of a water recycling distribution system, and a shift to higher skills and aptitudes

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34 Exhibit SJW-10, ch. 5 at 5-35.

35 Exhibit ORA-1, ch. 3at 3-19; and Tr. 237:22-238:13.

36 *See* D.09-11-032, Appendix B at §11.2.

37 Exhibit SJW-1, ch. 8 at 8-4 to 8-7.

from routine tasks."[38] SJWC requests that the Commission allow the inclusion in test year payroll expense of the four positions added in 2011 and the 23 new positions requested for 2013, for a total of 378 positions in Test Year 2013.

10.2. ORA

ORA estimates its recommended 2013 payroll expense by escalating SJWC's 2011 adjusted payroll expense for all SJWC employees by 2% for 2012 and 3% for 2013.[39] For 2014 and 2015, ORA estimates labor escalation factors of 1.8% and 2%, respectively.

ORA's adjustments to the 2011 payroll expense consist of: 1) exclusion of 2011 recorded expenses related to temporary and part time help that was not authorized by the Commission: 2) exclusion of expenses related to four additional employees not authorized by the Commission; 3) reduction of $285,967 to account for NTP&S performed by SJWC employees; and 4) exclusion of expenses related to vacant positions.

ORA also posits that SJWC's request that officer bonuses be 100% guaranteed provides "little incentive to operate efficiently and should not be permitted in rates."[40]

ORA opposed SJWC's forecasting methodology for payroll expense on various grounds, starting from using a different base year (2011), making a number of adjustments to exclude amounts from the base, and applying lower escalation rates to forecast test year expense. ORA also proposed to disallow

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[38] Exhibit SJW-1, ch. 8 at 4-8.

[39] ORA states that the 2% and 3% wage adjustments are based on existing collective bargaining agreement with union employees.

[40] ORA Opening Brief at 7.

24 out of 27 of the additional positions recently added or proposed by SJWC. The result was a test year payroll expense estimate nearly $2,740,000 (7.7%) lower than SJWC's estimate of $35,300,000.[41]

To estimate payroll expense for 2012, ORA applied a 2% escalation factor for all employees and officers, even though the actual increases in compensation for administrative employees and officers were higher. ORA also excluded all costs for temporary or part-time employees, for temporarily vacant positions, for labor related to NTP&S, and for the four positions SJWC added in 2012. ORA then escalated this 2012 estimate by the 3% union contract escalator to reach a payroll expense forecast for Test Year 2013.[42]

10.3. Discussion

The Commission adopts SJWC's payroll expense estimates using the 3% increase for union employees and 5% increase for administrative employees and officers. The application of the 3% increase recognizes the current contract escalator,[43] while use of the 5% escalation rate for administrative employees and officers is a reasonable estimate reflecting historical trends.

The Commission adopts 4 of the 27 new positions requested by SJWC for test Year 2013 expenses. The Commission includes these 4 positions as this reflects the actual addition of employees to SJWC's payroll in 2012, the increase in staff that might be expected given the growth in customers, currently funded but vacant positions, and the adopted estimates in this decision for capital

[41] Exhibit ORA-1, ch. 3 at 1.

[42] Exhibit ORA-1, ch. 3 at 3-13 to 3-18.

[43] This is the escalation rate also used by ORA for escalating union payroll from 2012 to 2013.

projects. In using this estimate, the Commission does not base its exclusion of the 23 other positions on ORA's argument which relies on the previous settlement adopted in D.09-11-032, as any settlement is a result of the negotiations and circumstances which apply to that proceeding.

The Commission excludes expenses related to temporary, part-time, and vacant positions, as such does not provide continuous or any benefit to ratepayers.

The Commission also excludes amounts for NTP&S in making payroll estimates. In D.10-10-019, the Commission stated that "it is not reasonable to allow a water or sewer utility to carry extra employees or put into rates additional labor costs which are not necessary for the provision of regulated utility service, in order to provide NTP&S."[44] Accordingly the Commission will exclude NTP&S amounts in its payroll estimates.

The Commission will not adopt SJWC's proposed officer bonus amounts in payroll expenses. As discussed herein, the Commission has increased such salaries by 5% as opposed to the 3% increase in such salaries proposed by ORA. This overall increase for all salaries provides SJWC an opportunity to provide lesser increases for some administrative and officer employees and greater increases for other administrative and officer employees should SJWC determine that a bonus compensation is deserved for certain employees.

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[44] *See* D.10-10-019 at Finding of Fact 37.

11. Pension and Benefits

11.1. Forecasting Methodology

11.1.1. SJWC

SJWC forecasts Pension and Benefit (P&B) expenses utilizing various methodologies based on the specific expense forecasted for each sub-account discussed below. Forecasted expenses as provided in SJWC's application were based on annualized 2011 estimates.[45] SJWC has corrected inflation factors for 2012 and 2013.[46]

11.1.2. ORA

ORA estimates total P&B expenses of $15,149,600, which is $3,820,400 less than SJWC's request. ORA generally uses the actual recorded data from the 45-day update for 2011 as the basis to estimate P&B expenses for 2013. For 2013, ORA applied only an inflation factor, while it included both inflation factor and customer growth to derive 2014 and 2015 P&B estimates. ORA believes that SJWC applied the incorrect annual escalation factors to all P&B forecasts, and reflected this adjustment for this in its recommendation.

ORA argues that for 2012 and 2013 P&B forecasts, except Post-Retirement Benefits other than Pensions, SJWC applied incorrect escalation factors to arrive at forecasts.[47]

11.1.3. Discussion

The Commission adopted P&B expenses to reflect the corrected 2011 recorded year amounts increased by the corrected inflation factors for

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45 Exhibit SJW-2, ch. 9 at WP 9-7.

46 Exhibit JCE-2, Table 2 at 4, lines 56-66.

47 Exhibit ORA-1, ch. 4 at 1-2.

2012 and 2013, but as explained previously P&B expenses do not include a customer growth factor. In total, the Commission adopts Pension and Benefits of $12,507,000 for 2013.

11.2. Retirement Plans

11.2.1. SJWC

SJWC recommends that the Commission adopt a Test Year 2013 Retirement Plans expense of $9,721,820, based on the 2012 actual Retirement Plans expense of $9,466,297 provided in SJWC's March 22, 2012 actuarial report, escalated by the weighted escalation factor and a customer growth factor.[48]

SJWC posits that ORA's recommendation of $7,384,000 for SJWC's 2013 Retirement Plans expense is improbable, as it would result in a decrease of $2,082,000 from the 2012 recorded cost of $9,466,000.[49] SJWC states that increases in service costs – a major component of pension expense – are not temporary or a result of financial downturn, but are a result of changes in employee participant's salaries, which are not likely to decrease on the order necessary to precipitate a reduction in the Retirement Plans expense as proposed by ORA. SJWC also states that unamortized losses due to investment losses during the financial downturn totaling $41.7 million in 2012 need to be recovered. In order for the Retirement Plans expense to drop to the ORA-recommended forecast of $7,384,000, expected return on assets would need to exceed $30,000,000 in 2012 to offset the existing loss balance being amortized, which SJWC believes is unlikely.

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[48] SJWC updated its original forecast, which was based on the best estimate available at the time of SJWC's January 3, 2012 application filing, to reflect the final actuarial report. *Reference:* Exhibit SJW-1, ch. 9 at 3; and Exhibit SJW-10, ch. 8 at 9-2 to 9-3.

[49] Exhibit SJW-10, ch. 9 at 9-4.

11.2.2. ORA

Retirement Plan expense refers to expenses for the qualified plan that covers all employees. It consists of a Defined Benefit Pension Plan and a Supplemental Executive Retirement Plan. ORA estimates Test Year 2013 Retirement Plan expense of $7,384,000, based on a five-year average of 2008 to 2011 recorded data and actuarial estimates for 2012. ORA then applies a 2013 inflation factor to the five-year average to derive the Test Year 2013 expense forecast.[50]

ORA posits that by using a five-year average, its estimate normalizes the high and low amounts and reduces the effects of fluctuations for this expense item. By incorporating both the variation in past recorded pension expense and the most recent actuarially determined estimate for 2012, ORA believes its methodology is a more reasonable methodology than simply escalating the actuarial estimate of just one year.

11.2.3. Discussion

The Commission-adopted amounts for P&B Retirement Plan expenses reflect SJWC's 2012 actuarial report adjusted to eliminate the customer growth escalation effect. While ORA proposed use of a five-year average for Retirement Plan pension and benefit estimates adjusts for fluctuations in recorded amounts, SJWC's 2012 actuarial report is a more accurate expectation of pension and benefit costs in the test year as the purpose of an actuarial report is to evaluate current and future employee retirement costs based on statistical expectations.

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50 Exhibit ORA-1, ch. 4 at 4-3 to 4-5.

The Commission therefore adopts Retirement Plan costs of $9,663,837 Test Year 2013.

11.3. Retirement Savings Plan

11.3.1. SJWC

SJWC requests P&B Retirement Savings Plan expense of $1,118,000 compared to ORA's proposal of $1,030,000. SJWC agrees with ORA that the P&B Retirement Savings Plan expense should be based on a percentage of payroll, but SJWC uses forecasted payroll to arrive at the estimated 2013 expense.[51] The other difference between the parties with respect to SJWC's requested P&B Retirement Savings Plan expense is SJWC's inclusion of a customer growth factor.

11.3.2. ORA

Retirement Savings Plan is the employer matching contributions to the 401K plan. ORA estimates a Test Year 2013 Retirement Savings Plan expense of $1,030,300. Because the Retirement Savings Plan expense is impacted by payroll expense, ORA computed the average ratio of recorded Retirement Saving Plan expense to recorded Total Payroll expense for the five-year period 2007 to 2011. ORA then applied this computed average of 3.1636% to its estimate of Total Payroll to derive its 2013 estimate. The same 3.1636% was applied to projected payroll expenses for escalation years 2014 and 2015 to arrive at the Retirement Savings Plan expenses for these years.

ORA believes that SJWC: 1) incorrectly applied the 2014 inflation factor and 2012 customer growth to bring 2011 the expense up to 2012; 2) incorrectly applied the 2014 inflation factor and 2013 customer growth to bring the 2012

[51] Exhibit SJW-10, ch. 9 at 5.

expense level to the estimated Test Year 2013 expense forecast; and 3) correctly applied customer growth and inflation factors to determine escalation years 2014 and 2015 Retirement Savings Plan expense.

11.3.3. Discussion

The Commission adopts an amount of $1,063,900 for Retirement Savings Plan expense based on ORA's recommended 3.1636% of total adopted payroll. This amount excludes the customer growth factor discussed above. This results in an authorized Retirement Savings Plan expense of $1,063,900 for 2013.

11.4. Employee Stock Purchase Plan

11.4.1. SJWC

The only difference between the parties with respect to SJWC's Employee Stock Purchase Plan expense is SJWC's inclusion of a customer growth factor.[52] If the Commission authorizes the inclusion of the customer growth factor as proposed by SJWC, SJWC believes that its Employee Stock Purchase Plan expense estimate of $123,000 should also be approved.

11.4.2. ORA

ORA's estimate for the 2013 Employee Stock Purchase Plan expense is $122,000, which is $1,000 less than SJWC's estimate. The difference results from ORA's use of SJWC's updated recorded data for 2011, as well as the use of what ORA identifies as the correct annual inflation factors.

11.4.3. Discussion

The difference between ORA and SJWC regarding the Employee Stock Purchase Plan is the escalation proposed by SJWC for customer growth. As the

[52] Exhibit SJW-10, ch. 9 at 9-5; Exhibit ORA-1, ch. 4 at 4-6.

Commission is excluding customer growth, the adopted amount is ORA's estimate of $122,000.

11.5. Unfunded Pension Expense

Parties agree to a Test Year 2013 Unfunded Pension Expense of $56,000, and we adopt it as reasonable.

11.6. Post-Retirement Benefits Other than Pensions

11.6.1. SJWC

SJWC recommends that the Commission adopt a Test Year 2013 Post-Retirement Benefits Other Than Pensions (PBOP) expense of $1,060,740, based on the 2012 actual PBOP expense of $1,032,854 provided in SJWC's March 22, 2012 actuarial report, escalated by the weighted escalation factor and a customer growth factor.[53]

By contrast, ORA calculated SJWC's Test Year 2013 PBOP expense based on the five-year average of 2008 to 2011 recorded data and actuarial estimates for 2012.[54]

SJWC believes that ORA's averaging results in a recommendation that is lower than SJWC's 2012 recorded cost of $1,032,854, is highly unlikely.[55] And as with other P&B costs, SJWC states that PBOP expense increases over the 2008 to 2012 period were largely attributable to the amortization of unrecognized losses due to asset investment losses in 2009 and 2012. In order for the PBOP expense to decrease dramatically enough to meet ORA's recommended PBOP expense amount, SJWC posits that the expected return on assets would need to exceed the

[53] Exhibit SJW-10, ch. 9 at 9-7.

[54] Exhibit ORA-1, ch. 4 at 4-7.

[55] Exhibit SJW-10, ch. 9 at 9-6.

current loss balance being amortized (which is $3,900,000) by $151,000 for 2012. SJWC believes this event is unlikely, therefore, SJWC requests that the 2012 PBOP expense, as presented on SJWC's March 22, 2012 actuarial report, should be the basis for forecasting PBOP expense, upon which the weighted escalation factor and a customer growth factor should be applied, to reach a Test Year 2013 PBOP expense of $1,060,740.[56]

11.6.2. ORA

Similar to the methodology it employed to calculate SJWC's forecasted Retirement Plan expense, ORA uses the five-year average of actual recorded expense from 2008 to 2011 and the actuarial estimate for 2012 to derive its recommended forecast of PBOP expense of $$887,000. ORA believes this is a more reasonable methodology than SJWC's use of one year of actuarial data, because ORA's method incorporates both past recorded data with actuarial estimates.

11.6.3. Discussion

As discussed above, the Commission adopts retirement related costs based on SJWC's 2012 actuarial report adjusted to exclude the customer growth factor. Consistent with that methodology, the Commission adopts a PBOP amount of $1,030,300.

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[56] Exhibit SJW-10, ch. 9 at 9-7.

11.7. Life Insurance

11.7.1. SJWC

The only difference between the parties with respect to SJWC's requested Life Insurance expense regarding SJWC's inclusion of a customer growth factor.[57] If the Commission authorizes the inclusion of the customer growth factor as proposed by SJWC, its Life Insurance expense estimate (as presented in its rebuttal testimony) is $179,000.

11.7.2. ORA

ORA's estimate for the 2013 Life Insurance expense of $178,000 is $1,000 less than SJWC's estimate. ORA uses SJWC's updated recorded data for 2011 and what it identifies as the correct annual inflation factors.

11.7.3. Discussion

The Commission's adopts a Life Insurance expense estimate of $178,000 based on ORA's updated data, because it does not add a customer growth factor to the estimate.

11.8. Medical Insurance

11.8.1. SJWC

SJWC estimated its forecast for Test Year 2013 Medical Insurance expense of $4,982,000, using a 9% escalation factor.[58] In rebuttal testimony, SJWC clarified that the 9% five-year average represented in SJWC's Application is not a composite of premium rate increases across for past providers, but is based only on premium rate increases for the Kaiser HMO plan the company experienced

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[57] Exhibit SJW-10, ch. 8at 8-19; and Exhibit ORA-1, ch. 4 at 4-8.

[58] Exhibit SJW-1, ch. 9 at 2.

over the 2007-2012 period.[59] SJWC posits that ORA's did not understand that this 9% escalation factor represented the five-year average of premium rate increases for past SJWC health care providers, and believes ORA's recommendation is not appropriate.

SJWC believes that it is entirely appropriate to use the 9% escalation factor, the five-year average of increases for the Kaiser HMO plan – to forecast SJWC's Medical Insurance expense of $4,981,900 for Test Year 2013.

11.8.2. ORA

ORA estimates Kaiser Medical Insurance of approximately $4,430,000, which is $552,000 less than SJWC's request. ORA's estimate is based on an increase factor of 4.29%, which ORA believes is consistent with actual trends and published expectations. ORA states that this factor is consistent with the health insurance premium increases projected by IHS Global Insight.

ORA instead recommended that the Test Year 2013 expense be derived by applying the most recent (for the period 2011/2012) percentage increase in premiums for Kaiser only (for the period 2011/2012), which is 4.29% to arrive at an its estimate of $4,429,900, is not appropriate.[60]

ORA also posits that the difference between it and SJWC's estimate is due to what ORA identifies as errors in escalating base amounts and SJWC's use of an additional increase factor of 9% per year.

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[59] Exhibit SJW-10, ch. 8 at 8-19 to 20; and Exhibit SJW-1, ch. 5 at 9-10.

[60] Exhibit ORA-1, ch. 4 at 4-8 to 4-9.

11.8.3. Discussion

ORA estimate for medical insurance reflects existing cost trends as well as expected health premium costs. Therefore, the Commission adopts an amount of $4,430,000 for medical insurance.

11.9. Health Savings Account

ORA and SJWC agree on a P&B Health Savings Account forecast of $65,000, an amount the Commission adopts as reasonable.

11.10. Dental Insurance

ORA does not object to the SJWC's estimate of $602,100 presented in rebuttal testimony.[61] The Commission adopts this amount as reasonable.

11.11. Other Employee Benefits

11.11.1. SJWC

SJWC estimates a Test Year 2013 forecast amount of $275,500 for Other Employee Benefits expense.[62] ORA recommends a Test Year 2013 forecast of $234,500 for Other Employee Benefits expense.[63]

SJWC believes that ORA's use of a ratio of Other Employee Benefits to Total Payroll does not provide an accurate measure of this expense, as Other Employee Benefits contains many items that fluctuate irrespective of the Total Payroll, such as the cost of mandated training and licensing for distribution and treatment licenses as well as the annual certified educational units required to maintain such licensing. Given the increase in regulatory requirements to

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[61] Exhibit SJW-1, ch. 5 at 10; and Exhibit SJW-1, ch. 9 at 2.

[62] Exhibit SJW-10, ch. 8 at 8-21.

[63] Exhibit ORA-1, ch. 4 at 4-11.

attain and maintain higher grades of certifications in this area, SJWC posits that this licensing expense continues to rise at a rate greater than that of Total Payroll.

SJWC also notes that Other Employee Benefits includes the cost of retiree functions – SJWC posits that this cost will continue to escalate with increased retirements over the next 10 years due to an aging workforce.[64]

11.11.2. ORA

ORA estimates Other Employee Benefits expense of $234,500. Because ORA believes that this expense is tied to payroll expense, ORA computed the average percentage, of recorded Other Employee Benefits to recorded Total Payroll expense for the five-year period 2007-2011. ORA then applied the computed average of 0.7199% to its estimate of Total Payroll to arrive at its recommended, Other Employee Benefit expense for test year 2013.

ORA also posits that the difference between it and SJWC's estimate is due to what ORA identifies as SJWC's errors in escalating base amounts that are based "on an annualized forecast of the 2011 expense level."

11.11.3. Discussion

While ORA ratio methodology between payroll, and Other Employee Benefits expense might be useful in another context, SJWC's method recognizes the changing effects of training, licensing and an aging employee workforce and thus is a more useful measure of these costs. Therefore, the Commission adopts SJWC's estimate of $275,500 for Other Employee Benefits expense.

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[64] Exhibit SJW-10, ch. 8 at 21.

11.12. Long-Term Disability Insurance

ORA and SJWC agree on an estimated $169,000 for this expense, and the Commission adopts it as reasonable.

12. Transportation Expense

12.1. Transportation Labor

12.1.1. SJWC

SJWC requests Transportation Labor expense of $397,000. SJWC accepts ORA correction of a $13,000 error in a "gross-up ratio" used in SJWC's spreadsheet formula.[65] The remaining $32,000 of the difference between SJWC's and ORA estimates[66] is due to the differing payroll estimates, which have already been discussed in Section 9 herein.

12.1.2. ORA

ORA recommends Transportation Labor Expense of $352,000 for Test Year 2013, compared to SJWC's request of $397,000. ORA applies the same methodology used by SJWC to estimate Transportation Labor,[67] but corrects what it identifies as an error in the gross-up ratio used in SJWC's spreadsheet formula for the Test Year and Escalation Years, which SJWC accepts.

12.1.3. Discussion

As both ORA and SJWC use adopted payroll to determine transportation labor, the Commission applies its adopted payroll to determine transportation

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[65] Exhibit ORA-1, ch. 5 at 5-16 to 5-17.

[66] Exhibit JCE-2, at 2, line 4.

[67] Transportation Labor Estimation Method - utilizes the recorded 2011 amount increased by the same percentage increase estimated for total Labor expense (from 2011 to the forecast year).

labor expense. The amount is corrected by the $13,000 error recognized by SJWC and ORA, and results in transportation labor of $ 369,700.

12.2. Transportation Payroll Tax

12.2.1. SJWC

After a pair of corrections in SJWC's update filing identified by ORA, the remaining difference between SJWC's and ORA estimates of $25,000 for Transportation – Payroll Taxes is due to the differences in their respective payroll estimates, which has already been discussed in Section 9 herein.[68]

12.2.2. ORA

ORA's recommendation of $197,000 for Transportation Payroll Tax is based on its lower Transportation Labor expense recommendation. Additionally, ORA recommends two corrections in SJWC's Application work papers, regarding an item in SJWC's 45-Day Update,[69] an incorrect cell reference in the formula used to calculate Total Expense Payroll in SJWC's originally filed work papers. SJWC accepted both of these proposed corrections.

12.2.3. Discussion

The Commission's adopted Transportation Payroll Tax is proportional to the Commission's adopted transportation labor expense, after correcting for the 45-day update item and the incorrect reference used in SJWC's work papers. This adopted Transportation Payroll Tax is $207,000.

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[68] Exhibit ORA-1, ch. 5 at 5-17 and Exhibit JCE-2, at 2, line 5.

[69] The first error discovered by ORA was in SJWC's calculation of the percentage increase in Labor expense to be applied to previous years Payroll Taxes expense to arrive at the current year's Payroll Tax estimate. At ORA's request SJWC's 45-Day Update corrected this error.

12.3. Transportation Insurance

12.3.1. SJWC

The $6,000 difference between the parties' estimates for this expense is due primarily to SJWC's calculation based on the recorded 2011 expense escalated to the test year, while ORA averaged the expense for 2010 and 2011, escalating that figure.[70] SJWC posits that the 2010 expense considered by ORA is an outlier year which is substantially lower than the four previous years and the 2011 expense.[71]

12.3.2. ORA

ORA estimate of Transportation Insurance of $104,400 is based on a two-year average (2010-2011) plus escalation. ORA uses a two-year average, because it believes the forecast on a one-year data point does not accurately reflect the fluctuating trend exhibited in the recorded cost data of this account. In its rebuttal, SJWC stated that ORA did not escalate the recorded 2010 figure before calculating its two-year average. ORA agreed to correct this oversight, adding $2,400 to its original $102,000 recommendation.

12.3.3. Discussion

As the use of a two-year average as recommended by ORA reduces the effects of fluctuating expenses, the Commission adopts ORA's proposed amount of $104,400 for this expense.

12.4. Transportation Fuel

12.4.1. SJWC

SJWC's projected purchased fuel expense of $848,000 is based on recorded 2011 expenses escalated by a 15% annual escalation factor derived from historical

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[70] Exhibit ORA-1, ch. 5 at 5-17 to 5-18.

[71] Exhibit SJW-10, ch. 5 at 5-12.

increases (averaging 16%) during the five-year period 2007-2011.[72] SJWC also explained that it anticipates increased fuel usage due to SJWC doing more "heavy equipment work," increased staff, and addition of emergency generators.

In rebuttal testimony, SJWC explained that in recent years, it has increased the amount of self-performed heavy equipment and truck work which results in the use of more fuel.[73] SJWC also stated that its compliance with more stringent emissions controls applicable to its 24 diesel-powered trucks has increased fuel use and that, due to Ford's discontinuance of a fleet program for its Escape Hybrids, SJWC plans for a slight decrease in the number of hybrid vehicles in its vehicle fleet.

Thus, based on recorded experience in the base period and ongoing trends due to regulatory and market factors, SJWC believes it has justified the 15% annual escalator included in its estimate of Transportation – Fuel expense of $848,000.

12.4.2. ORA

ORA recommends Transportation Fuel Expense of $563,000, based on a recorded five year average of fuel cost plus an escalation factor. ORA uses such a long average because of significant fluctuations in fuel cost from year to year, ranging from -30% to +42%. ORA also adjusts SJWC's request based on: 1) ORA's consideration of the more fuel efficient vehicles that will be purchased by SJWC; 2) ORA's recommended disallowance of all new vehicle purchases in

[72] Exhibit SJW-1, ch. 8 at 2-3.

[73] Exhibit SJW-10, ch. 3 at 3-3 to 3-5.

connection with new employee positions; and 3) what ORA considers the lack of supporting data provided by SJWC regarding its request.

12.4.3. Discussion

As noted by ORA, five-year recorded Transportation Fuel Expenses demonstrate significant fluctuations during the past five years. Accordingly, it is reasonable to average these costs over time and increase the costs by an escalation factor to develop a base amount for Transportation Fuel Expense. The Commission agrees with ORA that not all new or existing employees must necessarily be provided vehicles, although the Commission has increased this expense to reflect the four new employees that are added to company staffing. However the Commission also agrees that any new vehicles should be more fuel efficient than existing vehicles. Application of this estimating methodology supports ORA recommended Transportation Fuel Expense amount of $563,000, increased by $4,200 for new employees[74] for a total of $567,200 which the Commission adopts for this expense.

12.5. Transportation Depreciation

12.5.1. SJWC

SJWC originally proposed $1,289,947 for its Transportation – Depreciation expense. ORA found an error in the net salvage percentage used for this plant sub-account, stating that it should be 19.2% rather than the 0.2% used in SJWC's Depreciation Study.[75]

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[74] Based on Total Transportation Fuel Expense for existing employees of $563,000 divided by total number of existing employees, times four (new employees authorized herein).

[75] Exhibit ORA-1, ch. 5 at 5-19 to 5-20.

SJWC adjusted its estimate to reflect ORA correction of the net salvage rate, which reduced SJWC's test year estimate of Transportation – Depreciation to $830,671. The remaining difference of $129,371 is owing to the difference between SJWC and ORA in test year estimates of the investment in vehicles.

12.5.2. ORA

ORA posits that SJWC's Depreciation Study contains an error in the net salvage value for the transportation account. ORA's recommended Test Year 2013 Transportation – Depreciation expense estimate is $701,300, which incorporates a correction to this error (which was accepted by SJWC in its rebuttal testimony) as well as ORA, recommended adjustments to Transportation plant investment. SJWC's estimate for the Transportation-Depreciation expense component is derived from its estimated Transportation plant investment. Correcting this error reduces SJWC's requested Test Year 2013, Transportation - Depreciation expense amount by about $460,000, from $1,289,947 to $830,671, and comparable reductions in other forecast years, which SJWC agrees to.

12.5.3. Discussion

The Commission-adopted Transportation Depreciation expense is based on ORA's corrected estimate adjusted for the increase in four additional staff, which results in $830,671.

12.6. Other Transportation Expense

12.6.1. SJWC

SJWC requested Transportation – Other expense of $805,000, which includes transportation costs related to activities such items as travel, telephone, contracted work, tools, licenses and permits, office supplies, outside printing and design, and maintenance agreements. SJWC based its estimate on recorded

2011 amounts plus escalation, while ORA states that its estimates are based on recorded five-year averages plus escalation and removal of the customer growth factor.[76]

SJWC believes that ORA[77] selectively chose the five-year average in each instance where the 2011 expense exceeds that average, while agreeing with SJWC's use of the 2011 expense where the average is higher. SJWC states that its use of the last recorded year, 2011, as a base for estimating Transportation - Other expenses for Test Year 2013 captures the rising trend for these costs while discounting the unusually high 2010 amounts. If the Commission prefers to apply ORA's recommended five-year average, SJWC believes it should do so consistently with respect to the Pumping - Other and Maintenance Transmission & Distribution – Other expenses.

12.6.2. ORA

ORA Transportation - Other expense estimate of $737,000 is based on a recorded five-year-average plus escalation. ORA notes that the annual totals for this expense fluctuate from year to year, which it believes supports the use of averaging of recorded expenses for forecasting purposes.

12.6.3. Discussion

Other Transportation expense, similar to other recorded expenses discussed in this opinion, fluctuates over time. This variance suggests that an average of past years is the most reasonable estimate of these expenses

[76] Exhibit ORA-1, ch. 5 at 5-22.

[77] Exhibit SJW-10, ch. 5 at 5-17.

in the test year. Accordingly, the Commission adopts ORA estimate of $737,000 for Other Transportation Expense.

13. Regulatory Fees

13.1. SJWC

SJWC requests Water Quality Regulatory Fees of $373,000, which is based on an escalated five-year average with additional recognition of a $50,000 cost in each of 2012 and 2013 to obtain a new National Pollutant Discharge Elimination System (NPDES) permit (which SJWC updated to $27,995 for 2013), an ongoing increase of $32,000 per year in California Department of Public Health (CDPH) water system fees beginning in 2012, and a one-time 2013 cost of $250,000 to obtain new permits and agreements from the United States Army Corps of Engineers, the San Francisco Regional Water Quality Control Board, and the Department of Fish & Game necessary for ongoing watershed maintenance activities (referred to as a Watershed Maintenance Regional General Permit).[78] SJWC proposes that an incremental cost of $19,000 for CDPH Water System Fees also be included, along with the $250,000 test year cost of obtaining a Watershed Maintenance Regional General Permit (WMRGP). SJWC posits that this would result in an allowance of $360,000 for Water Quality Regulatory Fees in Test Year 2013, which is $13,000 less than the amount reflected in the Joint Comparison Exhibit.[79]

SJWC disagrees with ORA's recommendation to exclude its proposed increase of $32,000 in CDPH fees, stating that CDPH has raised its hourly rates

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[78] Exhibit SJW-1, ch. 8 at 4 and ch. 16 at 5-7.

[79] Exhibit JCE-2 at 2, line 13.

and expects to conduct more sanitary surveys, indicating that higher fees will be charged in the future.

SJWC expects to expend the $250,000 budget for the WMRPG project in 2013, and that there will be further expense in 2014 as SJWC staff shepherds the necessary permits through each of the responsible agencies. Therefore SJWC disagrees with ORA's proposal to allocate the cost for this project over three years.[80]

13.2. ORA

ORA proposes a forecast of $150,000 for Water Quality – Regulatory Fees expense. ORA also proposes that, because there was no observable trend in the CDPH Water System Fees during the five year period 2007-2011, simply increasing the fee by $19,000 is not supported. With no observable trend, ORA determined that it was most appropriate to use the five year average for each of the forecast years.

SJWC requests an increase to its baseline estimate in 2012 and 2013 by $50,000 to fund its share of an estimated $250,000 in "[o]ne-time cost for filing and obtaining a Watershed Maintenance Regional General Permit." SJWC subsequently and revised the estimate from $50,000 to $27,995. ORA accepts this lower estimate and increases the five-year average baseline by $27,995 per year for 2012 and 2013. ORA also recommends that the recorded costs of this one-time expense be removed for forecasting purposes in the next GRC.

SJWC seeks to increase its baseline estimate by an additional $250,000 in 2013 to obtain the WMRGP. ORA does not oppose the total amount requested

[80] Exhibit SJW-10, ch. 13 at 13-4.

but makes an adjustment to the timing of the funding. ORA recommends amortizing this $250,000 one-time expense over the 2013-2015 period. Correspondingly, ORA adjusts SJWC's estim-98ate to add $83,333 to the 2012, 2013 and 2014 baseline estimates, and recommends that the recorded costs of this one-time expense be removed for forecasting purposes in the next GRC.

13.3. Discussion

As water quality is an increasingly critical safety matter which may impact future water quality regulations, the Commission adopts SJWC's estimate for water quality related regulatory fees. However, while additional expenses may be incurred in the future, the Commission agrees that the WMRGP is a one- time cost. Therefore, SJWC's regulatory permit expenses are adjusted to amortize this permit fee over three years. This adjustment results in an adopted amount of $206,333 for regulatory fee expenses.

14. Operation and Maintenance Expenses

SJWC states that the overall difference between ORA and SJWC's estimates of Operation & Maintenance (O&M) expenses for Test Year 2013 as displayed in the Joint Comparison Exhibit is approximately $9.1 million – a 7.9% difference between SJWC's updated estimate of $125.0 million and ORA estimate of $115.9 million.[81] The majority of this different is due to their respective recommendations of Conservation expense ($2.8 million for SJWC and $77,800 for ORA), which are discussed in Section 24 herein. The remaining differences are discussed in Sections 15 and 16.

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[81] Exhibit JCE-2 at 3, line 40.

15. Operations Expenses

15.1. Purchased Water

ORA and SJWC agree on the cost of Purchased Water expense of $48,713,000. The Commission adopts it as reasonable.

15.2. Other Sources of Supply

15.2.1. SJWC

SJWC requests Other Sources of Supply expense of $1,091,000. There are differences between SJWC's and ORA's methods of estimating Test Year 2013 for the "Other" categories of expenses.

15.2.2. ORA

ORA estimates that Other Sources of Supply will cost $986,000. This account is made up of four components – Labor, Transportation, Purchased Material & Supply, and Other.

ORA used the same allocation methodology as SJWC to allocate total company labor to this account, but corrected what it identifies as several errors in SJWC's estimates.

Even though ORA used the same allocation methodology as SJWC, because ORA proposed Transportation Purchased Material & Supply expenses are lower than SJWC's, these components of Other Sources of Supply are also lower than SJWC's request.

Given what it considers significant fluctuations in the Other component, ORA escalated a five year average instead of using a single base year with escalation and customer growth as SJWC did.

15.2.3. Discussion

Consistent with the Commission's expense forecasting method adopted elsewhere to reasonably adjust for fluctuating costs, the Commission's adopted expense for Other Sources of Supply is $1,008,700, based on a five-year average which has been escalated.

15.3. Purchased Power

15.3.1. SJWC

ORA offers a slightly higher estimate of Purchased Power expense ($5,865,000) than does the Company ($5,754,000). The difference of $111,000 is not due to a difference in methodology, but to ORA's estimates of customer sales, which are higher than SJWC's, resulting in a higher estimated annual water supply requirement. Because energy consumption is a function of the water supply requirement, ORA's estimates result in a higher recommended purchased power estimate.[82]

15.3.2. ORA

ORA accepts the Purchased Power rates used in SJWC's Application and 45-day Update but applies them to ORA's estimated annual water supply requirement quantities to arrive at its estimated Purchased Power expense of $5,865,000, which is $111,000 more than SJWC's request.

15.3.3. Discussion

The Commission's adopted customer estimates reflect an average of both SJWC's and ORA estimating methods. Consistent with that approach and in recognition of continuing conservation, the Commission adopts an amount of $5,809,500 which represents the midpoint between ORA's and SJWC's Purchased Power estimates.

[82] Exhibit ORA-1, ch. 5 at 5-34.

15.4. Pump Tax

15.4.1. SJWC

SJWC's Pump Tax request of $33,174,000 is based on the unit price charged by the Santa Clara Valley Water District times SJWC's requested water supply requirement. As with Purchased Power, the difference between SJWC's and ORA's estimate of Pump Tax expense is due not from a difference in methodology but from that the difference between SJWC's and ORA's estimates of customer sales.[83]

15.4.2. ORA

ORA accepts the Pump Tax rates requested in SJWC's Application and 45-day Update but applies them to ORA's estimated annual water supply requirement quantities to arrive at its estimated Pump Tax costs $34,358,000, which is $1,184,000 greater than SJWC's request.

15.4.3. Discussion

The Commission's adopted water usage as discussed above is an average of the two amounts estimated by ORA and SJWC, and consistent with that amount the Commission adopts an average of the two estimates for pump tax, or $33,766,000.

15.5. Other Pumping

15.5.1. SJWC

SJWC requests Other Pumping Expense of $3,021,000. There are differences between SJWC's and ORA's methods of estimating Test Year 2013 for the "Other" categories of expenses.

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[83] Exhibit ORA-1, ch. 5 at 5-35; Exhibit JCE-2 at 3, line 19.

15.5.2. ORA

ORA recommends Other Pumping Expense of $2,757,000. This expense consists of Labor, Transportation, and Purchased Material & Supply, which are all allocated components based on total company estimates. ORA makes similar adjustments to the components of Other Source of Supply are made to Other Pumping expense as well. ORA accepts SJWC's Update for the Other component of this expense.

15.5.3. Discussion

The Commission-adopted amount for Other Pumping reflects the previous estimates for labor, transportation, Materials and Supplies, and the Other component of this expense as discussed herein. Therefore, the adopted amount for Other Pumping expense is $2,852,300.

15.6. Chemical Expense

15.6.1. SJWC

SJWC requests $519,000 for Chemical expense. SJWC states that its chemicals cost per million gallons of groundwater production has increased every year for the past five years, with an average annual increase of 19.6% and an average increase of 22.2% over the past three years. For these reasons, SJWC estimated Chemicals expense for Test Year 2013 by adding an average annual 20% increment to its recorded 2011 expense.[84] SJWC uses these averages because of fluctuations during the average period (2006-2010).

SJWC opposes ORA's proposed three-year average estimation method, explaining that the volume of chemicals used in a given year depends on the

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[84] Exhibit SJW-1, ch. 8 at 4, and ch. 16 at 7-8.

amount of groundwater and surface water treated; the average cost of chemicals per unit of water produced; and the trend in that average cost. SJWC also noted that ORA reliance on a three-year average does not account for the fluctuations in annual Chemicals expense, or variations in the frequency of chemicals deliveries.

15.6.2. ORA

ORA proposes Chemical Expense of $383,000, which is $136,000 less than SJWC's request of $519,000. SJWC's 20% per year increase for the period 2013-2015. ORA bases its estimate on a three year average plus escalation, which it feels better captures recent production and treatment requirements. ORA opposed this 20% annual adjustment factor, claiming that the historical percentage increases were applicable only to 61% of SJWC's Chemicals expense and that a review of sample invoices for chemical purchases from 2009 to 2011 did not confirm an increasing trend of fuel costs, taxes and mill fees. ORA also noted that an increasing unit price in dollars per million gallons may be offset by lower demand for water, and that utilizing a three-year average captures recent production and treatment requirements.[85] ORA believes it is overreaching for SJWC to apply its calculated 20% annual increase to its total Chemical expense based on only a portion of its Chemical expenses.

ORA found that the invoices provided by SJWC in support of its claim of expected increases due to increased fuel cost, compliance taxes and mill fees fail to show an increasing trend of these cost elements as claimed by SJWC. Contrary to SJWC's underlying assumption in forecasting chemical expense,

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[85] Exhibit ORA-1, ch. 5 at 5-36 to 5-39.

ORA posits that a percentage change in average unit price ($/MG) does not necessarily equate to an equal percentage change in total costs.

15.6.3. Discussion

A reasonable estimate for chemical expense should reflect both the trend in costs and the actual amount of water being treated, a fact noted by ORA in its estimate. SJWC's estimate is based on a greater frequency of observations in developing a historical percentage increase. Therefore, the Commission adopts SJWC's estimate adjusted for greater water usage. This results in a Commission adopted amount of $519,000 for chemical expense.

15.7. Other Water Treatment

15.7.1. SJWC

SJWC request Other Water Treatment expense of $3,198,000. There are differences between SJWC's and ORA's methods of estimating Test Year 2013 for the "Other" categories of expenses.

15.7.2. ORA

ORA recommends Other Water Treatment Expense of $2,575,000. This account consists of Labor, Transportation, Purchased Material & Supply, Water Quality Regulatory Fee expense and Other. Because annual recorded costs for this expense category fluctuate from year to year by as much as 300%, ORA posits that an escalated five year average best reflect the future cost pattern of this expense.

15.7.3. Discussion

The Commission adopts as reasonable an average of past Other Water Treatment costs as proposed by ORA. However, this amount is adjusted upwards to reflect the Commission's adopted water quality regulatory expenses discussed above. Therefore, the Commission adopts ORA proposed average of

$2,575,000 increased by the water quality difference with SJWC of $171,200, or a total adopted expense of $2,746,200.

15.8. Transmission and Distribution

15.8.1. SJWC

SJWC's request of $4,440,000 for T&D expense consists of four components: a) Labor; b) Transportation; c) Purchased Services; and d) Other. The first three components are allocated portions of the total estimates for those cost categories.

15.8.2. ORA

ORA proposes T&D Expense of $4,068,000. The difference between ORA's proposal and SJWC's request is ORA's removal of the customer growth factor used by SJWC in its estimate.

15.8.3. Discussion

As the Commission is removing customer growth from its adopted expense estimates, the Commission adopts $4,068,000 for T&D expense.

15.9. Customer Accounts

15.9.1. SJWC

Customer Accounts expense is comprised of seven components, including Uncollectables, Labor, Transportation, materials and supplies (M&S), Other, Postage, and Conservation. As in the case of T&D expense, Labor, Transportation, and Purchased Services are allocated portions of the total estimates for those cost categories.

ORA accepts SJWC's estimated Uncollectable Factor of 0.1843%, so the difference in estimated Uncollectables expense (ORA's estimate exceeds SJWC's updated estimate by $32,000) is due to the difference in estimated total revenues.[86] SJWC's updated estimate of $485,000 for Test Year 2013 Billing Postage expense is based on recorded 2011 plus two years of customer growth. SJWC noted that it was not requesting an increase in the allowance for e-billing fees, even though the percentage of e-bills is on an increasing trend.

15.9.2. ORA

ORA proposes Customer Account Expense of $7,865,000. Differences between ORA and SJWC result primarily (accounts for over 90% of the difference) from ORA's recommended disallowance of Conservation related costs. Additionally, differences arise from: 1) Difference between ORA's and SJWC's estimates of total revenues; 2) Allocation of Labor, Transportation, and Purchased Services – M&S; 3) Use by ORA of a five-year escalated average for the Other category due to the significant fluctuation in the recorded amounts, and no customer growth factor; and 4) ORA's consideration of the recorded number of paper and electronic bills, the decreased use of paper bills, the costs of each, and expected postage increases.

15.9.3. Discussion

As the Commission is removing customer growth from its adopted expense estimates, and the Commission uses its adopted figures for the various components of Customer Accounts expense, the Commission adopts $8,173,800.

16. Maintenance Expenses

Adopted expenses for the accounts listed below reflect amounts which have been allocated from adopted Labor expense, Transportation expense, Purchased

[86] ORA-1, Ch.5; Exhibit JCE-2, at 3, line 24.

material and Supply, Regulatory Fee expense and Other expense. These accounts include:

1. Source of Supply Maintenance Expenses
2. Pumping Plant Maintenance
3. T&D Plant Maintenance
4. Maintenance T&D Purchased Services

16.1. Source of Supply-Plant Maintenance

16.1.1. SJWC

SJWC requests Source of Supply-Plant Maintenance Expense of $131,000. As in the case of T&D expense, Labor, Transportation, and Purchased Services are allocated portions of the total estimates for those cost categories.

16.1.2. ORA

ORA proposes Source of Supply-Plant Maintenance Expense of $120,000, compared to SJWC's request of $131,000. This expense consists of Labor and Purchased Services – M&S. Differences between ORA and SJWC result from differences regarding allocation of the three components of this expense.

16.2. Pumping Plant Maintenance

16.2.1. SJWC

SJWC requests Pumping Plant Maintenance Expense of $1,151,000. As in the case of T&D expense, Labor and Purchased Services are allocated portions of the total estimates for those cost categories.

16.2.2. ORA

ORA proposes Pumping Plant Maintenance Expense of $1,069,000, compared to SJWC's request of $1,151,000. This expense consists of Labor and Purchased Services – M&S. Differences between ORA and SJWC result from differences regarding allocation of the three components of this expense.

16.3. Transmission & Distribution Plant Maintenance

16.3.1. SJWC

SJWC requests Transmission & Distribution Plant expense of $176,000 is comprised of four components: a) Labor; b) Transportation; c) Purchased Services; and d) other. These components are allocated portions of the total estimates for those categories.

16.3.2. ORA

ORA proposes Water Treatment Plant Maintenance Expense of $170,000, compared to SJWC's request of $176,000. Differences between ORA and SJWC result from differences regarding allocation of the four components of this expense.

16.4. Maintenance T&D Purchased Services

16.4.1. SJWC

SJWC's request of $3,701,000 for Maintenance T&D Purchased Services expense is based on the five-year inflation-adjusted average of actual Operations and Maintenance purchased services expenses applying inflation.

SJWC believes that ARC Flash assessment, implementation, training, and labeling are essential in providing additional information technology (IT) education, training, and contracted work, and to satisfy increasingly stringent water quality standards.

16.4.2. ORA

ORA recommends $3,415,000 for Maintenance T&D Purchased Services. ORA accepts SJWC's allocation methodology, but because ORA's total Purchased M&S expense estimate is lower than SJWC's request, ORA's T&D expense is also lower.

16.4.3. Discussion (Maintenance-Source of

Supply, Pumping, Water Treatment Plant, T&D Labor, and Purchased Services

The amounts adopted by the Commission for these various maintenance expenses are determined by an allocation of adopted Labor and Purchased Services expenses.

With regards to ARC Flash, ORA does not indicate that it opposes the need for ARC Flash training and assessment. However, ORA explains that in response to an inquiry, SJWC no longer requests a separate amount for ARC Flash training and assessment but rather expects to meet these requirements through an electrical engineer hired by SJWC in 2011. As discussed above with regard to employee labor costs, this decision provides for the hiring of three new employees. Therefore, should SJWC determine that the ARC Flash training and assessment is necessary, this decision provides for the retention of the electrical engineer to accomplish that assessment and training.

17. Purchased Services O&M

For Purchased Services, ORA accepts SJWC's 45-day Update estimate except for the customer growth factor as explained earlier. SJWC's Update estimate of $76,924 is based on five-year escalated recorded average. ORA's estimate is $76,702. The Commission adopts ORA's estimate of $76,702.

17.1. Purchased Services – Water Quality

17.1.1. SJWC

After adjustments to recorded data, SJWC estimates that $659,000 for purchased services related to water quality activities. SJWC argues these expenses are necessary for monitoring costs and to meet increasingly stringent water quality standards. As an example SJWC states that there will be a continuing expense of $100,000 to meet NPDES requirements. SJWC believes that ORA's estimating method of eliminating certain costs before determining an average amount results in an estimate lower than a five-year historical average.

17.1.2. ORA

ORA contends that SJWC's recorded costs in prior years include amounts for specific costs which are unique to a specific year and therefore should be adjusted out before making estimates. ORA explains that this estimating method results in double-counting of the costs in the test year as SJWC includes the amount as part of the historical expense and then includes it again as an add on cost. As a result of ORA's recommended adjustments and estimating methods, ORA recommends an amount of $443,000 for this cost in 2013. ORA adds that, if the Commission adopts NPDES costs of $100,000 for Test Year 2013, the expense should be adjusted by approximately $38,000 to remove the cost from historical amounts for estimating purposes.

17.1.3. Discussion

The Commission recognizes that future water quality costs are likely to increase over time as water quality standards become more stringent. However in this instance the argument between SJWC and ORA reflects primarily estimating methods rather than water quality standards. As it appears both ORA and SJWC estimate using historical averages which exclude one-time expenses, the Commission adopts ORA's estimate, but increases it by an amount of $62,000 ($100,000-38,000) to recognize SJWC's compliance requirements for NPDES costs. This results in an estimate of $505,000 for this expense.

18. Administrative and General Expenses

18.1. Office Supplies

18.1.1. SJWC

The category of A&G Office Supplies includes a number of transportation-related expenses. SJWC requests A&G Office Supplies of $1,794,000. The remaining contested A&G Office Supplies items are related to the M&S category.

SJWC states that it inadvertently included the incorrect amount in its work papers for its Utility Supplier Diversity Program (USDP) of $90,600.[87] SJWC states that it provided a detailed justification for the increased USDP budget, explaining that it was necessary to help SJWC meet the Commission's newly mandated General Order (GO) 156 requirements through expanded outreach to Women, Minority and Disabled Veterans Business Enterprises (WMDVBE).

For expenses associated with accounts for Landscaping Travel and Incidental, Bank Service Charges; and Other Office Supplies, SJWC based its estimates on the 2011 recorded amounts plus escalation and customer growth factors.[88] SJWC posits that, because these expenses will continue to follow this upward trend, use of 2011 recorded cost provides the most accurate period upon which to base an escalation to the 2013 forecast.

18.1.2. ORA

ORA recommends Office Supplies Expense of $1,647,000. Office Supplies Expense consists of Transportation and M&S. Differences in this account result from: 1) Different allocations of the Transportation component by ORA and

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[87] Exhibit SJW-2a, ch. 9 at WP 9-4; and Exhibit SJW-1, ch. 9 at 3.
[88] Exhibit SJW-2A, ch. 9 at WP 4.

SJWC; and 2) Different estimates by ORA and SJWC, of the various components of M&S, including A&G Postage, Telephone and Internet Access, Stationary and Printing, Landscaping and Janitorial Services, Miscellaneous General Expenses, Travel and Incidental, Bank Service Charges, and Other Office Supplies and Expenses. The differences in Item 2 result from either ORA's use of different escalated base totals or ORA not applying a customer growth factor in addition to escalation, as done by SJWC.

ORA does not oppose SJWC's request for USDP, but objects to SJWC's corrected request of $136,500 for Test Year 2013.[89]

Instead of the 2011 recorded amount, ORA recommends using a three-year average base period (2009-2011) escalated to Test Year 2013 in order to smooth out year to year fluctuations instead of using one year of data.

18.1.3. Discussion

The Commission adopts Office Supplies expense based on allocated expenses from other categories and the elimination of the customer growth factor. The Commission therefore adopts Test Year 2013 Office Supply Expense of $1,783,000.

18.2. Property Insurance

18.2.1. SJWC

SJWC based its $194,000 test year forecast for Property Insurance on an estimate provided by its insurance broker.[90]

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[89] Data provided to ORA by SJWC in its Response to ORA Data Request PPM-13, April 3, 2012. Reference: Exhibit ORA-1, ch. 5 at 5-49; and Exhibit SJW-10, ch. 5 at 5-20 to 5-21.

[90] Exhibit SJW-1, ch. 9 at 3.

SJWC states that its insurance brokers projected rate increases of 4.3% between 2011 and 2012 and 8.0% between 2012 and 2013 to reflect current market conditions to calculate Property Insurance expense.

18.2.2. ORA

ORA estimates Property Insurance Expense of $137,000. Instead of utilizing what SJWC identifies as information provided by its insurance broker, ORA recommends that a five-year average percentage increase of 2.0% be used to forecast estimates for the test year, citing the fluctuation from year to year associated with this expense.[91]

18.2.3. Discussion

The Commission adopts SJWC's estimate for Property Insurance as it reflects an estimate provided by an expert opinion for anticipated insurance costs. SJWC is therefore authorized Property Insurance expense of $194,000 for 2013.

18.3. Injuries and Damages Insurance

Injuries and Damages Insurance expenses consists of two components: 1) Workers' Compensation Insurance; and 2) Public Liability Insurance (PLI).

18.3.1. SJWC

SJWC estimated its test year and escalation years forecast for its Worker's Compensation Insurance (WCI) expense by increasing its baseline estimate by an average of the percentage increases in premiums over the three-year period from 2009-2011, or 25% each year. SJWC believes that the 2009-2011 period captures certain of the volatility in annual premium history experienced as a result of the

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[91] Exhibit ORA-1, ch. 5 at 5-50.

2004 institution, and subsequent roll-back, of cost reduction reforms, but excludes years where booked expenses were artificially low due to the application of credits from retrospective years (dating back to 2003-2006) that the Company will not receive on a going-forward basis.[92] ORA notes an incorrectly calculated WCI: Labor expense ratio and recommends a ratio of 1.44%. SJWC acknowledges the correction to the WCI: Labor expense ratio and uses the accurate ratio of 1.44% to arrive at the "SJWC Current" value provided in the Joint Comparison Exhibit. SJWC stands by the original escalation rate of 25% as submitted in its Application, supporting the adjusted estimate of $637,000 for Test Year 2012.[93]

SJWC based its Test Year 2013 forecast of $1,298,000 for Public Liability Insurance (PLI) on estimates provided by its insurance broker.[94] As with its Property Insurance forecast, SJWC sought the expertise of its insurance broker to inform the development of its PLI expense forecast, resulting in an escalation factor of 8% in 2012 and 5.4% in 2013. Using the historical five-year average expense and these escalation factors, SJWC projects a 2013 expense of $1,298,000.[95]

18.3.2. ORA

ORA estimates WCI expense of $512,000. Even though ORA agrees that an adjustment to reflect an increasing trend in this expense is reasonable, it estimated an annual factor of 9% instead of SJWC's 25%, which is based on the

[92] Exhibit SJW-1, ch. 5 at 11.

[93] Exhibit JCE-2, at 4, line 45.

[94] Exhibit SJW-1, ch. 9 at 3.

[95] Exhibit SJW-10, ch. 5 at 5-22 and Attachment D.

2012-2015 average annual increase in WCI rates provided by SJWC's insurance broker.[96]

ORA estimates PLI expense of $973,000. This expense consists of Public Liability Insurance, Directors' and Officers' Liability, and Provisions for Injuries and Damages. ORA accepts SJWC's estimates for Directors and Officers' Liability and Provisions for Injuries and Damages, but differs with SJWC regarding the Public Liability Insurance component. ORA posits that, because recorded amounts for this component have been going down because 2009, and SJWC provided no support for their base year 2011 figure of $850,000, PLI expense should be based on 2011 recorded costs plus a 2% escalation factor – citing a steady decline in recorded annual amounts for this expense.[97]

18.3.3. Discussion

ORA's estimate of WCI reasonably relies on a combination of SJWC's broker's estimate, and more recent escalation rates. Therefore, the Commission adopts ORA estimate of $512,000 for WCI. While the Commission bases its Property Insurance expense on SJWC's broker's estimate, in this instance the recorded amounts for PLI between 2009 and 2011 continually decline. It is unreasonable to expect this expense, even if based on SJWC's broker's estimate to exceed by almost 68% the amount recorded in 2011. Therefore, the Commission adopts ORA estimate of $973,000 for PLI.

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[96] Exhibit ORA-1, ch. 5 at 5-52.

[97] Exhibit ORA-1, ch. 5 at 5-52 to 5-53.

18.4. Regulatory Commission

18.4.1. SJWC

SJWC estimated its Regulatory Commission expense of $1,000,000 based on the assumption that, over a three-year period, it will incur legal, consulting and other fees associated with a fully litigated GRC, one cost of capital proceeding, at least one formal application coming out of the GRC, and miscellaneous legal and consultant work not related to a formal proceeding such as an Order Instituting Rulemaking (OIR).[98] SJWC also states that regulatory costs from the 2006-2008 period to the 2009-2011 period have escalated as a result of the increasing amount and complexity of regulatory activity.[99]

ORA did not contest the validity of these trends, but argued that the addition of one regulatory staff position in 2010 should help SJWC "reduce or at least contain" these costs.[100] SJWC counters that one extra staff person for a large investor owned utility such as SJWC is not sufficient to address the increasing amount and complexity of regulatory activity faced by SJWC.

18.4.2. ORA

ORA proposes Regulatory Commission expense of $235,000, compared to SJWC's request of $341,000 for the test year. ORA states that SJWC did not develop a detailed quantitative analysis to arrive at the three-year estimate of $1,000,000, and did not supply any quantitative analysis in support of its request.

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[98] Exhibit SJW-1, ch. 9 at 2; Exhibit SJW-2a at WP-9-8; and Exhibit SJW-10, ch. 5 at 5-24 to 5-25.

[99] Exhibit ORA-1, ch. 5 at 5-54.

[100] Exhibit ORA-1, ch. 5 at 5-55.

ORA also rejects SJWC's reasoning that changes due to the Rate Case Plan can be used to explain the increase in regulatory costs from the 2009-2011 cycle to the 2012-2014 cycle, because the change occurred from the 2006-2008 cycle to the 2009-2011 cycle.

ORA did not contest the total cost incurred by SJWC in its 2009-2011 cycle, but disagrees that the total recorded cost of $689,000 from the last cycle provided a reasonable estimate for the 2012-2014 cycle.[101] ORA used the same amortization and escalation approach as SJWC, and spread the estimated total over 2012, 2013 and 2014.

18.4.3. Discussion

While ORA's estimate more accurately reflects recorded Regulatory Commission Expenses, SJWC is correct that increased regulatory activity may be reasonably foreseen. In this proceeding, SJWC and ORA were not able to achieve a settlement agreement and thus demonstrated the potential for increased regulatory activity and consequently expenses. However, SJWC's estimate of $1,000,000 over a three year period is not well founded either. Therefore, the Commission adopts an average of SJWC's and ORA's regulatory expense estimates or $288,000 for Test Year 2013. Over a three-year period this adopted amount provides for $864,000 in regulatory expenses.

18.5. Outside Services

18.5.1. SJWC

SJWC estimated the Outside Services – Legal expense by using the base year 2011 annualized estimate of $700,000 and including the customer growth

[101] Exhibit ORA-1, ch. 5 at 5-55 to 5-56.

escalation factor and specific expenses associated with the Records and Information Management (RIM) project to derive a Test Year 2013 expense of $895,000. SJWC illustrates that recorded 2011 outside legal expense is an outlier, due SJWC having received reimbursements for approximately $360,000 in legal fees related to a lawsuit concluded in 2011, which offset the Outside Services Legal expense. SJWC posits that because this resulted in an irregularly low expense for 2011, 2011 should not be used to estimate future outside legal expenses.

The only difference between the parties with respect to SJWC's Outside Services – Other expense is the issue ORA raised regarding SJWC's inclusion of a customer growth factor.[102]

18.5.2. ORA

ORA proposed Outside Services-Legal of $467,000 compared to SJWC's request of $635,000. ORA states that it used SJWC's baseline estimate and escalation factor. In its calculation, ORA also excluded a customer growth factor used by SJWC, as well as Records and Information Management Initiative (RIM) expenses. ORA excludes these RIM costs because it has requested that RIM capital investment be disallowed. ORA also believes additional RIM costs can be absorbed into the current project budget.

ORA recommends Outside Services-Other expense of $1,967,000, compared to SJWC's request of $1,989,000. The only difference between the two parties is ORA's rejection of a customer growth factor.

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[102] Exhibit SJW-2A, ch. 9 at WP 9-8; and Exhibit ORA-1, ch. 5 at 5-56 to 5-58.

18.5.3. Discussion

Because SJWC already provides good customer service, the Commission denies SJWC's request for the additional expenditure to support the RIM program. The Commission also excludes customer growth, as it has done throughout this decision. The Commission therefore adopts $1,978,700 for Outside Services expense.

18.6. A&G General Corporate

ORA proposes A&G General Corporate expense of $829,900 compared to SJWC's request of $835,000. The difference results from SJWC's addition of a customer growth factor that is not used by ORA.

As the Commission has excluded customer growth from its adopted expenses, the Commission adopts ORA estimate of $829,900.

18.7. A&G Dues and Membership

18.7.1. SJWC

SJWC based its $472,200 estimate of Dues and Memberships expense by escalating 2011 recorded data.[103] The Dues and Memberships expense category consists of both Company Dues and Employee Dues.

SJWC states that dues for the California Water Association (CWA) and the National Association of Water Companies (NAWC) have increased over time, and because these rates track recorded utility revenue, are likely continue to increase. SJWC believes it receives considerable benefits from participation in Chambers of Commerce, and request recovery of fees for these organizations.

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[103] Exhibit SJW-1, ch. 9 at Table 9-B.

SJWC requested that the Commission adopt an Employee Dues estimate of $28,000.[104] These particular dues include membership in various community-based organizations, including the Quota Club, Rotary Club, San Jose Lions Club, and the San Jose Athletic Club. SJWC posits that athletic club membership is a component of executive compensation necessary to attract high-quality management, which in turn benefits ratepayers through better overall utility operations.[105]

18.7.2. ORA

ORA proposes A&G Dues and Membership expense of $354,000. This difference results from ORA: 1) removal of an escalation factor used by SJWC due to what ORA identifies as no consistent increase in dues paid; 2) use of updated percentages that account for the deduction of lobbying expenses from dues for the CWA, NAWC, and the Water Reuse Association; 3) removal of all Chamber of Commerce dues pursuant to D.04-07-022;[106] and 4) removal of dues for memberships that ORA posits provide no ratepayer benefit, including dues to the Quota Club, the Rotary Club, the San Jose Lion's Club, and the San Jose Athletic Club. ORA recommended disallowance of Employee Dues for membership in various community-based organizations, including the Quota Club, Rotary Club, San Jose Lions Club, and the San Jose Athletic Club, claiming that it is "unclear" what ratepayer benefits result from these employee memberships.[107]

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[104] Exhibit SJW-1, ch. 9 at Table 9-B.

[105] Exhibit SJW-10, ch. 5 at 5-28.

[106] Exhibit SJW-1, ch. 9 at Table 9-B.

[107] Exhibit ORA-1, ch. 5 at 5-59 to 5-60.

18.7.3. Discussion

Although SJWC argues that membership in certain organizations such as the San Jose Athletic Club benefit ratepayers by attracting and keeping high-quality management, that benefit is uncertain and not proven. Asking that ratepayers support similar memberships in various clubs and other organizations has been a matter of contention in many past proceedings for water and other utilities. In this proceeding, the Commission adopts an amount of $375,400 which excludes membership costs for the Quota Club, the Rotary Club, the San Jose Lion's Club and the San Jose Athletic Club, but provides an escalation factor for the included A&G Dues and Memberships. In excluding these amounts from ratepayer funding, the Commission does not imply that such organizations do not serve useful and beneficial social functions but that these are not functions which provide direct benefits to ratepayers. Should SJWC determine that such dues and memberships are valuable, it is within its discretion to pay for these with non-ratepayer dollars.

The Commission therefore adopts Test Year 2013 A&G Dues and Membership Expense of $375,400.

18.8. Rent

18.8.1. SJWC

SJWC based its Rents expense of $482,000 on an escalated five-year average.[108]

SJWC agrees that ORA's methodology would provide an accurate forecast, but disagrees with the calculation ORA performed in order to arrive at its

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108 Exhibit SJW-1, ch. 9 at 1, and Tables 9-A and 9-B.

forecasted rent expense for 2013.[109] Applying what it believes is the appropriate weighted escalation factors for 2012 and 2013 to the 2011 recorded values for each of the components included in the Rents expense category, SJWC produces a forecasted 2013 Rents expense of $482,000.

18.8.2. ORA

ORA estimates Rent expense of $311,000 compared to SJWC's estimate of $482,000. ORA based its forecast on SJWC's recorded 2011 rental costs, because it believes this reflects more recent rental deeds and costs. ORA recommended the forecast be based on the 2011 recorded year, adjusted to reflect the current rent amount for the 2010 South Bascom Avenue facility, to reach an estimated $311,000 for the Test Year 2013.[110]

18.8.3. Discussion

Although rental costs have fluctuated in the past, the most recent rental agreements best reflects expected costs in TY 2013. Therefore, the Commission adopts ORA's Rent expense estimate of $311,000

18.9. A&G – Transferred Expenses

18.9.1. SJWC

SJWC estimates ($6,939,000) for Administrative Transferred Expenses based on the recorded five-year average. These expenses consist of costs related to work performed for SJWC affiliates, administrative costs related to capitalized construction projects, and some incremental costs related to provision of non-tariffed products and services. Some of these Transferred Expenses are

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109 Exhibit SJW-10, ch. 5 at 5-28 to 5-29.

110 Exhibit ORA-1, ch. 5 at 5-61.

treated as a reduction to total operating expenses, are not included in revenue requirement, and are not passed along to ratepayers.

SJWC posits that the base period used for escalation purposes should be based on the expense category under consideration. In this case, SJWC believes the five-year average forecasting methodology provides a smoothing effect to the fluctuations.

18.9.2. ORA

ORA estimates A&G - Transferred expense of ($7,617,000). ORA bases its estimate on recorded year 2011 data plus escalation instead of a five-year average (as done by SJWC) in order to account for what it identifies as an increasing trend.

18.9.3. Discussion

The majority of the Transferred Expenses reflect those administrative and general expenses which due to capitalization are removed from operational expenses. While both SJWC and ORA argue over an absolute amount, it is not whether an absolute amount is capitalized but rather what is the proper capitalization ratio between A&G that is expensed and capitalized. An average of SJWC's recorded capitalized percentages for the years 2007-2011 is 20.1% (based on Commission annual report data). The Commission has applied this percentage to total A&G expenses to determine A&G expenses and A&G capitalized.

19. Taxes Other Than Income

19.1. Ad Valorem

The difference between SJWC's request of $6,058,000 and ORA recommendation of $6,021,000 is entirely attributable to differences between the parties' estimates of Utility Plant in Service.[111] Accordingly, the calculation of test year Ad Valorem Tax expense depends on the adopted value for Utility Plant in Service.

19.1.1. Discussion

The adopted amount of $5,978,000 for Ad Valorem taxes reflects the amount of plant adopted herein.

19.2. Payroll

19.2.1. SJWC

Payroll taxes result from the Federal Insurance Contributions Act (FICA), the Federal Unemployment Tax Act (FUTA), and the California State Unemployment Insurance Program (SUI). SJWC estimates payroll taxes based on the historical ratio of payroll taxes to total expensed direct payroll.[112]

SJWC explains that, due to possible fluctuations in future rates and payroll caps, SJWC forecasts FICA taxes based on the recorded ratio of these taxes to expensed payroll. SJWC's application included an incorrect ratio of 0.0779, which was based on incomplete information, and was subsequently corrected. SJWC applied the corrected ratio of.0926 to the total expensed direct payroll, which results in a Payroll Tax forecast of $2,520,000.[113] SJWC states that because payroll tax expense is a function of payroll expense, and then the final authorized payroll tax will be dependent on the authorized payroll expense.

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111 Exhibit ORA-1, ch. 6 at 6-1.

112 Exhibit SJW-10, ch. 5 at 31-32.

113 Exhibit SJW-10, ch. 5 at 31-32.

19.2.2. ORA

ORA recommends Payroll Tax of $1,916,000 compared to SJWC's request of $2,520,000. Differences between ORA and SJWC are attributable to the differences in payroll estimates.

19.2.3. Discussion

In a manner similar to Ad Valorem Taxes, Commission-adopted payroll taxes reflect the adopted payroll amount. Applying this methodology to payroll taxes results in a Commission-adopted amount of $ $2,402,400 for payroll taxes.

19.3. Local Franchise Fees

19.3.1. SJWC

SJWC pays a percentage of its gross revenues as local franchise fees to the County of Santa Clara and to some of the cities within which it serves. ORA accepts SJWC's method for calculating Franchise Fees expense and uses the same local franchise tax rate provided in SJWC's updated work papers.

The difference between SJWC's request of $618,000 and ORA's recommendation of $559,000 is a result of the difference between the parties' estimates of Total Revenues excluding deferred revenues.[114] Accordingly, the calculation of test year Franchise Fees expense depends on the adopted values for Total Revenues and deferred revenues.

19.3.2. ORA

ORA proposes Local Franchise Fees of $559,000 compared to SJWC's request of $618,000. Differences between SJWC's and ORA's estimated amounts are due to differences in estimated revenues.

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[114] Exhibit ORA-1, ch. 6 at 6-1.

19.3.3. Discussion

The Commission adopts Franchise Fees based on the adopted revenues, resulting in $588,500.

20. Income Taxes

20.1. SJWC

SJWC requests Total Income Taxes of $18,946,000, which consists of California Corporate Franchise Tax (CIT) of $4,078,000 and Federal Income Tax (FIT) of $14,862,000. The differences between SJWC's and ORA's estimates of FIT and CCFT are due in part to differences in the calculation of the Domestic Production Activities Deduction (DPAD) and the net operating loss carry-forward resulting from the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (Tax Relief Act), and in calculating depreciation for CCFT purposes as well as the interest expense deduction. Remaining differences are due to differences in revenues, expenses, and rate base estimates between SJWC and ORA.[115]

SJWC calculated the ratemaking interest deduction using its Weighted Average Rate Base multiplied by the authorized Weighted Cost of Debt. ORA employed the same formula, except that it applied the Weighted Cost of Debt from the pending settlement in SJWC's cost of capital proceeding, A.11-05-001. The $836,000 difference between the parties for this line item reflects the different Weighted Cost of Debt factors as well as differences in the parties' estimates of Weighted Average Rate Base.[116]

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[115] Exhibit ORA-1, ch, 7 at 7-1 to 7-3.

[116] Exhibit JCE-2, at 5, line 79.

The $1,226,000 difference between the parties with respect to CCFT depreciation for tax purposes results from differences between SJWC's and ORA's recommended plant additions.

As a result of the bonus depreciation provisions, SJWC expects to report a Net Operating Loss (NOL) for tax purposes in 2011 and 2012, and understands that a NOL reported for tax purposes can be carried forward to reduce deferred taxes (and therefore increase rate base) for ratemaking purposes. Anticipating that it will not report any taxable income after applying the NOL in years 2013 and 2014, SJWC will not be able to utilize the DPAD in those years, and so it includes zero DPAD in calculating test year FIT for ratemaking purposes.[117]

20.2. ORA

ORA recommends Total Income Taxes of $15,477,000 which consist of CIT of $3,601,000 and FIT of $11,870,000.

The differences between ORA and SJWC are due primarily to the parties' treatment of the DPAD, the net operating loss carry-forward resulting from the Tax Relief Act, and differences in the forecasts of revenues, expenses, rate base, and interest cost.

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[117] Bonus depreciation provisions of the Tax Relief Act create a timing difference that results in the reporting of tax losses in years when financial reports show net income. The timing difference is recorded as a deferred tax liability, while a deferred tax asset is generated related to a tax NOL caused by bonus depreciation. The tax loss will be used in future years to reduce income for federal tax purposes. The deferred tax liability, net of the deferred tax asset, is an offset to rate base, which is captured in the memorandum account established pursuant to Commission Resolution L-411A. Exhibit SJW-10, ch. 12 (Rajalingam), at 12-1 to 2. For ratemaking purposes and financial reporting purposes, the deferred tax liability and the deferred tax asset arising from the bonus depreciation are calculated in accordance with the concept of basic "Normalization" that is employed in accounting for income taxes by utilities and is deducted from rate base.

ORA recommends CCFT Depreciation of ($33,932,000). ORA recommends FIT Depreciation of ($32,947,000) compared to SJWC's request of ($35,157,000). These depreciation figures are different due to the difference in the Parties' requested plant additions.

ORA recommends Ratemaking Interest Expense Deduction for taxes of ($17,168,000). Differences in this deduction result from ORA's use of the Weighted Cost of Debt from the pending settlement in A.11-05-001 instead of the currently authorized figure used by SJWC, and the difference in the parties' forecast plant additions.

ORA recommends DPAD for taxes of ($3,207,000) compared to SJWC's request of zero. ORA posits that SJWC's application of prior year's NOL to test year tax calculations is retroactive ratemaking, and should not be allowed. Because rates are set prospectively, ORA calculates the DPAD for 2013 and 2014 by multiplying the 9 percent[118] of SJWC's Qualified Production Activities Income, reflecting that amount as a deduction in 2013 and 2014. ORA also removed the NOL carry-forward used by SJWC to calculate test year taxes.

ORA and SJWC agree on a 50% Meals Deductions for taxes of ($89,000), and Tax on CIAC and Advances of $6,000.

20.3. Discussion

The Commission's adopted income taxes are based on the adopted revenues, expenses, and plant amounts herein. With regard to income tax calculations for ratemaking purposes, the adopted income taxes should reflect the estimated expenses and tax deductions, rather than actual income taxes that

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118 *See* Internal Revenue Code Section 199.

may be calculated for other purposes. Although it is a complex matter, DPAD is an example of such a difference, and results from a timing difference which applies to those years in which SJWC shows net income for financial purposes rather than regulatory purposes. However, the availability of DPAD is restricted when there is a NOL carryover which in turn reduces taxable income. Thus it becomes a question of whether DPAD can be applied to ratemaking taxes when there exists in the recording of actual taxes a net operating loss carryover. It is not reasonable to reflect the actual tax effects on ratemaking income taxes as the basis for the tax calculations is a mixture of actual income and ratemaking income for tax purposes.

As explained by SJWC, the resulting application of DPAD would create a deferred tax asset and deferred tax liability, which are deducted from rate base. Therefore, the Commission has calculated income taxes in the manner recommended by SJWC which applies DPAD not directly to the tax calculation but by removing the tax asset and tax liability from rate base. The Commission therefore adopts FIT of $13,153,000 and CIT of $3,528,000 for 2013.

21. Utility Plant in Service

21.1. SJWC

SJWC requests a Utility Plant in Service budget of $93,883,000 for 2013. As indicated in Table 11-B of Exhibit SJWC-1A, the most substantial planned investments are in the areas of Source of Supply, Reservoirs and Tanks, Pump Stations and Equipment, Recycled Water Pipeline Extensions, New and Replacement Mains, Services, Meters, and Green/Alternative Energy.[119]

SJWC states that it has weighed the options of: 1) doing nothing; 2) repairing existing plant; or 3) replacing existing plant. SJWC posits that, given the age of its plant and the need to comply with current regulations and industry standards, replacing is the appropriate option to take.

21.2. ORA

ORA recommends Utility Plant in Service projects of $72,804,000 for test year 2013. ORA and SJWC agree on $59,640,000 of SJWC's request, with ORA recommending another $13,164,000 for the balance and SJWC requesting $34,243,000. ORA supports many but not all of SJWC's requested construction projects, including main replacement projects, reservoir and tank projects, and pump stations improvement. ORA recommends the Commission give greater weight to projects that provide water supply and reliability and disallow further investment by SJWC in the areas of recycled water infrastructure, solar panel installation, and hydro-turbine generation projects.

21.3. Discussion

In determining a reasonable amount to adopt for SJWC's 2013 capital budget, the Commission considered plant additions proposed for 2012 and those proposed for 2013. In addition, the Commission reviewed SJWC's 2014 proposed construction budget. As discussed above, ORA agrees with SJWC on the majority of plant additions. However in some instances ORA either estimates lesser costs or recommends that certain plant additions not be included in

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119 Exhibit SJW-2A at WP 11-8 through 11-10.

adopted rate base amounts. Although it may seem that 2012 additions should already be included in recorded plant, the information provided in the record is based on known plant in 2011, and therefore the Commission's adopted plant for 2013 is developed from that basis.

The Commission's adoption of a plant estimate using estimated capital budget amounts does not imply that SJWC must necessarily proceed with those projects which it presented for inclusion in rate base. The Commission adopts a reasonable amount of plant based on the best estimates of plant necessary to provide safe and reliable service to its customers. While the Commission addresses disputed plant projects as discussed below, this discussion does not determine whether a particular plant project should be constructed but rather whether it represents a reasonable amount for plant, and therefore rate base. The Commission expects that SJWC will apply the adopted capital budget in a prudent manner to assure safe operation of the system.

As the Commission is adopting all of the plant projects which are not in dispute between SJWC and ORA, Commission resolution of plant projects which are in dispute between SJWC and ORA are discussed below.

1. The Commission adopts miscellaneous rights-of-way costs of $10,300 as necessary for current and future water system access.
2. The Commission adopts ORA's estimate of 2012 costs for standby power generators in recognition that these costs are more representative of actual costs.
3. Pipeline replacement project estimates are discussed below.
4. Pipeline renewal projects for lines 2-inches or less are discussed below.
5. The Commission adopts ORA's estimate of the costs for changing out obsolete Sensus meters. The Commission

believes that the more recent data reflects actual costs. However, the Commission recognizes that over time inflation will affect cost and therefore has applied SJWC's requested 3% inflation rate to the ORA estimates. This inflation rate has been applied to estimates for 2012, 2013 and 2014.

6. The Commission will not adopt SJWC's proposal for automatic meter reading at this time. While automatic meter reading is widely used by many energy utilities, it is not yet widely used by water utilities. Should SJWC determine that such a pilot program may have net benefits for reducing costs for customers, it should request including the cost of a pilot program as part of its next GRC. Such request should be accompanied by a fully documented cost-benefit study.
7. The Commission will not adopt SJWC's proposal for a workforce management system as it is uncertain that such a system is reasonable or necessary at this time.
8. The Commission will adopt ORA recommendation for the costs of new trucks and cars. The Commission's adopted amount for these vehicles recognizes that older vehicles must be periodically replaced. However, the need for additional vehicles is significantly tempered by the Commission adoption of only four of SJWC's requested 27 new positions. The Commission will however allow for the purchase of 4 vehicles for the four new employees. This amount adds $60,000 to ORA recommended vehicle budget.
9. The Commission adopts ORA's estimated amount of $816,300 for mobile standby generator trailers. This amount is a reasonable estimate of the total cost of such trailers for use during emergencies and natural disasters.
10. The Commission will not adopt SJWC's request for work including booster pumps at the Mireval or Overlook Stations. A review of the information provided indicates that while the capacity of the existing systems are near a maximum, increased conservation is likely to reduce the

need for additional capacity at this time. While this work is not included in plant for 2013 or 2014, SJWC may determine that the replacement of MCC and booster pumps are needed as part of future plant additions and therefore may request them in its next General Rate Case.

11. While ORA agrees with many information management technology projects, ORA disagreed that SJWC should incur approximately $1.4 million on a Rate Impact Measure (RIM). However, as ORA points out, the RIM project is expected to incur not only significant cost initially but also on-going expenses. ORA also argues that there are demonstrated alternatives to the RIM project. Although the Commission supports technological advancements and refinements, in this instance the Commission agrees with ORA that other alternatives should be considered before SJWC embarks on RIM.

12. SJWC proposes to install a stand-by generator at SJWC's office building at an estimated cost of $491,200. ORA does not object to this plant installation but indicates that a more reasonable cost should be $325,300. The Commission adopts ORA's estimate as reasonable.

13. ORA and SJWC agree on the plant amounts for reservoir and tank projects for both 2012 and 2013, of $13,302,600 and $14,280,800 respectively. However, ORA recommends that $2.467 million for roof support work and a new membrane filter at the Almaden Valley Station be postponed beyond 2014 pending a 2013 consultant study. As this work does not appear to be imminently necessary, the Commission will not adopt this amount in 2014 plant estimates.

14. ORA also recommends that $825,000 for redwood tank construction at the Koch Lane Station also not be included in the 2014 plant. While SJWC agrees with ORA that the station has not delivered water into the system since 2007, SJWC believes the station is needed for water quality sampling and alternative supply purposes. The Commission agrees that there are other alternative water

supply options for SJWC and therefore finds that construction of this facility is not necessary at this time. Consistent with this determination, the Commission does not adopt SJWC's proposal to replace the MCC at the Koch lane Station.

15. In anticipation that there may be additional years with little precipitation, and the potential need for well production, the Commission recognizes that the booster pumps at the Franciscan, Miguelito Road, and Buena Vista Stations may be necessary. Therefore, the Commission will provide that if these 2014 proposed projects, including the replacement and relocation of the MCC at the Franciscan and Miguelito Road Stations are necessary, then SJWC may file Tier 2 Advice Letters for recovery of these costs.[120] However, the maximum amounts are capped at $1,234,800 at the Franciscan Station, $1,360,400 at the Miguelito Road Station and $885,100 at the Buena Vista Station. Although these SJWC estimated costs are capped at the adopted amounts, the Commission expects that any amount requested up to the indicated caps will be reviewed for reasonableness.

16. Although ORA agrees with SJWC that a standby power generator should be installed at the Varner Ct. Station, ORA notes that this should be a 10 kilowatt (KW) generator and not a 30 KW generator which SJWC estimates to cost $202,700. ORA estimates a lower cost of $69,300, which the Commission adopts for this project.

17. For attrition year 2014, SJWC requests $1,704,700 for a standby generator at the Williams Road Station, and $1,404,200 for a standby generator at the Tully Road Station, ORA argues these projects are unnecessary at this time as there are other alternative water supply means in

[120] Tier 2 Advice Letter shall be filed pursuant to General Order 96-B requirements. http://docs.cpuc.ca.gov/PUBLISHED/GENERAL_ORDER/164747.htm#P1123_115309
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the event of a natural disaster. ORA also objects to the estimated costs of these facilities. SJWC disagrees explaining the need for groundwater production requiring generator power in an emergency in the affected water supply zones. Although SJWC may determine that there are alternative means for providing water supply in the event of an emergency, in recognition of the potential safety implications the Commission adopts the costs for installing these two generators in 2014, as requested by SJWC.

18. The Commission adopts SJWC's request of Total Station Survey equipment costs of $65,900 as necessary for current and future water system operation.

The most significant plant addition cost difference between ORA and SJWC is the proposed Pipeline Replacement Program. SJWC argues that in D.09-11-032[121] the Commission adopted SJWC's proposal to replace 1% of SJWC's pipelines. This rate equates to a 100-year average life expectancy for SJWC's pipelines, or 24 miles per year. SJWC argues that its proposal continues the rate adopted in D.09-11-032, and recognizes the aging of the pipeline system, particularly cast iron and thin-walled pipelines. SJWC notes that this rate is intended to reduce leaks and the potential for catastrophic failures.

Alternatively, ORA proposes that a more appropriate rate should be 0.83%, equating to a 120-year replacement rate, or 20 miles of pipeline per year. ORA notes that the adopted rate of 1% in D.09-11-032 effectively doubled the rate from the then previous pipeline replacement rate of 0.5%. ORA contends that while its' proposed 0.83% rate will result in a longer period for pipeline replacement, the cost difference between the 100-year and 120-year replacement

[121] *See* D.09-11-032 at 31.

rates is significant and that the pipelines proposed for replacement average only 60 years old.

While the Commission supports infrastructure improvements particularly to avoid catastrophic failure which may have safety implications and negatively affect customers, the Commission must also consider the costs to ratepayers of improvements against the background of measured leakage and leak repair costs for water pipelines. In order to balance these concerns, the Commission adopts a replacement rate of 0.90% per year. In the next GRC if SJWC determines that this rate is insufficient, we agree with ORA that SJWC should provide information regarding leakage rates and leak repair costs to justify an increased pipeline repair replacement rate.

The Commission also applies the 0.90% rate to the replacing of services (pipelines under 2-inch diameter) consistent with SJWC's and ORA's recommendation.

SJWC and ORA do not agree on the installation of SJWC's proposed photovoltaic (PV) energy system at the Williams Road Station, or a micro-hydro turbine generator system at the Alum Rock Turnout. ORA contends that a cost-benefit analysis shows that the payback period of 24 years for the PV system does not justify its installation, while SJWC contends the payback period is 13 years. ORA also references a previous solar pilot project (Columbine) which SJWC constructed and was intended to gather information on expected and actual performance. The information on performance for this project is only partially known and the outcome remains uncertain. While the Commission is supportive of PV installations where needed and cost-effective and where such installations further the alternative energy goals, in this instance there is insufficient information to conclude that the Williams Road PV system would sufficiently benefit SJWC's ratepayers. For these reasons, the Commission will consider in the next GRC whether the Williams Road solar project or other solar projects should be included in test year plant.

Including the micro-hydro turbine generator in SJWC's plant additions is also speculative at this time. As the Commission recently adopted, (R.) 13-12-011 to consider the energy saving possibilities from the energy-water nexus, it is premature to begin such projects before information is developed in R. 13-12-011.

As a result of the adjustments discussed above, the Commission adopts total Utility Plant in Service of $1,124,588,000.

22. Depreciation Expense and Reserve

22.1. SJWC

SJWC has determined annual depreciation accruals by preparing annual depreciation studies and computations to reflect current weighting among ages, classes and types of depreciable properties, and their future life expectancies. Depreciation accruals for 2012-2014 are based upon the depreciation study performed for 2011 adjusted for the budgeted additions, estimated retirements, sales and adjustments for each year. Based on these depreciation studies SJWC's recommended composite depreciation rate for the Test Year 2013 is 3.51%.[122]

Due to the timing of the Application in January 2012 versus the depreciation study which was prepared in September 2011, SJWC did not include full year-end numbers.[123] Subsequently, SJWC provided an updated

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[122] Exhibit SJW-1, ch. 12 at 1-2.

[123] Exhibit SJW-2, Ch. 12, at WP 12-7.

study with year-end 2011 final balances, resulting in a 3.50% depreciation rate; and one which SJWC posits is the most accurate rate.

22.2. ORA

ORA recommends Depreciation Expense of $33,059,000 compared to SJWC's request of $33,266,000. The majority of the differences between ORA's and SJWC's estimates of depreciation expense and depreciation reserve are due to differences in their estimates of depreciable plant. ORA used a depreciation rate of 3.46% based upon SJWC work papers and corrected errors in SJWC's depreciation study, and use of revised salvage values. ORA also decreased the retirement component of the depreciation reserve's forecast to align with what it believes is the historical relationship between retired plant removed from ratebase and added to depreciation reserve. In future GRCs, ORA recommends that SJWC submit depreciation studies in a digital spreadsheet format and that links between utility plant and depreciation work papers replace the use of hardcoded entries wherever possible, in order to facilitate the review of depreciation data.

22.3. Discussion

The Commission adopts an amount for Depreciation Expense based on the adopted plant as discussed above, and applies ORA's recommended rate of 3.46% as reasonable. In addition, the Commission directs SJWC to submit depreciation studies in a manner which links utility plant and depreciation, such that the review of depreciation data may be facilitated. The Commission adopts Depreciation Expense of $32,892,000 for 2013.

23. Cash Working Capital and Rate Base

23.1. SJWC

For ratemaking purposes, the Commission allows the inclusion of amounts invested in working capital as an addition to rate base. Working capital consists of materials and supplies and working cash. The largest component of working cash is the average deficiency as a result of paying expenses, taxes and accrued depreciation in advance of collecting revenues. This component is calculated utilizing a lead-lag study. SJWC calculates working cash based on the procedures outlined in CPUC Standard Practice U-16-W – Determination of Cash Working Allowance (SPU-16).[124]

Although not stated in Exhibit SJW-10, SJWC stipulates to the adjustments made by ORA regarding minimum bank cash deposit and customer deposits. SJWC further stipulates to ORA's recommended adjustments (1), (3), (4), (5), and (6) to the lead-lag study.[125] These adjustments are incorporated in the SJWC "SJWC Current" columns in Exhibit JCE-1, Table 2 and Exhibit JCE-2, Table 2.

ORA argues that "the lag days related to interest expense must be considered in a lead-lag study, like any other cash expense."[126] SJWC posits that if this were true, and any "cash expense" should be included in the lead-lag study, then construction cash and dividends, which SPU-16 also specifically

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[124] Exhibit SJW-1, ch. 13 at 2.

[125] SJWC Opening Brief at 123: (1) decreasing revenue lag days from 56 to 51; (2) including debt interest expense with the calculation of lag days; (3) removing depreciation expense from the calculation of lag days; (4) adjusting purchased water expense lag days from 4.6 to 40.3; (5) adjusting pump tax expense lag days from 11 to 46.8; (6) adjust rent lead days from 76.1 to 15; and (7) adjust expense lag days for the Other O&M category from 9.8 days to 45 days. Id. at 10-4 to 10-6.

[126] Exhibit ORA-1, ch.10 at 10-4 to 10-5.

states should not be included in the "cash requirement", would be included in the lead-lag study as well. The Commission specifically noted that these expenses, including interest, should not be included in the working capital calculation, and thus they should not be included in the lead-lag study.[127]

SJWC also believes that ORA's recommendation regarding the exclusion of depreciation expense from the lead lag study is also not in conformance with SPU-16, which lists depreciation as one of the expenses used to develop lead-lag days.

SJWC notes that the final working capital estimate will be based on what the Commission adopts for operating revenue and for expense items. However, the final calculation of working cash should not include interest expense and should include depreciation expense.

23.2. ORA

Ratebase consists of plant in service, cash working capital, materials and supplies, with deductions for accumulated depreciation reserves, contributions in aid of construction, customer advances for construction, and accumulated deferred income taxes. ORA recommends a rate base figure of $509,420. Differences between ORA and SJWC consist primarily of differences in the parties' estimates of plant in service, depreciation, taxes, and cash working capital.

Cash working capital is the additional amount of capital that is required to permanently fund ongoing operations and bridge the gap between the time expenditures are made and the time collections are received. Cash working

[127] Exhibit SJW-10, ch. 5 at 32-33.

capital consists of operational cash, investor funds required to cover timing differences between cash expenditures and revenue collections (includes results of a lead-lag study).

ORA proposes two adjustments to the operational cash component proposed by SJWC of ($373,000): 1) Removal of the Minimum Bank Cash Deposit of $200,000, because SJWC indicated that this amount came from a past rate case and SJWC incurs no fees for not maintaining a minimum bank balance; and 2) increase of the estimate for Customer Deposits to $1,135,679, which ORA bases on a five-year average to account for fluctuations, instead of the one year figure used by SJWC. These adjustments result in an ORA-recommended operational cash component of ($619,979).

The second component of cash working capital is the working capital estimate of investor funds that might be required to cover any timing differences between cash expenditures and revenue collections. A lead lag study is used to calculate this figure. ORA proposes several adjustments to SJWC's proposal: 1) ORA adjusted the average revenue lag days estimated by SJWC from 56 to 51 days, taking into consideration customer billing on both a bi-monthly and monthly basis, compared to SJWC's estimate based on all customers being billed bi-monthly, which would result in a decrease of approximately $2,000,000 in cash working capital; 2) ORA includes within its calculation of lag days the actual cash payment of debt interest expense that SJWC excluded from the lead-lag study. Pursuant to SPU-16, ORA believe that debt interest expense cannot be included in the operational cash component of cash working capital, but should be included in the lead-lag study. This results in a reduction to rate base of approximately $1,700,000; 3) ORA removes the category of depreciation expense (a non-cash expense) from the lead-lag study, because non-cash items should not be included in the estimation of cash based items, such as cash working capital; and 4) ORA proposed correction of miscellaneous calculations related to the number of lag days for payment of Purchased Water and Pump Tax, Rents, and Other O&M, which result in a net change in lag days of an additional 45.9 days.

23.3. Discussion

Both SJWC and ORA look to SPU-16 as a guide in making working cash calculations. However, SJWC and ORA disagree in the application of the elements described in SPU-16 to the working cash determination. A review of SPU-16[128] shows that book depreciation is included as an expense for the lead-lag study, however with an amount of zero lag days. Conversely, SPU-16 specifically excludes interest expense as a component in the lead lag study.[129] Although interest expense represents a cash payment by SJWC, it has been excluded because it has been considered a component of the cost of capital, and therefore has been treated independently of operational cash requirements. The Commission's adopted working cash amount reflects these determinations.

As a result of the adjustments discussed above, the Commission adopts Cash Working Capital of $9,702,000 and Rate Base of $516,464,000 for 2013.

24. Conservation Program Expense

24.1. SJWC

SJWC's ongoing conservation program consists of a residential and commercial water audit program, distribution of low-flow showerheads and

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[128] SPU-16 at 1-15.

[129] SPU-16 at 1-5.

faucet aerators, public information and education, and participation in various programs offered by SCVWD. The latter activities offered by SCVWD, including rebate programs, sub-metering, retrofitting 187 new recycled water customers landscape surveys, and public outreach, are cost-effective and sensible to offer at a regional level and are indirectly funded through the wholesale rates SJWC pays to SCVWD. The total forecasted cost of SJWC's on-going conservation program in 2013 (not including programs indirectly funded through wholesale rates) is $120,153.[130]

A further set of water conservation programs is proposed in conjunction with implementation of SJWC's proposed Water Revenue Adjustment Mechanism (WRAM). The proposed programs include: a landscape budget/survey program; a high efficiency toilet direct install program; participation in the existing SCVWD landscape rebate program; cooperation with Resource Action Programs in the provision of "Water Wise" school education kits; a commercial, institutional, and industrial (CII) survey program; and a pilot program to study the effectiveness of a new technology – the Aquacue barnacle to help customers better understand their water use and become more efficient. The total cost for these new programs is projected to be $4,151,100 over the three-year rate case period, not including the proposed Aquacue pilot program with a Test Year 2013 cost of $1,324,800.[131]

ORA opposes SJWC's proposals to introduce new water conservation programs, noting that customers already have significantly reduced water

[130] Exhibit SJW-2A, ch. 8 at WP 8-25.

[131] Exhibit SJW-2A, ch. 8 at WP 8-25.

consumption and this reduction is the primary driver of SJWC's request to increase rates in this GRC. SJWC stressed that its intentions regarding water conservation are based on implementation of the Commission's own policies favoring water conservation, SJWC states that water usage was low in 2010 and 2011 due to the economic downturn, cooler weather, and conservation efforts, but noted that water use may rebound and SJWC cannot predict the timing or extent of such a rebound. For this reason, SJWC urges a robust conservation programs must be in place in order to reach the mandated policy goals for 2020 and to comply with public policy goals.

24.2. ORA

ORA recommends Conservation Program expense of $77,800. ORA states that the increase in SJWC's Conservation Program expenses is due to SJWC's proposed increase in its conservation efforts related to the WRAM/MCBA implementation and continuation of the recycled water retrofit program. With customers' already reduced per capita water consumption, and SJWC's use of this reduced water use as one of a number of reasons for its requested increase in rates, ORA posits that SJWC should not be granted an increase in conservation spending to pursue new and expanded conservation programs. ORA recommends, instead, that extending SJWC's historical trend of conservation spending, adjusted for inflation, should be used to estimate test year forecasts.

In particular, ORA recommends that: 1) SJWC's proposed High Efficiency Toilet Direct Install Toilet Program, estimated at $400,000 per year be denied as the Santa Clara Valley Water District (SCVWD) already has such a program, and SJWC has not presented the cost benefit of replacing existing toilets with high efficiency ones to its customers so they can make their own decision; 2) SJWC's request of $340,000 in 2013, in order to add an additional $0.75 per square foot to the customer rebate for turf removal, be denied, as the water saved would cost $12,539/acre foot – much greater than the cost of SJWC's most expensive water; 3) SJWC's request of $300,000 for a new landscape survey program be denied, as SJWC's program is similar to an SCVWD program and would be duplicative; 4) SJWC's request of $150,000 for its Commercial, Institutional, and Industrial (CII) Survey Program be denied, as this is similar to a program that was discontinued by SCVWD in 2012, and SJWC has not determined why the SCVWD program was discontinued; and 5) SJWC's request of $100,000 per year for classroom activities and hands-on home projects for young students be denied, as SJWC customers already obtain a number of the devices that would be offered by the program.

24.3. Discussion

Although the Commission is highly supportive of conservation programs, particularly in light of the current declared California drought, the Commission also reviews and analyzes existing and proposed programs in light of their cost, effectiveness, and benefits, and consideration of whether such programs are supported through other agencies. In this instance the Commission will not adopt those conservation programs which appear to duplicate other programs. Therefore the following programs are not included in SJWC's adopted conservation expenses: Toilet Replacement ($400,000) and the Landscape survey ($300,000). Both of these programs are being pursued through SCVWD. In addition, adopted conservation expenses do not include the CII Survey Program ($150,000) as it is similar to a previous SCVWD program which was discontinued for unspecified reasons, and the turf removal program ($340,000) which costs significantly more than the cost of saved water. While the Commission is not adopting expenses for these programs, it has provided significant amounts for the remaining conservation programs. As a result of the adjustments discussed above, the Commission adopts Conservation Program expense of $217,000 for 2013.

25. Non-Tariffed Products and Services

25.1. SJWC

SJWC participates in several business activities employing utility assets which would otherwise go underutilized. This activity produces revenue of $555,866. All risk related to these NTP&S are borne by the shareholders, while the associated revenue generates benefits to both ratepayers and shareholders. The provision of all NTP&S is performed in accordance with the Commission's Rules for Water and Sewer Utilities Regarding Affiliate Transaction and the Use of Regulated Assets for Non-Tariffed Utility Services (ATRs) established in D.11-10-034.[132]

Although not stated in rebuttal, SJWC concurs with ORA's position regarding the classification of the City of San Jose Miscellaneous contract services. However, SJWC posits that ORA's deduction of $285,967 from SJWC's labor expense associated with labor utilized for NTP&S provision is not in compliance with the ATRs authorized in D.11-10-034, specifically ATR X.B, which allows a utility to offer products and services that (amongst other qualifications) meet various "excess of unused capacity" and qualifications. SJWC believes that the NTP&S related labor falls under these "excess or unused capacity" qualifications.[133]

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[132] Exhibit SJW-1, ch. 8 at 5.

[133] Exhibit SJW-10, ch. 5 at 35-36.

SJWC posits that the $285,967 of labor expense reduction sought by ORA is clearly related to non-incremental NTP&S labor, and thus is allowed for recovery under the Commission's ATRs.

25.2. ORA

ORA estimates gross revenue derived from NTP&S activities that are allocated to ratepayers to be $576,943 for the Test Year 2013, plus an additional $100,000 per provisions of Rules X.C.5 and X.C.6 of D.10-10-019.

ORA also recommends that $285,967 of Payroll Expense be deducted, for ratemaking purposes, which represents 2011 labor expense pertaining to SJWC's NTP&S activities that it believes should be borne by shareholders not ratepayers. The adjusted 2011 Total Payroll Expense should then be used as the starting basis to forecast Test Year 2013 Total Payroll Expense.[134]

The $13,140 difference in NTP&S gross revenue between ORA and SJWC results from ORA's application of a composite inflation factor on a five year average of recorded gross revenue for NTP&S, compared to SJWC's use of specific inflation factors for a specific NTP&S contract or no inflation factor if none was included in a contract.

ORA recommends $285,967 of labor should be removed because, if it remains, SJWC would be reimbursed twice for this SJWC personnel labor cost – once through the 2013 forecasted estimate for Total Company labor, and again through payment for contracted services from its NTP&S customers. ORA therefore recommends that the forecast NTP&S payroll be based on the reduced 2011 payroll figure and a 3% inflation factor for both components.

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[134] Exhibit ORA-1, ch. 12 at 5-7.

In subsequent responses to data requests, SJWC identified the positions and departments of SJWC personnel utilized for the City of San Jose O&M and the City of Cupertino water system lease for 2011. This information allowed ORA to match the requested additional personnel in the current GRC to the positions and functions of employees currently rendering services for NTP&S activities. ORA does not find any reasonable justification for increasing the number of new personnel in departments where existing personnel in these same departments have been providing labor for NTP&S activities under SJWC's claims of excess capacity.

25.3. Discussion

D.10-10-019, as modified by D.11-10-034 and D12-01-042, established specific rules by which water utilities allocate and account for costs for NTP&S. SJWC and ORA agree on the reduction in NTP&S gross revenue ($100,000) to fulfill the allocation rule before allocating revenues between the utility and ratepayers. However, a difference exists in the development of labor costs where such labor costs include costs relating to the provision of NTP&S. ORA recommends that the 2011 labor cost which serves as a basis for forecasting test year labor cost should be adjusted downward to exclude costs incurred for NTP&S, and that the Commission did not intend to exclude such costs by referencing incremental costs as unreasonable for utility rates. ORA argues that such costs are reimbursed through invoices to NTP&S parties, and also from ratepayers.

SJWC contends that under NTP&S rules the costs it seeks to recover do not meet the definition of incremental costs that would be incurred by the utility through the provision of NTP&S. That is, SJWC argues that the Commission specifically referenced incremental costs as being excluded from rates and it should therefore be inferred that non-incremental costs can be recovered from rates.

The issue before the Commission is whether exclusion of a category of expenses in rates means that expenses which can be argued as not in that category may necessarily be included in rates. In this instance the argument is not reasonable. Instead the Commission must consider whether the expenses are just and reasonable, not by their definition, but by whether they are incurred to provide NTP&S and therefore should be excluded from rates as directed by D.10-10-019. As ORA points out, the expenses SJWC seeks were incurred to provide NTP&S and therefore should not be considered in determining test year labor costs. Consistent with D.10-10-019 the Commission finds that these expenses are not reasonable because the expenses provide NTP&S.

26. Memorandum Accounts

26.1. Health Care Memorandum Account

26.1.1. SJWC

SJWC states that it has experienced dramatic year-to-year fluctuations in medical and dental premiums, which it believes will likely be amplified by the passage of the Patient Protection and Affordable Care Act (ACA), and the possible taxable nature of such benefits. SJWC posits that enactment of the ACA will increase employer and employee payroll tax liabilities. SJWC states that it has limited flexibility to increase employee contribution in the short term based on the current union contracts, but could seek increased contributions in future negotiations. Due to what it considers the unpredictability of premium increases resulting from compliance with the ACA, it requests approval of a Health Care Memorandum Account (HCMA).[135]

26.1.2. ORA

SJWC's proposed HCMA would track any cost increases in health and dental premiums that might arise due to any reason. ORA posits that the fluctuations in medical and dental premiums referred to by SJWC in support of its request and SJWC's use of the last recorded cost as a basis for escalation, can be addressed through increased employee contributions.

26.1.3. Discussion

The Commission does not adopt a health care memorandum account at this time. Despite the uncertainty of costs generated by the ACA, this decision adopts adequate expenses for health and medical insurance costs. As SJWC states, it may determine in the future that changes in employee contributions are reasonable and include this matter in negotiations for a future union contract.

26.2. International Financial Accounting Standards

26.2.1. SJWC

As a publicly traded investor owned utility SJW Corporation (SJWC Corp.), SJWC's parent company will have to comply with the proposed change from reporting its financial results under Generally Accepted Accounting Principles (GAAP). As a result, SJW Corp. will be required to report its financial results in compliance International Financial Reporting Standards (IFRS) once the Securities and Exchange Commission (SEC) elects to move forward with the initiative. SJWC states that the implementation of IFRS is beyond the control of

[135] Exhibit SJW-10, ch. 8 at 22.

SJWC and related costs may be significant. Due to the uncertainty related to the adoption and implementation timeline, and the magnitude of potential costs related to IFRS conversion and adoption, SJWC seeks authority to establish a memorandum account to prospectively record IFRS compliance related costs.

SJWC posits that the adoption of IFRS will impact all areas of financial accounting, reporting, and disclosure, requiring major modifications, staff training, restatement of historical financial information, and reporting to third parties such as the Commission, the IRS and note holders. SJWC therefore believes that the cost and effort involved in converting from GAAP to IFRS will be significant and cannot be accurately predicted, requiring the use of a memorandum account.

26.2.2. ORA

ORA believes that although the actual timing and costs of moving to IFRS remain uncertain, as demonstrated by the SEC multiple delays in deciding if and when to adopt the IFRS, the protection offered by a memorandum account to record any potential compliance costs is not necessary. ORA goes on to state that given the continual process by which utilities must comply with new and regularly updated accounting standards, this ongoing process of compliance is not new and fluctuations in compliance costs are captured in existing forecasting methodologies.

26.2.3. Discussion

The Commission authorizes SJWC to establish an IFRS memorandum account to prospectively record IFRS compliance related costs. In allowing SJWC to establish this account, the Commission finds that expenses incurred for IFRS compliance meets the criteria necessary to establish a memo account. These criteria are:

1. The expense is caused by an event of an exceptional nature that is not under the utility's control. SJWC does not have control over regulations implemented by the SEC.
2. The expense cannot have been reasonably foreseen in the utility's last general rate case and will occur before the utility's next scheduled rate case. Although this proceeding is a general rate case, the expenses are expected to occur between this GRC and SJWC's next GRC.
3. The expense is of a substantial nature as to the amount of money involved when any offsetting cost decreases are taken into account. As explained by SJWC the financial and accounting areas impacted are significant and costs are therefore expected to be substantial.
4. The ratepayers will benefit by the memorandum account treatment. Rather than attempting to estimate the costs of SJWC's compliance with IFRS and including those costs which may overestimate actual costs, a memorandum account will only allow costs necessary for IFRS compliance to be included in rates.

Although the Commission authorizes SJWC to establish an IFRS memo account, the Commission also directs SJWC to report in its next GRC whether continuation of the memo account is necessary, and the amounts which have been recorded in that account.

26.3. Chromium VI

26.3.1. SJWC

SJWC states that Chromium VI naturally occurs in the San Jose area drinking water aquifer, and that State and Federal agencies are in the process of setting Maximum Contaminant Level (MCL) for Chromium VI. SJWC believes that the potential cost impact of a very low MCL for chromium VI – even one significantly higher than the recently adopted Public Health Goal – is tremendous. SJWC requests authority to establish a Chromium VI

Memorandum Account for potential compliance costs related to the treatment of chromium VI upon the establishment of state and/or federal regulations for treatment levels. The trigger event for establishing this memorandum account will be the establishment of a MCL by the state and/or federal regulatory agencies. This memorandum account would track operating expenses and capital expenditures related to meeting the established MCL.[136]

SJWC believes its request for the creation of a memorandum account for Chromium VI complies with the Commission's criteria for creation of a memorandum account - the regulation of chromium VI is exceptional in nature, creation of the new regulation is not under SJWC's control, creation of the new regulation could not be reasonably foreseen in this GRC, the new regulation may occur before the next GRC, and is potentially substantial in its financial impact. SJWC posits that ratepayers will benefit by SJWC treating this potential expense with a memorandum account because they will be charged accurately for the expense of compliance with an MCL for chromium VI.[137]

26.3.2. ORA

For reasons similar to its opposition to creating an IFRS memorandum account, ORA recommends against the creation of a new memorandum account to track operating expenses and capital expenditures related to meeting a new Chromium VI standard. ORA posits that the ability to track expenses and capital expenditures in a new memorandum account should not be arbitrarily set to commence upon the adoption of any new MCL without consideration of SJWC's

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[136] Exhibit SJW-1, ch. 16 at 5.

[137] Exhibit SJW-10, ch. 13 at 5-6.

actual ability to meet the standard once established. ORA states that the costs of complying with new drinking water regulations over the years are reflected in the recorded expenses of SJWC, and considered in the estimation of forecasts of those compliance costs. Because this forecast captures the continuing cycle of cost increases to meet new requirements and cost decreases from efficiency gains, ORA believes that any costs incurred to comply with a new Chromium VI requirement would be captured in the normal course of estimating this cost for the test year. ORA posits that utilizing such forecasted costs fosters discipline and efficiency as SJWC strives to control costs, instead of recording all compliance costs in a memorandum account.

26.3.3. Discussion

Whether Chromium VI costs are included in other expenses or whether such costs should be considered in the course of estimating expenses in GRCs is only one issue. It is premature to argue over the method for considering the costs for complying with Chromium VI standards as the compliance costs are unknown. A final MCL for Chromium 6 was set at 10 parts per billion effective July 1, 2014. This is 500 times higher than the recently adopted Public Health Goal 0.2 parts per billion. This decision provides that, when these consequences are more certain following adoption of final Chromium VI MCL, SJWC may file an Advice Letter requesting the establishment of a Chromium VI memorandum account.

26.4. Resolution L-411

26.4.1. SJWC

On December 17, 2010, President Obama signed the Tax Relief Act, which, among other provisions, provides for 100% bonus depreciation on certain business property put into service after September 8, 2010 and before

January 1, 2012, and a 50% bonus depreciation for property placed into service thereafter and before January 1, 2013. On June 23, 2011, the Commission passed Resolution (Res.) L-411A, which established a one-way memorandum account for all cost-of-service rate regulated utilities that do not address the Tax Relief Act in a 2011 or 2012 test year GRC to track the impacts of the Tax Relief Act. SJWC filed Advice Letter 432A on August 18, 2011, to open a 2010 Tax Act Memorandum Account in compliance with this resolution, which was approved by the Commission in August of 2011.[138]

ORA has stipulated to the removal of this balance from the total memorandum account balance, as indicated in Exhibit JCE-01, Table 4, line 9.

SJWC recommends that the memo account be reviewed in the next GRC in 2015, unless any balance exceeds 2% of authorized revenue requirement.[139]

26.4.2. ORA

In its direct testimony, ORA had recommended that SJWC refund the balance in its Res. L-411 Memorandum Account. During hearings, ORA agreed to the removal of $452,200 from SJWC's Res. L-411 Memorandum Account.

26.4.3. Discussion

The Commission authorizes the removal of the balance ($452,200) from the Res. L-411 memorandum account balance. As requested by SJWC, this memorandum account will be reviewed in the next GRC unless any balance

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138 Exhibit SJW-1, ch. 10 at 3.

139 Exhibit SJW-10, ch. 5 at 41.

exceeds 2% of the authorized revenue requirement, in which case the utility may propose rate adjustments consistent with D.06-04-037.[140]

26.5. Recovery of Current Balance in Balancing Accounts

SJWC requested the recovery of an under-collection of $2,598,912 accrued in balancing accounts via a 12-month surcharge of $0.0492 per CCF and the refund of $650,456 of an over-collection accrued in various memorandum accounts via a 12-month surcredit of $0.2498 per service connection per month.[141]

ORA agreed with SJWC's requested balancing account amortization. Given ORA's subsequent removal of the over-collection associated with the Res. L-411A Memorandum Account, ORA agrees with the memorandum account over-collection stated in SJWC's Application.

26.5.1. Discussion

The Commission accepts the recommendation of SJWC and ORA regarding the recovery of current balances in balancing accounts and this decision authorizes the recovery of the $2,598,912 under-collection in balancing accounts and the refund of $650,456 over-collection accrued in various memorandum accounts.

27. Other Requests

27.1. Bascom Avenue Facility in Rate Base

Upon reviewing SJWC's Rebuttal Testimony, ORA agreed that $382,000 is an "appropriate rent expense for test year 2013."[142]

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140 *See* D.06-04-037 at Ordering Paragraph 3.

141 Exhibit SJW-1, ch. 17 at 3.

142 Tr. 320:2-320:5 (Ma/ORA).

27.1.1. Discussion

The Commission includes this revised rent expense of $382,000 in its adopted expenses for this GRC.

27.2. Request to Update Tariff Schedule No. 1B

27.2.1. SJWC

SJWC requests that its Tariff Schedule No. 1b – General Metered Service With Automatic Fire Sprinkler System (Tariff Schedule No. 1B), be updated. No rate changes are requested as a result of the requested revision to Tariff Schedule No. 1B. SJWC proposes to expand this tariff to include meters of 1 1/2 inches and 3 inches, because it has received requests to provide such.

27.2.2. ORA

ORA is agreeable to this change, but would like SJWC to provide data in its next GRC on the number of customer in each meter service class and the revenues collected under this tariff. Because SJWC did not include this information in its current requested forecasted revenue, ORA posits that SJWC's forecasted revenue was understated, thus contributing to a larger than necessary proposed rate increase. Because of SJWC's special request to update this tariff in the current GRC, ORA discovered this unaccounted revenue, requested the number of customers incurring upsize charges under this tariff, and forecasted what it believes is a reasonable amount of associated revenue to be included in forecasted sales.

27.2.3. Discussion

The Commission adopts SJWC's requested tariff change. The Commission also directs SJWC to provide the requested customer information by meter service class and revenue collected under Tariff Schedule No. 1B in its next GRC.

28. Rate Design

The rate design issues addressed in this section differ from those addressed in Section 4 of this decision in that Section 4 only addressed rate design issues for one group of customers, the Mutuals, while in this section we address rate design for all customer classes, other than the Mutuals.

28.1. SJWC

SJWC proposes a new residential rate design based on a three-tiered system intended to encourage water conservation, while proposing to retain the current single quantity rate (SQR) for non-residential customers.[143]

SJWC's three-tier residential rate design proposal is conditioned upon concurrent Commission approval of its proposal for a full Water Revenue Adjustment Mechanism (WRAM)/Modified Cost Balancing Account (MCBA). Absent approval of the WRAM/MCBA, SJWC proposes to retain its present two-tier residential rate design.

SJWC's proposed three-tier rate design would set the Tier 1 rate below the SQR, the Tier 2 rate at the SQR, and the Tier 3 rate above that level, in order to send a price signal to encourage water conservation at higher levels of consumption. SJWC posits that this rate design promotes objectives of the Commission's Water Action Plan, and it will help SJWC meet the state's goal of reducing water consumption by 20% by 2020.[144]

ORA purports to see a regressive character in SJWC's rate design proposal, by which the highest-consumption residential users would incur the smallest

[143] Exhibit SJW-1, ch. 21 at 1.

[144] Exhibit SJW-1, ch. 21 at 2-3.

percentage increase. SJWC posits that if one looks at the effects of SJWC's proposed rate design without considering proposed changes in revenue requirement, the percentage bill increases resulting from SJWC's proposed rate design would be relatively constant from low to high consumption, with the highest increase of $0.31 (1.02%) at the level of 12 CCF.

28.2. ORA

Rate Design is the process of setting prices for utility service at levels that permit a utility to collect its total authorized revenue requirement. After calculation of SJWC's revenue requirement, a rate design that incorporates estimates of the number of customers and their future consumption levels is used to determine the actual rates that SJWC customers will be charged for utility service.

Even though ORA and SJWC both recommend a three-tier rate structure, they disagree with regards to the usage breakpoints of each tier. ORA recommends a rate design which it states will avoid any increase in rates for those SJWC customers with the lowest monthly consumption. In support of its recommendation, ORA states that it: 1) sends a positive message to those customers who have achieved and maintain conservation-oriented usage patterns; 2) demonstrates the Commission's commitment to affordability of utility service to meet basic human needs; 3) avoids regressive increase schedules where the highest-consumption residential users incur the smallest percentage increase; and 4) results in a first-tier commodity rate that offsets any rate increase and also provides a quantity of water for basic human needs at a discounted rate - meeting the dual objectives of equity and affordability.

Compared to SJWC's proposed rate structure, ORA posits that its recommended broader second tier allows for greater flexibility to reward the lowest-consumption customers with a lower first-tier rate without imposing an excessive increase on the users in the third tier. While both SJWC's and ORA's proposed rate structures maintain revenue neutrality, ORA states that its recommended structure also avoids instituting a regressive design that has the lowest-consumption per customer incurring the largest percentage increase.

28.3. Discussion

We agree with ORA's concerns regarding rate design, as rate design is the mechanism by which low consumption levels are encouraged and by which SJWC collects its authorized revenue requirement. As ORA points out, under SJWC's proposed rate design the lowest users of water will incur the greatest increases.[145] It is unreasonable to require customers using only 3 CCF of water or less per month to be subject to the greatest rate increase among residential tiers. The Commission notes that this lowest rate tier of 3 CCF equates to about 75 gallons of water daily. Customers who are able to consume water at such an extremely low usage rate should not see any increase which exceeds increases faced by customers in higher tiers. Further, we agree with ORA's proposed rate design as the second tier will provide an incentive for conservation while maintaining flexibility. Therefore, the Commission adopts ORA's recommended rate design for the recovery of the adopted revenue requirement herein.

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[145] Exhibit ORA-1, ch. 14 at 14-2.

29. Revenue Decoupling and WRAM/MCBA

29.1. SJWC

SJWC proposes to implement a revenue decoupling mechanism similar to the WRAM and MCBA that the Commission has approved for several other Class A water utilities.[146]

SJWC currently employs a "Monterey-style" WRAM, which tracks the difference between SJWC's authorized revenue (based on two-tier volumetric residential rates) and the revenue it would have received through a uniform SQR. SJWC posits that this type of WRAM does not decouple sales from revenues, therefore is a disincentive to water conservation programs. SJWC believes that its proposed WRAM/MCBA would provide it with a strong incentive to implement and pursue more aggressive and cost-effective conservation programs.[147]

SJWC states that its proposed WRAM would track the difference between adopted and actual revenue, excluding Private Fire Protection, and other revenue derived other than from metered service (but including revenue from metered recycled water service).[148] SJWC believes that ORA's opposition to decoupling of revenues ignores relevant State and Commission policy considerations and fails to consider the "fundamental truth that without decoupling, SJWC loses (or gains) revenues in conjunction with reduced (or increased) sales."

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[146] Exhibit SJW-1, ch. 19 at 2.
[147] Tr. 383:16-384:12 (Tully/ORA).
[148] Exhibit SJW-1, ch. 19 at 8-10.

SJWC posits that reduced sales will lead to increased rates with or without a WRAM/MCBA, because more than 50% of fixed costs are recovered through the quantity charges.[149] Regarding ORA's concern about the lack of symmetry, SJWC posits that the under-collections experienced by several water utilities using the requested type of WRAM/MCBA are not due to a lack of symmetry in the WRAM/MCBA, but rather a consequence of actual revenues being less than adopted forecasts. SJWC believes that the test for symmetry is how the WRAM works for sales above and below adopted levels and how the MCBA works for actual purchases and prices.

In reference to D.12-04-048, SJWC states that a key reason for the large under-collections has had nothing to do with the WRAM/MCBA but rather with the adopted sales forecasts.

29.2. ORA

ORA believes that SJWC's request for revenue decoupling with a WRAM/MCBA mechanism is unnecessary. ORA posits that SJWC is currently authorized a Monterey-Style WRAM (M-WRAM) and Incremental Cost Balancing Account (ICBA) have not prevented SJWC from realizing significant reductions in customer consumption, which is meeting or exceeding the State of California's goals. In its rebuttal testimony, SJWC refers to the Commission's authorization of pilot WRAM/MCBA mechanisms for other Class A water utilities. ORA points out that each of the WRAM/MCBA mechanisms adopted for other Class A water utilities were achieved through negotiated settlements as pilot programs; and that the Commission should not

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[149] Exhibit SJW-10, ch. 10 at 10-7.

authorize such a mechanism for SJWC just because other Class A water utilities have them; and because a negotiated settlement carries no precedential value. ORA recommends that prior to creating another WRAM/MCBA pilot program for SJWC, the Commission should assess the results of the various pilot programs currently authorized for other Class A water utilities.

29.3. Discussion

The Commission does not adopt SJWC's proposed change in its current Monterey-Style WRAM at this time. SJWC is correct that its current revenue decoupling mechanism (Monterey-Style WRAM) does not fully protect the utility against reduced sales, although it is also true that SJWC benefits through increased revenues from its Monterey Style WRAM when sales are increasing. While the Commission seeks to reduce risks both to water utilities and their customers from changes in sales through appropriate revenue and sales mechanisms which may help in conservation efforts, ORA is correct that similar mechanisms used by other water utilities were achieved through negotiated settlements which reflected many other considerations before these were adopted. Furthermore, the results of these programs, including the advantages and disadvantages to water utilities and their customers, has not been fully analyzed, so that the Commission can determine which sales risk mechanism best serves the interests of utilities and their customers.

As the current dry years persist, and the need for conservation of water resources continues, the Commission will consider in SJWC's next GRC, if not before, whether SJWC's current Monterey-Style WRAM is a useful water conservation mechanism that balances the risks of lost or increasing sales between the utility and its customers.

30. Categorization and Need for Hearing

SJWC requested that this matter be categorized as ratesetting. By Resolution ALJ 176-3287, dated January 12, 2012, the Commission preliminarily determined that this was a rate setting proceeding and that hearings would be necessary. There was no objection to the ratesetting categorization.

31. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code, and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on ________________, and reply comments were filed on _____________________ by __________________________.

32. Assignment of Proceeding

Catherine J. K. Sandoval is the assigned Commissioner and Seaneen M. Wilson is the assigned ALJ in this proceeding.

33. Findings of Fact

1. SJWC filed A. 12-01-003 requesting an increase over currently authorized rates of $47,394,000 in 2013, $12,963,000 in 2014, and $34,797,000 in 2015.
2. ORA protested A.12-01-003 on February 6, 2012.
3. Protests to the Application were filed by ORA and the Six Mutuals.
4. In order to accurately estimate test year revenues at present rates, revenues are adjusted by all Contributions in Aid of construction, revenue collected for the upsize meter charge and increased service charge revenue collected under Schedule 1C Tariff.
5. The settlement between SJWC and the Mutuals resolves all outstanding issues, and is reasonable.

6. Because SJWC and the Mutuals agreed to the removal of the "elevation charge" in their settlement agreement, ORA's concerns regarding the "elevation charge" are moot.

7. Conservation goals beyond those already achieved by SJWC are critical to limited water resources.

8. SJWC's estimate of water consumption based on the "new committee method" adjusted for reductions in consumption is reasonable.

9. A reasonable method to project the number of customers is to average ORA use of a five-year average capturing economic changes over a long time, and SJWC's use of a three-year average that reflects current customer trends.

10. Although SJWC should be allowed to continue its Recycled Water Program, due to uncertainties raised and not resolved in the Commission's recent R.10-11-014, it is premature to expand this program as SJWC proposes.

11. It is unreasonable to include customer growth escalation factors in test year expenses as test year expenses are escalated due to other factors.

12. D.07-05-062 applies customer growth to test year expense estimates to calculate escalation year expenses.

13. A reasonable method to determine union employee payroll expenses is to apply union employee contract increases based on a negotiated contract.

14. A reasonable method to determine payroll for administrative and officer employees is to review historical payroll trends for these employees.

15. Use of recent actuarial information to estimate future P&B costs is a reasonable method to estimate such costs as opposed to using recorded information and the actuarial information.

16. SJWC's and ORA's recommended use of a percentage of total payroll to determine retirement Savings Plan expense is reasonable.

17. Use of recent actuarial information to estimate PBOP is a reasonable method to estimate such costs as opposed to using recorded information and the recent actuarial information.

18. It is reasonable to estimate SJWC's medical insurance costs using cost trends and expected health premium costs.

19. The cost of Other Employee Benefits recognizes factors such as training, licensing and an aging workforce instead of using an average of only recorded expenses.

20. It is reasonable that Transportation Labor expense is an allocation of adopted payroll expense.

21. It is reasonable to determine Transportation Payroll Tax as proportional to Transportation Labor expense.

22. It is reasonable to estimate Transportation Insurance cost based on two years of recorded data rather than one year.

23. Because Transportation Fuel Expenses demonstrate significant fluctuations during the past five years, a reasonable method for estimating such costs is to use an average of the five recorded year amounts.

24. Although the addition of four new staff to SJWC's operations will increase transportation fuel costs in Test Year 2013, these costs will likely be offset due to the greater fuel efficiency of new vehicles.

25. Transportation Depreciation expenses are reasonably proportional to the total number of vehicles included in plant.

26. Because Other Transportation Expenses have fluctuated over the past years, a reasonable estimate of such expenses in Test Year 2013 is use an average of past years' recorded expenses.

27. As Other Sources of Supply expense varies over time, a five-year average of past expenses escalated to Test Year 2013 is reasonable for this expense.

28. A reasonable estimate of purchased power expenses is based on customer estimates. Because reasonable customer estimates are based on an average of ORA's and SJWC's amounts, estimated purchased power expense should be based on an average of ORA's and SJWC's Purchased Power estimates.

29. The Pump Tax expense is proportional to estimated water usage.

30. Expenses as this represents an allocation of other reasonably determined amounts for Labor, Transportation, and Purchased Material and supply.

31. A reasonable estimate for Chemical Expenses reflects both the trend in chemical costs and the amount of water being treated.

32. It is reasonable to allocate Labor, Transportation and Purchased Materials and Supply expenses to determine Other Water Treatment expense, and to adjust this amount by determined water quality regulatory expense.

33. Reasonable T&D expenses reflect removal of customer growth escalation.

34. In addition to developing recycled water policies, R.10-11-014 is intended to determine how costs of recycled water infrastructure should be allocated among stakeholders, including customer, IOUs, and public agencies not regulated by the Commission. Therefore, it is premature to allocate recycled water costs at this time.

35. SJWC's proposed Recycled Water Plan shows recycled water usage in 20 years equivalent to SJWC's proposed 2015 recycled water use.

36. ORA's proposed recommended Recycled Water Plan included four alignments that would allow SJWC to meet its recycled water usage for 2015.

37. The Commission supports development of recycled water, as stated in the 2010 Water Action Plan.

38. Reasonable Plant Maintenance expenses are an allocation of the reasonable costs for Labor, Transportation, and Purchased Services expense determined herein.

39. A reasonable estimate of Service O&M expense is $76,702.

40. A reasonable estimate of Office Supplies expense reflects the annual increase in such expenses but not the customer growth escalation.

41. It is reasonable to base Property Insurance expense on an expert opinion for anticipated insurance costs.

42. ORA's estimate for WCI is reasonable as it relies on SJWC's broker's estimate and recent escalation rates.

43. The recorded amounts for PLI between 2009 and 2011 continually decline but SJWC's estimate for PLI which is based on its broker's estimate for this expense exceeds the 2011 recorded amount by almost 68%.

44. As demonstrated by the lack of a settlement agreement in this proceeding, Regulatory Commission activities and consequently expenses may exceed normally expected activities and expenses.

45. As both SJWC's and ORA's estimates of regulatory expenses are not well founded, an average of these two estimates is a reasonable estimate for this expense.

46. It is reasonable to exclude from customer rates amounts paid to organizations which have no demonstrated value to ratepayers.

47. Recent rental cost agreements are a reasonable indication of test year rental costs.

48. Ad Valorem tax estimates are based on the amount of adopted utility plant in service. Payroll tax estimates are be based on the amount of adopted payroll.

49. Reasonable franchise fees are based on adopted revenues in the test year. Income taxes are be based on the adopted ratemaking expenses and plant amounts.

50. Estimates of reasonable plant additions in test year 2013, and attrition years 2014 and 2015 are as described herein.

51. It is reasonable to require that depreciation studies in future GRCs to link utility plant and depreciation in a manner that facilitates the review of depreciation data.

52. SPU-16 shows that book depreciation is an expense in the lead-lag study, however book depreciation in this study is assigned zero lag days.

53. SPU-16 specifically excludes interest expense as a cash component in the lead-lag study.

54. It is unreasonable to include in rates those conservation programs which are duplicated by others.

55. Conservation programs which can be justified by their cost, effectiveness and benefits can reasonably be included in rates.

56. NTP&S rules as defined by D.10-10-019, and modified by D.11-10-034 and D.12-01-042, do not permit inclusion in rates of those non-incremental costs used to provide NTP&S.

57. It is not the definition of whether costs are incremental or non-incremental to providing service to ratepayers that determines whether they can be included in rates, but whether these costs provide NTP&S that determines if the costs are reasonable for inclusion in rates.

58. As there exist many uncertainties as a result of ACA, establishing an ACA memorandum account at this time is unreasonable.

59. SJWC does not have control over regulations implemented by the SEC.

60. IFRS expenses are expected to occur between this GRC and SJWC's next GRC.

61. Substantial costs are expected to be incurred to comply with IFRS as promulgated by the SEC.

62. Establishing a memorandum account for IFRS expenses will benefit ratepayers because only those expenses directly related to IFRS will be included in rates, rather than an estimate of such costs.

63. SJWC should be authorized to establish an IFRS memorandum account to prospectively record IFRS compliance related costs, because the expenses recorded in the memorandum account meet the criteria necessary to establish a memorandum account.

64. Chromium VI Maximum Contaminant Level (MCL) of 10 parts per billion was adopted effective July 1, 2014. The costs for compliance with Chromium VI MCL are uncertain based on the record in this proceeding.

65. SJWC should be allowed an opportunity to request a memorandum account for compliance with these standards through an advice letter filing once compliance requirements are understood.

66. It is reasonable to remove the Tax Relief Act balance of $452,000 from the Resolution L-411 Memorandum Account, and review this memorandum account in SJWC's next GRC.

67. The recommendation of SJWC and ORA to recover $2,598,912 in balancing accounts and refund $650,456 in various memorandum accounts is reasonable.

68. Customers using the least amounts of water in the lowest tier should not be subject to the greatest percentage rate increase as a result of SJWC's GRC. Instead, it is reasonable that customers using the least amount of water should see rate increases that are similar to rate increases for customers in higher tiers.

69. ORA's proposed rate design provides an incentive for conservation while maintaining flexibility in rates.

70. SJWC's current Monterey-Style WRAM does not fully protect SJWC against reduced water sales. However, SJWC's Monterey-Style WRAM also allows SJWC to benefit when sales increase.

71. It is uncertain whether SJWCs' Monterey-Style WRAM, rather than those WRAMs used by other water utilities, is an adequate mechanism to encourage conservation and whether it serves and balances the interests of the utility and its customers due to increased or decreased sales.

Conclusions of Law

1. SJWC should be authorized to increase rates by amounts designed to increase revenue by $22,063,000 or 9.79% in its test year 2013, $11,579,000 or 4.72% in 2014, and $15,356,000 or 6.02% in 2015. Based on this, the monthly bill for the average SJWC residential customers using 1500 CCF of water with a 5/8" by 3/4" meter would increase by $7.96 or 20.8% to $46.20 from $38.24 for the test year 2013.

2. The rates adopted herein are just, reasonable, and nondiscriminatory.

3. It is unreasonable to include in rates those expenses incurred to provide NTP&S regardless of whether such expenses are incremental or non-incremental to utility service.

4. SJWC's application should be granted to the extent provided by the following order.

5. SJWC should be authorized to file, by Tier 1 Advice Letter, revised tariff schedules, and to concurrently cancel its present schedule for such service. This filing should be subject to approval by the Commission's DWA. The effective date of the revised schedules should be five days after filing.

6. The surcharge to true-up the interim rates should comply with Standard Practice U-27-W.

7. Four new employees should be added to the payroll expense for test year 2013 reflecting growth in customers despite reductions due to NTP&S and currently funded but vacant positions.

8. Employee Stock Purchase Plan cost of $122,000 is reasonable and should be adopted, as it excludes the customer growth factor.

9. Unfunded Pension Expense of $65,000 is reasonable and should be adopted.

10. As water quality is a safety matter, and as CDPH may increase both its rates and the number of water quality tests it conducts, the Commission should adopt $206,303 for Water Quality Regulatory Fees.

11. A one-time cost such as the Watershed Maintenance Regional General Permit cost should be amortized over the period between GRCs, or three years.

12. Purchased Water expense of $45,137,000 is reasonable and should be adopted.

13. The Commission should adopt $2,852,300 for Other Pumping expense.

14. Four alignments should be included in the Recycled Water Plan adopted by the Commission for SJWC.

15. The Commission should adopt $76,702 for Purchased Service O&M, as this cost excluded escalation for customer growth.

16. The Commission should adopt PLI expense of $973,000, for Test Year 2013.

17. The Commission should adopt rental expense for the Bascom Avenue Facility of $382,000.

18. SJWC should update its Tariff Schedule No.1B General Metered Service With Automatic Fire Sprinkler System to include meters of 1-1/2 and 3-inches.

19. For escalation year 2014, SJWC should file a Tier 1 Advice Letter in conformance with GO 96-B proposing a new revenue requirement and corresponding revised tariff schedules. The new revenue requirement should be calculated using an effective date of January 1, 2014. The shortfall in the calculated revenue requirement between the January 1, 2014 effective date and the effective date of the 2014 escalation year 2014 filing should be included in the surcharge calculation used to true-up the difference between interim and adopted rates. The escalation year 2014 Advice Letter should be filed within 20 days of the effective date of this decision. The proposed revised revenue requirement and rates should be reviewed by the DWA. DWA should inform the Commission if it finds that the revised rates do not conform to the RRCP, this order or other Commission decisions, and if so, should reject the filing.

20. For escalation year 2015 SJWC should file a Tier 1 Advice Letter, including work papers, no later than 45 days prior to the first day of the 2015 escalation year. To the extent that the pro forma earnings test for the 12 months ending September 30, 2014, as adopted in D. 04-06-018, exceeds the amount authorized in this decision, the requested increase must be reduced by the utility from the level authorized in this decision to conform to the pro-forma earnings test. The proposed revenue requirement and rates must be reviewed by the DWA. The DWA must inform the Commission if it finds that the revised rates do not conform to the RRCP, this order, or other Commission decision, and if so, reject the filing.

21. SJWC should file an advice letter requesting establishment of a memorandum account to record costs necessary to comply with Chromium IV standards.

22. SJWC should be authorized to file a Tier 1 Advice Letter requesting to establish an IFRS memorandum account to prospectively record IFRS compliance related costs. Costs in the IFRS memorandum account should be subject to a reasonableness review by DWA.

23. SJWC should be authorized to transfer $452,200 from its one-way 2010 Tax Act Memorandum Account. This memorandum account should be reviewed in SJWC's next GRC unless any balance in this account exceeds 2% of the authorized revenue requirement, in which case SJWC should propose a rate adjustment consistent with D.06-04-037.

24. As proposed by ORA and SJWC, SJWC should be authorized to recover the $2,598,912 under-collection in various balancing accounts via a 12-month surcharge of $0.0492 per CCF, and provide a refund of the $650,456 over-collection through a surcredit of $0.25 per service connection per month for 12 months for various memorandum accounts.

25. Recovery of the revenue requirement authorized in this order should be recovered utilizing the rate design proposed by ORA.

26. All motions not specifically ruled upon are denied.

27. This order should be effective immediately.

O R D E R

IT IS ORDERED that:

1. San Jose Water Company (SJWC) is authorized to increase rates by amounts designed to increase revenue by $22,063,000 or 9.79% in its test year

2013, $11,579,000 or 4.72% in 2014, and $15,356,000 or 6.02% in 2015. As a result of the revenue increase granted by this decision, the monthly bill for the average SJWC residential customers using 1500 cubic feet (CCF) of water with a 5/8" by 3/4" meter would increase by $7.96 or 20.8% to $46.20 from $38.24 for the test year 2013. This adopted rate changes include but are not limited to the following:

a. Four new employees are added to SJWC's payroll expense for test year 2013.

b. SJWC's Employee Stock Purchase Plan cost of $122,000 is adopted.

c. Unfunded Pension Expense $65,000 is adopted.

d. Water Quality Regulatory Fees of $206,303 is adopted.

e. A one-time cost such as the Watershed Maintenance Regional General Permit cost shall be amortized over the period between general rate cases, or three years.

f. Purchased Water expense of $45,137,000 is adopted.

g. Other Pumping expense of $2,852,300 is adopted.

h. Four alignments are included in San Jose Water Company's Recycled Water Plan.

i. Purchased Services Operations and Maintenance expense of $76,702 is adopted.

j. Public Liability Insurance expense of $973,000 is adopted.

k. Rental expense of $382,000 for the Bascom Avenue Facility is adopted.

1. San Jose Water Company is authorized to file by Tier 1 Advice Letter, the revised tariff schedules attached to this decision as Appendices…and to concurrently cancel its present schedules for such service.

2. San Jose Water Company (SJWC) is authorized to file by Tier 1 Advice Letter for a surcharge to true-up the difference between interim rates and

adopted rates. The surcharge must comply with Standard Practice U-27-W. The Tariff implementing the surcharge may be included in the filing authorized in Ordering Paragraph 3 or filed after SJWC calculates the revenue difference between interim rates and adopted rates. As the effective date of this order is after the beginning of the 2014 escalation year, the surcharge shall include differences between interim rates and adopted rates through the 2014 escalation year up to the effective date of this order.

3. For escalation year 2014, San Jose Water Company must file a Tier 1 Advice Letter within 20 days of the effective date of this order. This Advice Letter must be in conformance with General Order 96-B proposing new revenue requirements and corresponding revised tariff schedules. San Jose Water Company's advice letters must follow the escalation procedures set forth in the Revised Rate Case Plan (RRCP) for Class A Water Utilities adopted in Decision 07-05-062 and must include supporting work papers. To the extent that the pro forma earnings test for the 12 months ending September 30, 2013, as adopted in Decision 04-06-018, exceeds the amount authorized in this decision, the requested increase must be reduced by the utility from the level authorized in this decision to conform to the pro-forma earnings test. The revised tariff schedule for 2014 escalation will be effective no earlier than 45 days from the date of filing. The proposed revenue requirements and rates must be reviewed by the Commission's Division of Water and Audits (DWA). The DWA must inform the Commission if it finds that the revised rates do not conform to the RRCP, this order, or other Commission decision, and if so, reject the filing.

4. For escalation year 2015, San Jose Water Company must file a Tier 1 Advice Letter, including work papers, no later than 45 days prior to the first day of the 2015 escalation year. To the extent that the pro forma earnings test for the

12 months ending September 30, 2014, as adopted in Decision 04-06-018, exceeds the amount authorized in this decision, the requested increase must be reduced by the utility from the level authorized in this decision to conform to the pro-forma earnings test. The proposed revised revenue requirements and rates must be reviewed by the DWA. The DWA must inform the Commission if it finds that the revised rates do not conform to the RRCP, this order, or other Commission decision, and if so, reject the filing.

5. San Jose Water Company is authorized to file a Tier 1 Advice Letter requesting to establish an International Financial Reporting Standards (IFRS) memorandum account to prospectively record IFRS compliance related costs. Costs recorded in the IFRS memorandum account are subject to review for reasonableness by the Commission's Division of Water and Audits when SJWC requests recovery in rates for costs recorded in this account. SJWC shall report in its next General Rate Case whether the IFRS account should be continued.

6. San Jose Water Company may file an advice letter requesting establishment of a memorandum account to record costs necessary to comply with Chromium IV Maximum Contaminant Level established by the California Department of Health Services effective July 1, 2014.

7. San Jose Water Company is authorized to transfer the amount of $452,200, from its one-way 2010 Tax Act Memorandum Account. This memorandum account will be reviewed in SJWC's next general rate case unless any balance in this account exceeds 2% of the authorized revenue requirement, in which case the utility may propose a rate adjustment consistent with Decision 06-04-037.

8. San Jose Water Company is authorized to recover the $2,598,912 under-collection in various balancing accounts via a 12-month surcharge of

$0.0492 per hundred cubic feet, and provide a refund of $650,456 under-collection through a surcredit of $0.25 per service connection per month for 12 months for various memorandum accounts.

9. San Jose Water Company is authorized to revise its Tariff Schedule Number 1B to include meter sizes of 1.5 inches and 3 inches. SJWC shall provide data on the number of customers in this tariff schedule in its next GRC.

10. Recovery of the revenue requirement authorized in this order shall be recovered utilizing the rate design proposed by the Division of Ratepayer Advocates.

11. Application 12-01-003 is closed.

This order is effective today.

Dated ______________________________, at San Francisco, California.

ATTACHMENT A
TABLE A
Summary of Earnings and Rate of Return
Effective January 1, 2013
(Dollars in Thousands)

Line			Present Rates Effective 1-Jan-13		Authorized Rates Effective 1-Jan-13
1					
2					
3					
4	OPERATING REVENUES		$ 225,307		$ 249,989
5	DEFERRED REVENUE		$ 388		$ 388
6	OPERATING EXPENSES				
7		PURCHASED WATER	$ 48,713		$ 48,713
8		PUMP TAX	$ 35,384		$ 35,384
9		PURCHASED POWER	$ 5,995		$ 5,995
10		OTHER OPERATION AND MAINTENANCE	$ 657		$ 657
11		CHEMICALS	$ 519		$ 519
12		UNCOLLECTIBLES	$ 486		$ 486
13		O&M PAYROLL	$ 18,931		$ 18,931
14		TRANSPORTATION	$ 2,446		$ 2,446
15		PURCHASED SERVICES	$ 8,101		$ 8,101
16		CONSERVATION	$ 217		$ 217
17		OTHER ADMIN AND GEN. EXP.	$ 3,425		$ 3,425
18		A&G PAYROLL	$ 7,188		$ 7,188
19		PENSION	$ 9,693		$ 9,693
20		BENEFITS	$ 2,814		$ 2,814
21		HEALTH CARE & DENTAL	$ 5,043		$ 5,043
22		RENTS	$ 311		$ 311
23		PROPERTY INSURANCE	$ 194		$ 194
24		LIABILITY INSURANCE	$ 1,501		$ 1,501
25		A&G PURCHASED SERVICES	$ 2,734		$ 2,734
26		A&G TRANSFERRED SERVICES	$ (6,613)		$ (6,613)
27		TOTAL O. & M., A. & G., & MISC. EXP.	$ 147,739		$ 147,739
28	TAXES OTHER THAN INCOME				
29		AD VALOREM TAXES	$ 5,978		$ 5,978
30		LOCAL FRANCHISE TAXES & BUS. LIC.	$ 562		$ 620
31		PAYROLL TAXES	$ 2,402		$ 2,402
32		TOTAL GENERAL TAXES	$ 8,943		$ 9,001
33	DEPRECIATION & AMORTIZATION		$ 32,892		$ 32,892
34		S U B -T O T A L - OPERATING EXPENSES	$ 189,574		$ 189,632
35	INCOME TAXES:				
36		STATE INCOME TAX	$ 1,357		$ 3,528
37		FEDERAL INCOME TAX	$ 5,319		$ 13,153
38	TOTAL OPERATING EXPENSES		$ 196,250		$ 206,313
39	NET OPERATING REVENUE		$ 29,445		$ 44,064
40	DEPRECIATED RATE BASE		$ 516,464		$ 516,464
41	RATE OF RETURN		5.70%		8.53%
42	% INCREASE				10.94%

ATTACHMENT A
TABLE B
Summary of Earnings and Rate of Return
Effective July 1, 2013
(Dollars in Thousands)

Line			Authorized Rates Effective 1-Jul-13
1			
2			
3			
4	OPERATING REVENUES		$ 257,231
5	DEFERRED REVENUE		$ 388
6	OPERATING EXPENSES		
7		PURCHASED WATER	$ 52,626
8		PUMP TAX	$ 38,683
9		PURCHASED POWER	$ 5,995
10		OTHER OPERATION AND MAINTENANCE	$ 657
11		CHEMICALS	$ 519
12		UNCOLLECTIBLES	$ 499
13		O&M PAYROLL	$ 18,931
14		TRANSPORTATION	$ 2,446
15		PURCHASED SERVICES	$ 8,101
16		CONSERVATION	$ 217
17		OTHER ADMIN AND GEN. EXP.	$ 3,425
18		A&G PAYROLL	$ 7,188
19		PENSION	$ 9,693
20		BENEFITS	$ 2,814
21		HEALTH CARE & DENTAL	$ 5,043
22		RENTS	$ 311
23		PROPERTY INSURANCE	$ 194
24		LIABILITY INSURANCE	$ 1,501
25		A&G PURCHASED SERVICES	$ 2,734
26		A&G TRANSFERRED SERVICES	$ (6,613)
27		TOTAL O. & M., A. & G., & MISC. EXP.	$ 154,965
28	TAXES OTHER THAN INCOME		
29		AD VALOREM TAXES	$ 5,978
30		LOCAL FRANCHISE TAXES & BUS. LIC.	$ 637
31		PAYROLL TAXES	$ 2,402
32		TOTAL GENERAL TAXES	$ 9,018
33	DEPRECIATION & AMORTIZATION		$ 32,892
34		S U B -T O T A L - OPERATING EXPENSES	$ 196,875
35	INCOME TAXES:		
36		STATE INCOME TAX	$ 3,528
37		FEDERAL INCOME TAX	$ 13,153
38	TOTAL OPERATING EXPENSES		$ 213,556
39	NET OPERATING REVENUE		$ 44,064
40	DEPRECIATED RATE BASE		$ 516,674
41	RATE OF RETURN		8.53%

ATTACHMENT A
TABLE C
Summary of Earnings and Rate of Return
Effective January 1, 2014
(Dollars in Thousands)

Line		Authorized Rates Effective 1-Jan-14
1		
2		
3		
4	OPERATING REVENUES	$ 270,872
5	DEFERRED REVENUE	$ 388
6	OPERATING EXPENSES	
7	PURCHASED WATER	$ 52,785
8	PUMP TAX	$ 38,800
9	PURCHASED POWER	$ 6,013
10	OTHER OPERATION AND MAINTENANCE	$ 669
11	CHEMICALS	$ 528
12	UNCOLLECTIBLES	$ 508
13	O&M PAYROLL	$ 19,272
14	TRANSPORTATION	$ 2,488
15	PURCHASED SERVICES	$ 8,247
16	CONSERVATION	$ 221
17	OTHER ADMIN AND GEN. EXP.	$ 3,483
18	A&G PAYROLL	$ 7,317
19	PENSION	$ 9,868
20	BENEFITS	$ 2,865
21	HEALTH CARE & DENTAL	$ 5,134
22	RENTS	$ 317
23	PROPERTY INSURANCE	$ 198
24	LIABILITY INSURANCE	$ 1,528
25	A&G PURCHASED SERVICES	$ 2,783
26	A&G TRANSFERRED SERVICES	$ (6,726)
27	TOTAL O. & M., A. & G., & MISC. EXP.	$ 156,296
28	TAXES OTHER THAN INCOME	
29	AD VALOREM TAXES	$ 6,080
30	LOCAL FRANCHISE TAXES & BUS. LIC.	$ 648
31	PAYROLL TAXES	$ 2,446
32	TOTAL GENERAL TAXES	$ 9,174
33	DEPRECIATION & AMORTIZATION	$ 35,283
34	S U B -T O T A L - OPERATING EXPENSES	$ 200,752
35	INCOME TAXES:	
36	STATE INCOME TAX	$ 4,657
37	FEDERAL INCOME TAX	$ 17,375
38	TOTAL OPERATING EXPENSES	$ 222,784
39	NET OPERATING REVENUE	$ 48,476
40	DEPRECIATED RATE BASE	$ 567,168
41	RATE OF RETURN	8.55%

ATTACHMENT A
TABLE D
INCOME TAX CALCULATION
(Dollars in Thousands)

Line	Item	2013	2014
1	**Operating Revenue**	$ 247,369	$ 270,872
2	(Excluding Deferred Revenue)		
3			
4	Deductions		
5	O&M Expenses (Excl. Uncollectibles)	$ 121,324	$ 122,776
6	Uncollecibles	$ 457	$ 506
7	A&G Expenses	$ 26,289	$ 27,685
8	Taxes Other than Income Taxes	$ 8,412	$ 8,920
9	Local Franchise Taxes	$ 582	$ 613
10	Transportation Depreciation	$ (831)	$ (874)
11	Interest Expense	$ 16,748	$ 18,396
12	Meal Dissalowance, 50%	$ 89	$ 89
13	**Total Deductions**	**$ 173,071**	**$ 178,111**
14			
15	State Corporation Franchise Tax		
16	Tax Depreciation	$ 35,157	$ 39,145
17	Deferred Revenue (Net of Tax)	$ 229	$ 225
18	State Taxable Income	$ 39,369	$ 53,841
19	State Income Tax Rate	8.84%	8.84%
20	**State Income Tax**	**$ 3,480**	**$ 4,760**
21			
22	Federal Income Tax		
23	Tax Depreciation	$ 33,745	$ 37,298
24	State Franchise Tax	$ 3,480	$ 4,760
25	IRS Sect 199 QPA Deduction	$ -	$ -
26	Federal Taxable Income	$ 37,072	$ 50,703
27	Federal Income Tax Rate	35.00%	35.00%
28	**Federal Income Tax**	**$ 12,975**	**$ 17,746**
29			
30	Amortization of Prepaid Tax on CIAC	$ 6	$ 6
31			
32	Total Income Tax	16,461	22,512

ATTACHMENT A
TABLE E
Authorized Construction Budget
(Dollars in Thousands)

Line	Item	Adopted 2012	Adopted 2013	Adopted 2014
1	**CONSTRUCTION ITEM**			
2	Land	$ 10,300	$ 10,300	$ 10,300
3				
4	Source of Supply	$ 3,562,600	$ 5,968,600	$ 5,819,900
5				
6	Water Treatment	$ 502,400	$ 338,300	$ 20,100
7				
8	Reservoirs & Tanks	$13,302,600	$14,280,800	$ 15,953,400
9				
10	Pump Stations & Equipment	$ 7,108,800	$ 5,977,100	$ 11,164,000
11				
12	Distribution Systems:			
13	New Mains	$ 5,717,000	$ -	$ -
14	Service Transfers	$ 67,000	$ 167,100	$ 24,600
15	City, County & State	$ 412,000	$ 424,400	$ 437,100
16	Replacement Mains	$29,142,500	$33,297,600	$ 33,843,700
17	Main Extensions	$ 2,207,500	$ 2,419,000	$ 2,294,700
18	Services	$ 5,527,300	$ 6,539,000	$ 6,765,000
19	Meters	$ 3,665,570	$ 4,025,624	$ 4,222,475
20	Hydrants	$ 395,600	$ 407,500	$ 419,800
21				
22	Equipment	$ 4,249,600	$ 2,536,100	$ 2,126,100
23				
24	Structures & Non-Specifics	$ 2,917,210	$ 2,255,230	$ 873,675
25				
26	Green & Alternative Energy	$ -	$ -	$ -
27				
28	TOTAL CONSTRUCTION BUDGET	$78,787,980	$78,646,654	$ 83,974,850
29				
30	Cost of Retiring, Incl. in Budget	$ 2,060,000	$ 2,121,800	$ 2,185,500
31				
32	**TOTAL NEW PROJECTS**	$76,727,980	$76,524,854	$ 81,789,350

ATTACHMENT A
TABLE F
Authorized Ratebase
(Dollars in Thousands)

Line	Item	2013	Adopted 2014	Adopted
1	**ITEM**			
2	Utility Plant	$ 1,124,588	$ 1,203,898	
3	Materials & Supplies	$ 624	$ 624	
4	Working Cash	$ 9,702	$ 10,094	
5				
6	Depreciation Reserve	$ (383,502)	$ (419,654)	
7	Advances	$ (57,553)	$ (55,487)	
8	Contributions	$ (107,668)	$ (108,445)	
9	Plant Funded by SDWSRF Loan	$ (1,981)	$ (1,820)	
10	Reserve for Amortization	$ (438)	$ (454)	
11	Tax Deferrals	$ (74,196)	$ (68,255)	
12				
13	Rate Base, Taxed Contributions	$ 4,259	$ 4,201	
14	Rate Base, Taxed Advances	$ 2,629	$ 2,467	
15				
16	**RATE BASE**	$ 516,464	$ 567,168	

ATTACHMENT A
TABLE G
Authorized Customer and Sales Forecast

Line	Item	2013
1	Metered Services	
2	Residential	197,154
3	Business	20,301
4	Industrial	53
5	Public Authority	1,283
6	Resale	30
7	Other	112
8	**Total Potable Metered Services**	**218,933**
9	Raw Water	3
10	Recycled Water	132
11	**Total Non-Potable Metered Services**	**219,068**
12	Private Fire Service	3,567
13	**Total Active Services**	**222,635**
14	Average Sales per Customer (ccf/connection/yr)	
15	Residential	170
16	Business	819
17	Total Sales Per Customer Class (Kccf)	
18	Residential	33,496
19	Business	16,565
20	Industrial	216
21	Public Authority	2,598
22	Resale	256
23	Other	71
24	**Total Potable Metered Sales**	**53,202**
25	Raw Water	14
26	Recycled Water	673
27	**Total Sales**	**53,889**
28	Source of Supply (Kccf)	
29	Purchased Water	29,388
30	Surface Water	2,794
31	Well Supply	24,779
32	**Total Supply**	**56,961**

ATTACHMENT A
TABLE H
Miscellaneous Adopted Quantities

Line	Item	Authorized 2013	
1	Water Production	MG	Kccf
2	Purchased Water	21,984	29,388
3	Surface Water	2,090	2,794
4	Well Supply	18,536	24,779
5	Recycled Water	503	673
6	**Total Production**	**43,114**	**57,634**
7			
8	Purchased Water/Pump Tax Rates		
9	(effective July 1, 2013)		
10	Purchased Water ($ per MG)	$ 2,216	
11	Pump Tax ($ per MG)	$ 1,909	
12			
13	Purchased Water/Pump Tax Rates		
14	(effective July 1, 2013)		
15	Purchased Water ($ per MG)	$ 2,394	
16	Pump Tax ($ per MG)	$ 2,087	
17			
18	Purchased Power		
19	(effective January 1, 2013)		
19	Mixed Power Cost ($/kWh)	$ 0.15267	
20	Total Power Usage (kWh)	39,269,009	
21			
22	Other		
23	Net-to-Gross Multiplier	1.6947	
24	Customer Growth Factor	0.3%	
25	Uncollectible Rate	0.1843%	
26	Local Franchise Tax Rate	0.2354%	
27	California Corporate Franchise Tax Rate	8.84%	
28	Federal Tax Rate	35.00%	

ATTACHMENT A
TABLE I
Schedule 1 Rates
Effective January 1, 2013

Line	Item	Effective 1/1/2013
1	SCHEDULE NO. 1	
2	Service Charges	
3	5/8 x3/4-inch meter	$ 19.24
4	3/4-inch meter	$ 19.24
5	1-inch meter	$ 32.06
6	1 1/2-inch meter	$ 64.12
7	2-inch meter	$ 102.59
8	3-inch meter	$ 192.35
9	4-inch meter	$ 320.59
10	6-inch meter	$ 641.18
11	8-inch meter	$ 1,025.89
12	10-inch meter	$ 1,474.71
13		
14	Quantity Rates ($ per ccf)	
15	Residential Customers with 5/8 x 3/4-inch meter	
16	or 1-inch meter	
17	For Total Monthly Usage from 0 to 3 ccfs	$ 2.9491
18	For Total Monthly Usage fro 4 to 18 ccfs	$ 3.2768
19	For Total Monthly Usage from 19 ccfs and above	$ 3.6045
20		
21	All Other Customers	
22	For all water delivered	$ 3.2768

ATTACHMENT A
TABLE J
Schedule 1 Rates
Effective July 1, 2013

Line	Item	Effective 7/1/2013
1	SCHEDULE NO. 1	
2	Service Charges	
3	5/8 x3/4-inch meter	$ 19.24
4	3/4-inch meter	$ 19.24
5	1-inch meter	$ 32.06
6	1 1/2-inch meter	$ 64.12
7	2-inch meter	$ 102.59
8	3-inch meter	$ 192.35
9	4-inch meter	$ 320.59
10	6-inch meter	$ 641.18
11	8-inch meter	$ 1,025.89
12	10-inch meter	$ 1,474.71
13		
14	Quantity Rates ($ per ccf)	
15	Residential Customers with 5/8 x 3/4-inch meter	
16	or 1-inch meter	
17	For Total Monthly Usage fro 0 to 3 ccfs	$ 2.9491
18	For Total Monthly Usage fro 4 to 18 ccfs	$ 3.2768
19	For Total Monthly Usage fro 19 ccfs and above	$ 3.6045
20		
21	All Other Customers	
22	For all water delivered	$ 3.2768
23		
24	Purchased Water Cost Surcharge ($ per ccf):	$ 0.0739
25	For Purchased Water Unit Cost increase to $780 per Acre-ft	
26	effective July 1, 2013	
27		
28	Groundwater Extraction Cost Surcharge ($ per ccf):	$ 0.0623
29	For Groundwater Extraction Cost increase to $680 per Acre-ft	
30	effective July 1, 2013	

ATTACHMENT A
TABLE K
Schedule 1 Rates
Effective January 1, 2014

Line	Item	Effective 1/1/2014
1	SCHEDULE NO. 1	
2	Service Charges	
3	5/8 x3/4-inch meter	$ 20.68
4	3/4-inch meter	$ 20.68
5	1-inch meter	$ 34.47
6	1 1/2-inch meter	$ 68.94
7	2-inch meter	$ 110.30
8	3-inch meter	$ 206.81
9	4-inch meter	$ 344.68
10	6-inch meter	$ 689.36
11	8-inch meter	$ 1,102.98
12	10-inch meter	$ 1,585.53
13		
14	Quantity Rates ($ per ccf)	
15	Residential Customers with 5/8 x 3/4-inch meter	
16	or 1-inch meter	
17	For Total Monthly Usage from 0 to 3 ccfs	$ 3.3813
18	For Total Monthly Usage fro 4 to 18 ccfs	$ 3.4859
19	For Total Monthly Usage from 19 ccfs and above	$ 3.7125
20		
21	All Other Customers	
22	For all water delivered	$ 3.4859
23		
24	Purchased Water Cost Surcharge ($ per ccf):	$ 0.0739
25	For Purchased Water Unit Cost increase to $780 per Acre-ft	
26	effective July 1, 2013	
27		
28	Groundwater Extraction Cost Surcharge ($ per ccf):	$ 0.0623
29	For Groundwater Extraction Cost increase to $680 per Acre-ft	
30	effective July 1, 2013	

(END OF ATTACHMENT A)