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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of Application of Odd Fellows Sierra Recreation Association, a California corporation, and Sierra Park Water Company, Inc., a California corporation, for Certificate of Public Convenience and Necessity to Operate a Public Utility Water System near Long Barn, Tuolumne County, California and to Establish Rates for Service and For Sierra Park Water Company, Inc. to Issue Stock.	Application 13-09-023 (Filed September 20, 2013)
And Related Matter.	Case 12-03-017

ADMINISTRATIVE LAW JUDGE'S RULING ON WATER AND AUDIT DIVISION STAFF REPORT

By an informal email ruling served on October 1, 2014 I distributed a copy of a report prepared at my request by the Commission's Division of Water and Audits. This formal ruling affirms that email ruling and attaches the report for inclusion in the formal file for this proceeding.

The email ruling stated:

By an e-mail ruling dated June 2, 2014, the Commission's Division of Water and Audits was asked to perform some rate analysis and provide any expert recommendations. Attached to this ruling is the Water Division's report to the assigned Administrative Law Judge (Judge) dated September 30, 2014.

1. The Odd Fellows Sierra Recreation Association, Sierra Park Service Company and Sierra Park Water Company, Inc. may jointly file and serve Comments on this report no later than Friday, November 5, 2014.
2. The Complainants in Case 12-03-017 may also jointly file and serve Comments on this report no later than Friday, November 5, 2014.
3. Any party or Complainant may request an evidentiary hearing. This request must be separately filed and served no later than November 7, 2014 and must demonstrate good cause why the matters raised may only be resolved by hearing.
4. Reply Comments may be filed and served by all parties and complainants no later than Wednesday, November 26, 2014.
5. All Comments and Replies should not exceed 25 pages without prior approval by the Judge.
6. The staff of Water Division is asked to cooperate with the parties and complainants by providing any technical explanations or worksheets which would facilitate preparing Comments. The Water Division need not prepare any further analysis for the parties or Complainants.
7. All persons served a copy of this ruling are asked to reply to the Judge, simply acknowledging receipt of the ruling. (Please do not reply to ALJ Docket or anyone on the "cc" list.)

IT IS RULED that:

1. The parties and complainants are directed to respond as directed above and in the October 1, 2014 email ruling to the report (attached) prepared by the Commission's Division of Water and Audits.

2. Parties and Complainants need only acknowledge one time the receipt of either this ruling or the email ruling.

Dated October 7, 2014, at San Francisco, California.

/s/ DOUGLAS M. LONG
Douglas M. Long
Administrative Law Judge

ATTACHMENT

STATE OF CALIFORNIA EDMUND G. BROWN JR., *Governor*

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE

SAN FRANCISCO, CA 94102-3298

September 30, 2014

To: Administrative Law Judge Douglas Long

Subject: Staff report on A. 13-09-023 and C. 1203017

Pursuant to an e-mail Ruling of June 2, 2014 by Administrative Law Judge Douglas Long in the subject proceedings, the Division of Water and Audits hereby transmits its Staff Report. Any comments on the report should be directed to Mr. Ravi Kumra, P. E., at (415) 703-2571 or ravi.kumra@cpuc.ca.gov.

Ravi Kumra, P. E.
Senior Utilities Engineer
Division of Water and Audits

<u>California Public Utilities Commission</u>

<u>Division of Water and Audits</u>

<u>STAFF REPORT</u>

<u>ON</u>

<u>APPLICATION OF</u>

<u>Odd Fellows Sierra Recreation Association and Sierra Park Water Company, Inc.</u>

<u>For Certificate of Public Convenience and Necessity</u>

<u>A. 13-09-023</u>

<u>AND</u>

<u>Complaint by Fred Coleman, Steven Wallace, Larry L. Vaughn and Ruth Dargitz</u>

<u>Vs</u>

<u>Odd Fellows Sierra Recreation Association</u>

<u>C 13-03-017</u>

<u>September 30, 2014</u>

TABLE OF CONTENTS

Executive Summary

Based on a review of Application (A.) 13-09-023, Complaint (C.) 12-03-017 and the e-mail ruling of Administrative Law Judge (ALJ) Douglas Long dated June 2, 2014, the Division of Water and Audits (DWA) staff finds that:

1) The Odd Fellows Sierra Recreation Association (Recreation Association) which provided water to the Odd Fellows Sierra Homeowners Association (OFSHA), and later to certain lot owners within the OFSHA Subdivision, overcharged these lot owners for water service. In March 2013 when the Recreation Association formed the Sierra Park Water Company (Water Company), it too over-charged these lot owners. Staff recommends that the over-charged amounts for these lot owners should be refunded to each lot owner based on the over-charged amounts between March 2012 and the present;

2) Going forward, the monthly water service charge amount for each lot should be reduced to conform to revenue requirements shown in Tables 1 and 3. Some expenses reported by the Recreation Association and the Water Company (Applicants) were not appropriately justified and should be disallowed;

3) Applicants should develop formal Affiliate Transaction rules for all transactions between the Water Company , the Recreation Association and the Service Company and report compliance with those rules to the Commission during the next General Rate Case (GRC);

4) The Water Company should hire an engineering consultant to conduct an engineering study to: a) survey and evaluate the existing distribution system; b) recommend needed capital improvements; and c) recommend a capital budget with a time line for the same. The consultant should also develop a schedule for converting the existing unmetered water connections to metered connections in the development;

5) The Water Company should collect $40,000 through a separate surcharge on all lot owners over the next two years to fund the engineering study, subject to refund. All expenses associated with the study and revenues collected through the surcharge should be tracked in a memorandum account for a future reasonableness review either as part of the next GRC or through a separate Tier 3 Advice Letter filing with the Division of Water and Audits (DWA);

6) The Water Company should have unfettered access to water properties at no charge; and

7) Water rights to Sugar Pine Creek should be transferred to the Water Company at no charge.

Section 1 ***<u>Introduction</u>***

By E-Mail Ruling of June 2, 2014, Administrative Law Judge (ALJ) Douglas Long directed the DWA to review the rate base, cost of capital, and operating expenses which support the 2014 base year rates, i.e., Sierra Park Water Company's (Water Company) proposed revenue requirement and rate design. The Ruling enumerated the following requests and questions of DWA:

1. Based on the review of the filing, provide a nominal dollar base-line revenue requirement which can be deflated to 2012 and 2013 dollars in order to compare to the rates charged by the Odd Fellows which are the subject of the outstanding complaint, C. 12-03-017.

2. Based on the filing, provide a 2014 and 2015 revenue requirement and rate design as if the Water Company had filed a conventional Class D water company advice letter rate case pursuant to the usual Commission practices.

3. Provide an explanation for any changes to the revenue requirement and rate design proposed by the applicants. For example, changes in rate base, capital expenditures, expense, cost of capital, etc.

4. In light of the proposed spin-off of the Odd Fellows Sierra Recreation Association (Recreation Association)'s water operations and other changes which led to the creation of the Water Company, what, if any, recommendations would the DWA propose with respect to applying the Commission's affiliate transaction rules to the Water Company, the Service Company, and Odd Fellows? This question is posed in light of the use of shared employees, the similar ownership structure, and any possible remaining links to Odd Fellows after the creation of the separate Water Company.

5. With respect to question 4, the Commission's Affiliate Transaction Rules for water utilities include reporting requirements and are generally perpetual requirements. Are there any reasonable modifications DWA would suggest to the rules or to limit the application of the rules to some transition period, for example, for three or five years?

This report provides the requested responses to Administrative Law Judge (ALJ) Long's Ruling.

This report is divided into the following sections: Section 1: Background. This section describes the water system, the relevant issues associated with the system, a consultant's report to evaluate the system and recommend a capital budget, Complaint

(C.) 12-03-017, Application (A.) 13-09-023) and divestiture of the water company and service company by the Recreation Association; Section 2: Revenue Requirements. In this section, the filings of the Recreation Association and the Water Company (Applicants) were reviewed and Summaries of Earnings were developed for Fiscal Years (FY) 2014/15 and 2015/16. Using the Summary of Earnings for 2014, the expenses were deflated to FY's 2011/12, 2012/13 and 2013/14. Based on this, the under/over-collections from lot owners for water services provided by Recreation Association were computed from the date of filing of C. 12-03-017; Section 3: Responses to ALJ requests. In this section, responses to ALJ requests were developed based on Staff analysis of the filings; Section 4: Recommendations. In this section, Staff recommendations are presented for questions raised by the ALJ, rate design, resolution of C. 12-03-017 and Affiliate transaction related issues.

1.1 Description of water system

The Recreation Association operated and maintained facilities serving a small development of mostly vacation homes near the community of Long Barn, California in the Sierra Nevada Mountains. The community is located off of State Highway 108 at an approximate elevation of 4600 ft. The water supply to the development is from two wells that pump groundwater into the distribution system and 6 storage tanks. The total pumping capacity of the wells is approximately 170 gallons per minute (gpm). The total storage is approximately 300,000 gallons. The well sizes and storage volumes have served the community adequately over the years.

From 1986 to January 2012, the Recreation Association provided water to the Odd Fellows Sierra Homeowners Association (OFSHA). The OFSHA in turn, provided water to the owners of the lots within the subdivision. The Recreation Association states that as a direct result of the failure of the OFSHA to pay it for the provision of water and certain other services from June 1, 2011 to May 31, 2012 (FY 2011), the Recreation Association ceased providing services to the OFSHA in January 2012.[1] From January 2012 to May 31, 2013, the Recreation Association provided water directly to owners of the lots within the subdivision. Since June 1, 2013, the water services are provided by Sierra Park Water Company (Water Company). [2]

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[1] Per A. 13-09-023, Exhibit N, the Recreation Association was issued Water Supply Permit (03-11-11P-002) by the California Department of Public Health on February 28, 2011 to supply water for domestic purposes to the Recreation Association.

[2] The Sierra Park Water Company was formed by the Recreation Association on March 25, 2013.

1.2 Consultant report

In 2012, the Recreation Association retained Domenichelli and Associates, Inc., a Civil Engineering firm (Consultant), to evaluate its water supply and distribution system to provide guidance to assure property owners within this development there would be a reliable supply of water well into the future. The purpose of the study was to gather information regarding the existing water system and make recommendations regarding establishment of water use rates. The revenues would be used for continued operations and maintenance of the water system, including the repair and replacement of existing facilities. The Consultant also developed a long term capital expenditure budgets over a 20 year horizon and issued a report on December 8, 2013.[3]

In its report, the Consultant noted that the water system is not metered and the Recreation Association has not indicated a desire to meter services at this time. Between the wells and tanks, maximum domestic demands are met as long as there are no major system failures. Firefighting capacity is sufficient to provide several hours of flow within an acceptable range.[4] Improvements to the wells and storage tanks will require repairs of the lining for the tanks and upgrades such as pump and motor replacements for the wells. Due to age of the wells (18 and 28 years respectively), the wells will require major rehabilitation within the next 20 years. The distribution system is through a pipe network with mostly 4-inch diameter pipes with some 2-inch lines. The pipes are 40 to 60 years old. Based on information provided to the Consultant by the Recreation Association, the Consultant recommended that 100% of the system should be replaced by 8 inch and 6 inch diameter pipes over the next 40 years. The Consultant noted that the estimates of required facilities were based on a limited knowledge of the type and condition of the existing pipe materials and current condition of the well equipment.[5] The estimated cost for replacement of pipes was about $1.8 million. The estimated cost of repairing the tanks and rehabilitating the wells was about $270,000. The total cost for these tasks is about $2 million. [6]

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[3] A. 13-09-023, Exhibit Q: Capital Expenditures Report, Odd Fellows Sierra Recreation Association, Inc., Long Barn, California. Report issued by Domenichelli and Associates, Inc., December 8, 2013.

[4] Id, pg. 3

[5] Id, pg. 5

[6] Id, pg. 6

The Consultant recommends the establishment of a 5% contingency reserve fund for unforeseen or emergency needs and for minor improvements unrelated to the major repair or replacement of water supply facilities. The reserves would also be used for compliance with future water quality related regulations, provisioning and installation of metered services, improvements to the maintenance shop or equipment, and as a contingency for a major failure of a portion of the system requiring costly repairs or replacement.

Based on the above, the Consultant developed a capital budget and recommended a 5 year fixed monthly user fee of $71.52 which included a 3% inflation factor or, a fee of $75 which included a 5% reserve. The fee should be revisited over time to review the reserve account balances and make any necessary adjustments.

1.3 Complaint 12-03-017

On March 14, 2012, four lot owners (Complainants) filed Complaint (C.) 12-03-017 against the Odd Fellows Recreation Association (Recreation Association). The Complainants allege that the Recreation Association should be regulated by the CPUC since it was providing water to lot owners. The rates charged for water service are excessive and need to be modified with excessive amounts refunded to ratepayers.

1.4 Application 13-09-023

The Recreation Association and the Sierra Park Water Company (Water Company) (Applicants) filed Application (A.) 13-09-023 on September 20, 2013 for a Certificate of Public Convenience and Necessity (CPCN) to operate a Public Water Company and Water System near Long Barn, to establish rates for service, and for the Water Company to issue stock. Applicants state that since June 1, 2013, the Water Company has been providing water to the lot owners within the subdivision under a conditional approval of the California Water Resources Control Board (Water Board) dated June 14, 2013[7] and pursuant to a temporary Operating Lease with OFSHA. In response to a Staff Data Request, Applicants state that they have not prepared or executed any written leases or easements for payments by the Water Company to the Recreation Association or to the Service Company. Such documents will be prepared and executed following the approval of the Application by the Commission.[8]

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[7] Formerly, California Department of Public Health

[8] Data Request RK001, Question 8.

1.5 Divestiture by the Recreation Association

In March 2012, the Recreation Association formed two "For Profit" Corporations called the Sierra Park Water Company (Water Company) and the Sierra Park Services, Inc. (Service Company or SPSC). The Recreation Association states that: [9]

> The Recreation Association intends to transfer all water lines, wells, pumps, water storage tanks and related improvements located within the Park or on the Timber Land (the Water Related Personal Property to be Transferred" to the Water Company…
>
> The Recreation Association will lease to the Water Company, the area of the Timber Land on which the water lines and water storage tanks that currently serve the Park are located. The Service Company will lease the right to extract water from the Real Property to be transferred (after transfer by the Recreation Association) to the Water Company. In addition, the Service Company will grant an easement to the Water Company over, under and through the area of the Real Property to the Water Company to be transferred which the water pipes, wells and related improvements that currently serve the park are located.

The Water Company will own, operate, maintain, repair and improve the water system, including the distribution system, upon conveyance of the same by the Recreation Association. At the same time, the Recreation Association will convey all real property to the Service Company within the subdivision except rights to water from Sugar Pine Creek and a lot that is owned by the Recreation Association. The Applicants also state that:[10]

> … the Recreation Association will lease to the Water Company certain real estate property owned by it outside of the boundary lines of the Park on which the water tanks connected to the water distribution system for the lot owners of the Park are located for $5,000 per year.

[9] "Corrected Status Report of the Odd Fellows Sierra Recreation Association", Case No. C.12-03-017, filed on April 15, 2013

[10] "Joint response of Applicants Odd Fellows Sierra Recreation Association and Sierra Park Water Company, Inc, to June 2, 2014 e-mail ruling of ALJ Douglas Long for additional data and analysis", A. 13-09-023, dated June 23, 2014

> The real property to be conveyed to the Service Company includes real property on which the water system is located. The Service Company plans to lease the real property within the perimeter of the subdivision on which the wells that provide water to lot owners of the Park are located for $3,250 per year per well. The Service Company will also lease to the Water Company certain real property to be conveyed by the Recreation Association to the Service Company within the boundary lines of the Park on which the pipes used to distribute water to the lot owners of the Park are located for $39,140 per year.

The lease amounts are effective June 1, 2013 and will be reviewed annually. The Applicants also state that in the event the CPUC is concerned that the lease payments are too high, the Service Company and the Water Company would be willing to negotiating a lower lease payment in return for a much greater amount for use of water from the wells.

Section 2 ***<u>Revenue Requirements</u>***

To determine the revenue requirements for water service, Staff reviewed the historical and projected financial information filed by the Recreation Association and the Water Company and supplemental information received through data requests. Staff requested updates to estimated information that was filed with A. 13-09-023.

In response to Staff's request, the Recreation Association states that:

> . . . the Odd Fellows Recreation Association was the sole provider of all community services, including water, during the FY 2012 and 2013 for which we are submitting this information. It was the last of more than 50 some odd all services were provided to all property owners as a package of services. In that style of operations, there was less accounting effort in sorting out what was needed for providing water separate from all other services such as garbage disposal, Pine needle disposal, and other services, including the shared efforts of a paid caretaker, part time help and contracted services. During this phase, each year all property owners had the opportunity to review, discuss and approve a budget at each annual meeting, either in person or by proxy. . . . From June 1, 2013 forward the water services have been under the jurisdiction of the Sierra

> Park Water Company, SPWC, while other services are under the jurisdiction of the Sierra Park Services Company, SPSC . . .[11]

The Recreation Association provided its financial report updated to May 31, 2013.[12] In the financial report, the auditors state that

> . . . the financial statements do not express an opinion or provide any assurances about whether the financial statements are in accordance with accounting principles generally accepted in the United States of America . . . The policy is to prepare the financial statements on the modified basis of each cash receipts and cash disbursements. Accordingly, the accompanying financial statements are not intended to present the financial position or results of operations in conformity with accounting principles generally accepted in the United States of America. . . . We are not independent with respect to Odd Fellows Sierra Recreation Association, Inc.[13]

The financial report did not segregate all water related income and expenses. Rather, it presented all information for the Recreation Association for all activities that were handled by the Recreation Association. The Recreation Association also stated that it did not segregate records for the water service offered. Due to this, Staff could not rely on the accuracy of the historical financial information presented by the Recreation Association. In addition to the financial statements, Staff reviewed the invoices that justified the expenses reported by the Recreation Association in A. 13-09-023. However, staff was unable to find sufficient explanations to justify many of the expenditures claimed.

Staff requested updated financial information from the Water Company but the Water Company did not comply with Staff's request.[14] Therefore, Staff used the Budget Reports that came from the Water Company's Board of Director Minutes for financial

[11] E-mail from Ronald Hawke to Ravi Kumra, dated July 18, 2014.

[12] Odd Fellows Sierra Recreation Association Inc., Compiled Financial Statements, May 31, 2013.

[13] Id, at page 1

[14] Data Request RKK001

information related with Water Company operations.[15] Since financial information was reported for 11 months ended April 30, 2014, it was extrapolated to May 31, 2014.[16] The extrapolated expenses are referred to as "actual expenses" in this report. The FY 2013 financials were then escalated to FY 2014 (base year), 2015 and 2016 by using inflation factors approved by DWA. To determine the revenue requirements to 2011 and 2012, Staff deflated the FY 2013 amounts to 2012 and 2011 using inflation factors approved by DWA.

2.1 Revenue Requirements proposed by Applicants

For FY 2013,[17] the Water Company reported a revenue requirement of $343,220. Included in that amount is $20,000 reserve for unanticipated expenses, a capital replacement program[18] and lease charges of $51,100 for access to water related assets to the Service Company and to the Recreation Association,[19] legal charges of $30,900 and communications related expenses of $3,499. See Table 1, Col. "d". In contrast, Actual Expenses were $241,788.[20] Those expenses included lower charges for purchased power, employee labor, [21] water testing, accounting, consulting, communications and general expenses. Replacement reserves were not included. However, lease payments were included. Staff could not verify the expenditures reported by the Water Company because no backup documentation was provided. See Table 1, Col. "e".

[15] Sierra Park Water Company Board of Directors Meeting Minutes for June 7, 2014.

[16] The Fiscal Year for the Recreation Association and Water Company is from June 1 through May 31 of the following year.

[17] The Water Company reports its financial information on a Fiscal Year (FY) basis. FY runs from June 1 through May 31 of the following year.

[18] Capital expenditures are for Waterline Replacement, Well Rehabilitation and Tank Repairs.

[19] Easement leases are comprised of: (1) 6 Miles pipe access: $39,600; (2) Ground and access to 2 wells: $6,500; and (3) Access to water towers: $5,000

[20] Actual expenses are computed by extrapolating 11 month expenses as of 4/30/2013 to 05/31/2013. Expenses are as reported in the Board of Director Minutes of June 7, 2014.

[21] Employee costs were lower because of reimbursements received from the Service Company for use of Water Company staff.

By contrast, the Consultant reported Water Company revenue requirements of $294,191, $303,016, $312,107, $321,470 and $331,114 respectively for FY's 2012, 2013, 2014, 2015 and 2016.[22] Projected figures included estimates for waterline replacement, well rehabilitation and tank repairs.[23] An inflation factor of 3% was applied to the FY 2013 amounts to compute estimates for future years.

2.2 Staff recommendations for Revenue Requirements

For Class C and D water utilities, net income is calculated using both the rate of return (ROR) on rate base and a rate of margin (ROM) method. The method that produces the higher net income is used. The ROR may be set at a level above or below the recommended range, if warranted. Where little or no rate base exists, the ROM is used. The ROM is applied to operating expenses to determine the estimated dollar return, which is then compared with the average dollar ROR on rate base.[24]

The Water Company has less than 500 connections. As such, it qualifies as a Class D Water Company. Staff determines that since the Water Company's rate base is minimal, the ROM will produce a higher return for the Water Company. The ROM for Class D water utilities is 21.69% for 2014 and is used for all Summary of Earnings computations.

For FY 2013, Staff recommends a revenue requirement of $187,678. For that computation, Staff removed lease payments, reduced legal-related and maintenance charges, and included a ROM of $33,452. For computing revenue requirement for 2014 (Base-line), the FY 2013 revenue requirement was escalated by Commission's recommended inflation factors for Compensation Per Year Per Hour and Estimates of Non-Labor and Wage Escalation Rates. [25] [26] Similarly, the Base-line revenue

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[22] Application Exhibit O

[23] Estimates for Repair and Replacements for 2013, 2014, 2015 and 2016 are: $100,805; $103,829; $106,944; and $110,152.

[24] "Rates of Return and Rates of Margin for Class C and Class D Water Utilities", Memo to the Commission, from Rami Kahlon, Director, Division of Water and Audits and Kayode Kajopaiye, Chief, Water Company Audit, Finance & Compliance Branch, Dated March 21, 2014.

[25] ORA June 2014 Summary of Compensation Per Hour, Memo from Energy Division dated June 28, 2014.

[26] Estimates of Non-labor and Wage Escalation rates for 2014 through 2018 from the June HIS Global Insight U.S Economic Outlook, Memo from Office of Ratepayer Advocates Water Branch, dated July 28, 2014.

requirement was escalated to derive the revenue requirement for FY 2015 which was then escalated for FY 2016 revenue requirement. Based on this analysis, staff recommends baseline revenue requirements of $189,426, $194,272 and $198,042 respectively for FY 2014, 2015 and 2016. Including funding for a special engineering study to evaluate the water system, the revenue requirements for FY 2014 and 2015 will be $204,426 and $219,272 respectively. See Table 1, cols. "I", "j", "k".

Table 1: Sierra Park Water Company
Summary of Earnings

			From Utility filings [1]			Projected by Water Company	Staff recommendation					
		Fiscal Year	2011	2012	2013	2013 [2]	2011	2012	2013	2014 (Baseline)	2015	2016
		a	b	c	d	e	f	g	h	i	j	k
I		**Operating Revenues**										
1		Flat Rates	$ 145,471	$ 177,580	$ 312,683	$ 241,788	$ 170,970	$ 181,989	$ 187,678	$ 189,426	$ 194,272	$ 198,042
2		Metered Rates			$ -				$ -			
3		Fire Protection										
4		Other			$ 3,167							
5		Total Operating Revenues	$ 145,471	$ 177,580	$ 315,850	$ 241,788	$ 170,970	$ 181,989	$ 187,678	$ 189,426	$ 194,272	$ 198,042
II		**Operating Expenses**										
6		Purchased Water			$ -				$ -			
7		Purchased Power	$ 14,708	$ 13,498	$ 16,000	$ 7,600	$ 7,230	$ 7,410	$ 7,600	$ 7,722	$ 7,891	$ 8,065
8		Other Volume Related Expenses										
9		Employee Labor	$ 37,472	$ 42,203	$ 53,869	$ 32,860	$ 31,250	$ 32,060	$ 32,860	$ 33,386	$ 34,120	$ 34,871
10		Materials	$ 1,504	$ 888	$ 11,301	$ -	$ 910	$ 1,504	$ -	$ -	$ -	$ -
11		Contract Work (Excluding Water Testing)										
12		Water testing			$ 8,240	$ 2,847	$ 2,750	$ 2,780	$ 2,850	$ 2,896	$ 2,959	$ 3,024
13		Transportation Expense										
14		Other Plant Maintenace Expense	$ 21,737	$ 41,339	$ 39,140	$ 44,550	$ 37,170	$ 38,100	$ 39,038	$ 39,625	$ 40,500	$ 40,500
15		Office Salaries										
16		Management Salaries										
17		Employee Pension and Benefits			$ 7,643	$ 11,500	$ 6,680	$ 6,850.00	$ 7,015	$ 7,127	$ 7,284.27	$ 7,517.37
18		Uncollectibles [3]					$ 850	$ 900	$ 945	$ 950	$ 965	$ 985
19		Office Service & Rentals										
20		Office Supplies & Expenses							$ 1,100	$ 1,200	$ 1,300	$ 1,300
21		Professional Services										
	a	Accounting			$ 16,173	$ 13,800	$ 13,125	$ 13,450	$ 13,800	$ 14,021	$ 14,329	$ 14,788
	b	Legal			$ 30,900	$ 37,800	$ 2,630	$ 2,700	$ 10,000	$ 6,000	$ 6,096	$ 6,291
	c	Consulting	$ 44,013	$ 44,013	$ 48,875	$ 8,028	$ 8,332	$ 8,540	$ 8,028	$ 8,156	$ 8,336	$ 8,603
22		Insurance	$ 23,967	$ 12,003	$ 21,270	$ 23,430	$ 22,279	$ 22,836	$ 23,430	$ 23,805	$ 24,329	$ 25,107
23		Regulatory Commission Exp.								$ 3,000	$ 3,500	$ 4,000
24		General Expenses	$ 2,069	$ 4,248	$ 9,999	$ 5,530	$ 2,000	$ 7,000	$ 1,200	$ 1,300	$ 1,400	$ 1,000
25		minus expenses capitalized		$ (3,585)		$ (4,882)						
26		Total Operating Expenses	$ 145,471	$ 154,607	$ 263,410	$ 183,064	$ 135,206	$ 144,131	$ 147,866	$ 149,188	$ 153,010	$ 156,052
III		**Deductions**										
27		Depreciation Expense										
28		Ad Valorem Taxes										
29		Payroll Tax			$ 4,496	$ 5,081	$ 2,950	$ 3,020	$ 3,100	$ 3,175	$ 3,280	$ 3,280
30		Taxes other than Income			$ 3,708	$ 2,460	$ 2,340	$ 2,400	$ 2,460	$ 2,500	$ 2,555	$ 2,611
31		States Income Taxes							$ 800	$ 800	$ 800	$ 800
32		Federal Income Tax										
33		Lease payments for easements			$ 51,100	$ 51,183	$ -	$ -	$ -	$ -	$ -	$ -
34		Reserves			$ 20,000							
35		Total Deductions	$ -	$ -	$ 79,304	$ 58,724	$ 5,290	$ 5,420	$ 6,360	$ 6,475	$ 6,635	$ 6,691
36		Total Deductions and Expenses	$ 145,471	$ 154,607	$ 342,714	$ 241,788	$ 140,496	$ 149,551	$ 154,226	$ 155,663	$ 159,645	$ 162,743
37		Net income before taxes										
IV		**Rate Base**										
38		Depreciation [4]		$ 22,973	$ 506							
39		Rate of Margin [5]			$ -		$ 30,474	$ 32,438	$ 33,452	$ 33,763	$ 34,627	$ 35,299
V		**Revenue requirement and assessments**										
40		**Base revenue requirement excluding special study**										
	a	Base Revenue requirement	$ 145,471	$ 177,580	$ 343,220	$ 241,788	$ 170,970	$ 181,989	$ 187,678	$ 189,426	$ 194,272	$ 198,042
	b	Revenue requirement/ Connection	$ 399.65	$ 487.86	$ 942.91	$ 664.25	$ 469.70	$ 499.97	$ 515.60	$ 520.40	$ 533.71	$ 544.07
	c	Revenue requirement/ Connection/Mo	$ 33.30	$ 40.65	$ 78.58	$ 55.35	$ 39.14	$ 41.66	$ 42.97	$ 43.37	$ 44.48	$ 45.34
41		**Revenue requirement for special study**										
	a	Engineering consulant Fee								$ 15,000	$ 25,000	$ -
	b	Revenue requirement/ Connection								$ 41.21	$ 68.68	
	c	Revenue requirement/ Connection/Mo								$ 3.43	$ 5.72	
42		**Revenue Requirement including special study**										
	a	Requirement including special study	$ 145,471	$ 177,580	$ 343,220	$ 241,788	$ 170,970	$ 181,989	$ 187,678	$ 204,426	$ 219,272	$ 198,042
	b	Revenue requirement/ Connection	$ 399.65	$ 487.86	$ 942.91	$ 664.25	$ 469.70	$ 499.97	$ 515.60	$ 561.61	$ 602.40	$ 544.07
	c	Revenue requirement/ Connection/Mo	$ 33.30	$ 40.65	$ 78.58	$ 55.35	$ 39.14	$ 41.66	$ 42.97	$ 46.80	$ 50.20	$ 45.34

Notes
1. A. 13-09-023, Ex. P
2. Sierra Park Water Company, Board of Directors Meeting Minutes, June 7, 2014. Amounts are extra-polated to 5/31/2014.
3. Assume approximately 1% of Operating Expenses as uncollectible expense
4. No Depreciation expenses for water related assets were reported
5. Rate of Margin of 21.69% applied to Operating expenses

2.3 Revenue Requirements for FY 2011 and 2012

For computing a revenue requirement for 2012, the revenue requirement for 2013 was deflated using Commission approved escalation factors for 2012. Similarly, the 2011 revenue requirement was derived by deflating the 2012 revenue requirement. Based on this, Staff has determined that the revenue requirements for FYs 2011 and 2012 are $170,970 and $181,989, respectively. See Table 1, cols "f" and "g".

Section 3: ***<u>Responses to ALJ's ruling</u>***

This section contains Staff's responses to ALJ Long's requests. Staff recommendations are presented in Section 4. .

Request # 1: Based on the review of the filing, provide a nominal dollar base-line revenue requirement which can be deflated to 2012 and 2013 dollars in order to compare to the rates charged by the Odd Fellows which are the subject of an outstanding complaint.

Revenue requirements

The base-line revenue requirement for 2014 is deflated to 2013 using inflation factors authorized by DWA. The inflation factors for 2012 are then applied to the deflated FY 2013 revenue requirement to calculate the 2012 revenue requirement. Similarly, for FY 2011, the inflation factors for 2011 are applied to the deflated FY 2012 revenue requirement. The revenue requirements for FY 2011, 2012, 2013 and 2014 are: $170,970; $181,989; $187,678; and $204,426.[27] To compute the revenue requirement per connection, divide the revenue requirement by 364. See Table 1 for details.

Computations for overcharges from complainants

To determine over/under charges from C. 12-03-017, Staff recommends the rates associated with the deflated revenue requirements for each lot should be compared with amounts charged complainants. The difference of the two will be the over/under charge associated with C. 12-03-017.

Using Staff recommended revenue requirements for FY's 2011, 2012, 2013 and 2014 divided by 364 connections, Staff determined the revenue requirement for each lot in the development. This was compared with the amounts collected from the complainants from the date of filing of C. 12-03-017. Based on this comparison, Staff has determined that lot owners were over-charged for water service. See Table 2 for details

<u>Table 2: Computation of extra amounts collected</u>

	Domecheli Report		*Asessment Amount*		*Assessment / Lot*	*Over/(Under) Collection/Lot*	*Total Over/Under Collection [1]*		
	w/o CIP	*w/CIP*	*Improved Lot*	*Unimproved Lot*	*per staff Recommendation (w/o special study)*	*Improved Lot*	*Unimproved Lot*	*Improved Lot (305 lots)*	*Unimproved Lot (59 lots)*
	a	*b*	*c*	*d*	*e*	*f=c-e*	*g=e-d*	*h=f*305*	*i=g*59*
6/1/2011-5/31/2012			$ 793	$ 793	$ 470	$ 323	$ 323	$ 24,651.88	$ 4,768.73
6/1/2012-5/31/2013	$ 522	$ 802	$ 825	$ 759	$ 500	$ 325	$ 259	$ 99,134.20	$ 15,282.78
6/1/2013-5/31/2014	$ 537	$ 826	$ 968	$ 890	$ 516	$ 452	$ 374	$ 137,982.60	$ 22,089.72
6/1/2014-5/31/2015	$ 553	$ 851	$ 997	$ 997	$ 520	$ 477	$ 477	$ 145,374.91	$ 28,119.34
6/1/2015-5/31/2016					$ 534				
							Sub-total	$ 407,144	$ 70,261
							Total	$ 477,404	

<u>Notes</u>

1. Extra amount is calculated for 3 months for FY 2011.

[27] Includes $15,000 for a special engineering study

Request # 2: Based on the filing, provide a 2014 and 2015 revenue requirement and rate design as if Water Company had filed a conventional Class D water company advice letter rate case pursuant to the usual Commission practices.

Revenue requirements for 2014 and 2015

Revenue requirements were computed for FY's 2014 and 2015 as if the Water Company had filed a conventional Class D water company advice letter. A discussed above, for each year, revenue requirement based on ROM method was higher than those computed based on Rate of Return method. Therefore, the ROM was used to compute the revenue requirement. The Revenue Requirements are summarized in Table 3 below.

Table 3: Staff Recommended Revenue Requirements

Period	*Asessment per lot*			*Revenue Requirement*	
	w/o special study	*special study*	*Total*	*w/o special study*	*with special study*
a	*b*	*c*	*d=b+c*	*e=b*364*	*f=d*364*
6/1/2011-5/31/2012	$ 469.70		$ 469.70	$ 170,970	$ 170,970
6/1/2012-5/31/2013	$ 499.97		$ 499.97	$ 181,989	$ 181,989
6/1/2013-5/31/2014	$ 515.60		$ 515.60	$ 187,678	$ 187,678
6/1/2014-5/31/2015	$ 520.40	$ 41.21	$ 561.61	$ 189,426	$ 204,426
6/1/2015-5/31/2016	$ 533.71	$ 68.68	$ 602.40	$ 194,272	$ 219,272

Request # 3: Provide an explanation for any changes to the revenue requirement and rate design proposed by the applicants. For example, changes in rate base, capital expenditures, expense, cost of capital, etc.

Changes in revenue requirements and rate design proposed by applicants

Applicants based their rate design on estimates that exceeded actual costs by a significant amount. Some items included: higher estimates for purchased power than shown historically; charging full-time employee wages, benefits and taxes for an employee who devoted only 61% of his time for Water Company related matters; charging higher than actual amounts for materials; charging higher than authorized amounts for water testing; charging higher than reasonable legal and consulting related expenses; charging higher than reasonable general expenses; charging for lease payments for easements to water related assets; and setting up a replacement reserve schedule without proper justification.

Revenue requirements and rate design proposed by Staff

In the revenue requirement and rate design proposed by Staff, Staff removes some of the excess charges and recommends adding recovery for net revenue based on a ROM method, and recommends inclusion of $40,000 to undertake a detailed study to determine an appropriate capital budget for the Water Company for required system improvements. The study is expected to be initiated in FY 2014 and completed in FY 2015. As a result, the annual per lot revenue requirements for FY 2014, 2015 and 2016 including funds for a special engineering study will be $561.61, $602.40 and $544.07 respectively.[28] It should be noted that the revenue requirement will go down in FY 2016 because funding for the special study will no longer be required. The funds collected for this study will be tracked in a special memorandum account and will be approved following reasonableness review by the Commission either as part of the next general rate case or a separate Tier 3 Advice Letter filing. See Table 1 for details.

Request # 4: In light of the proposed spin-off of Odd Fellows' water operations and other changes which led to the creation of the Water Company, what, if any, recommendations would DWA propose with respect to applying the Commission's Affiliate Transaction Rules to the Water Company, the Service Company, and Odd Fellows (Recreation Association)? This question is posed in light of the use of shared employees, the similar ownership structure, and any possible remaining links to Odd Fellows after the creation of the separate Water Company.

Affiliate transactions

The Commission Affiliate Transaction Rules (Rules) are contained in D.10-10-019. These rules are specifically meant for Class A and B water companies. Application of these Rules requires detailed reporting requirements which may be too onerous for the Water Company. Staff recognizes that sometimes it is difficult to hire outside experts by a small company. However, when it is necessary to use Water Company employees, Water Company must ensure that all affiliate related work is done after its own work has been completed, a proper tracking of time spent is maintained and approved at all times, the Water Company is fully compensated for all employee expenses (including but not limited to wages, benefits, applicable taxes and any ancillary costs like transportation) that are incurred by the Water Company.

Request # 5: With respect to Request #4, the Commission's Affiliate Transaction Rules for water utilities include reporting requirements and are generally perpetual requirements. Are there any reasonable modifications DWA would suggest to the Rules or to limit the application of the Rules to some transition period, for example, for three or five years?

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[28] The revenue requirements for FY 2014, 2015 and 2016 without the special study will be $520.40, $533.71 and $544.07, respectively.

Staff believes that Affiliate Transaction Rules should be adhered to at all times and compliance with the Rules should be reported by the Water Company in each General Rate Case (GRC).

Section 4: ***<u>Staff Recommendations</u>***

In this section, Staff makes recommendations based on its evaluation of A. 13-09-023 and C. 12-03-017. In Section 4.1, recommendations based on responses to ALJ Long's requests are presented. In Section 4.2, additional staff recommendations are discussed.

4.1 Recommendations for ALJ questions

1. Request 1: Refund of excess amounts collected

(i) The Recreation Association should refund, with interest at a rate established by the ALJ, the excess amounts collected from March 2012 through May 31, 2013 as shown in Table 2. Refunds to be made over a period of 2 years to all lot owners in 4 semi-annual installments.

(ii) The Water Company should refund the excess amounts collected, with interest at a rate established by the ALJ, from June 1, 2013 through May 31, 2014 as shown in Table 2. Refunds to be made via a credit against the regular assessment to all lot owners in 4 semi-annual installments.

(iii) The Water Company should refund all over-collected amounts from June 1, 2014 to the date of adoption of rates by the Commission per schedule of rates shown in Table 2.

(iv) The Water Company should immediately reduce the annual amount assessed for each connection from $997 to $520 per year for FY 2014.

2. Request 2: Per Lot assessments for FY 2015 and 2016

(i) The Water Company should modify the lot assessments to $533.71 and $ 544.07 for FY 2015 and 2016 as shown in Table 1.

(ii) A special assessment of $41.21 and $68.68 per lot should be added for the special study for FY 2014 and 2015 respectively as shown in Table 3.

3. Request 3: Changes in revenue requirements proposed by Applicants and Staff

(i) Applicant should provide justification of amounts disallowed by Staff if it wants to include the disallowed amounts in rates.

4. Requests 4 and 5: Affiliate transactions

(i) All affiliated companies must adopt formal affiliate transaction rules.

(ii) Any Board members who are also members of the affiliates should recuse themselves from making any decisions regarding use of Water Company resources.

(iii) Water Company should make available its staff only after staff has completed their obligation to the Water Company.

(iv) Water Company should maintain detailed auditable records when its staff is used by any affiliate.

(v) Water Company should be promptly reimbursed fair market value for services performed by its staff or equipment used for affiliates. For example, for labor expenses, Water Company must charge a fully loaded rate that includes the employee salary, benefits, taxes, transportation and ancillary expenses.

(vi) All Affiliate Transaction Rules should be adhered to at all times and compliance with the Rules should be reported by the Water Company in each GRC.

4.2 Additional staff recommendations

1. Evaluate capital expenditure needs of Water Company

The Water Company has not justified capital expenditures based on a comprehensive engineering evaluation of the existing water distribution system, well rehabilitation and tank replacement. There are also issues raised regarding the exact location of distribution pipes in the subdivision. Staff recommends that the Water Company should work with DWA staff to hire an engineering consultant to:

a. Survey and determine the exact location of distribution system in its area of service.

b. Evaluate the condition of the existing distribution system, the wells and the water tanks.

c. Develop a schedule for converting the existing unmetered water connections to metered connections.

2. Establish replacement timelines and replacement reserves

Based on the engineering consultant's report, the Water Company should establish a time line and replacement reserves for capital expenditures needed for Water Company operations going forward.

3. Establish a memorandum account to track engineering study costs

The Water Company may collect $15,000 ($41.20 per lot) and $25,000 ($68.68 per lot) during FY 2014 and 2015, respectively, subject to refund for the special study discussed above. The Water Company should establish a memorandum account to track costs associated with the special study and may seek Commission approval of these costs and offsetting revenues collected in its next GRC or through a separate Tier 3 Advice Letter filing.

4. Remove charges for access to water properties

Water Company should consider condemnation and eminent domain proceedings to seek access to all water properties without payment of any easement leases to the Recreation Association or the Service Company.

5. Transfer water rights to water company

Given the age of the two wells which serve as the primary source of water, it is important to have a reliable backup source of water supply in case one or both wells are out of service. Sugar Pine Creek serves as a backup water source for the Water Company. Not making that source readily available when needed places the Water Company in a vulnerable position. It is recommended that the water rights to Sugar Pine Creek should be transferred to the Water Company at no cost.

Appendix A: Review of expenses for Water Company

Expenses requested in A.13-09-023 and recommended by DWA are shown in Table 1. The following are staff comments on expenses for the Water Company.

1. Operating expenses

1.1 Administration and Fees

For purposes of computing rates, the Water Company budgeted FY 2013 operating expenses of $263,410. Compared with this, the expenses for 12 months based on actual 11 month expenses were $183,064. Staff recommends an amount of $147,860, $149,188; $153,010; and $156,010 for FY 2013, 2014, 2015 and 2016. Details are discussed below.

Insurance

Water Company's budgeted and actual insurance premiums are $21,270 and $23,430, respectively, for FY 2013. The annual insurance premium for year ended May 31, 2013 (FY 2012) for the Recreation Association was $15,213 for water services as well as other services required by the Recreation Association. FY 2013 insurance expenses represent an increase of 54% over what the Recreation Association paid in FY 2012 for all activities including those related with provisioning of water services.

Staff recommends adoption of the current insurance premiums but encourages the Water Company to review its insurance needs and investigate competitive bids to reduce the insurance costs.

Employee Expenses

The Water Company's budgeted and actual employee expenses for FY 2013 were $57,019[29] and $70,450,[30] respectively.

The Water Company has one full time employee while the Service Company and the Recreation Association have none. The Water Company employee performs tasks for the three entities on an as needed basis. For this, the water company is reimbursed actual employee expenses by the Service Company. During FY 2013, the Water

[29] Comprised of $44,960 payroll, $7,563 benefits and $4,496 payroll taxes. See Table 1, col "d".

[30] Comprised of $53, 869 payroll, $11,500 benefits and $5,081 payroll taxes. See Table 1, col. "e".

Company was reimbursed $24,106 by the Service Company (SPS) for this employee. This is 39% of projected 12 month employee expense. Based on this, the Water Company employee devoted 61% of his time on Water Company related business.

Staff recommends that $42,975 (61% of $70,450) should be charged to Water Company for this employee inclusive of wages, benefits and payroll taxes. For future years, this amount is increased based on escalated compensation recommended by DWA.

Accounting

The Water Company's budgeted and actual accounting expenses are $16,173 and $13,800 respectively for FY 2013. Staff recommends that accounting expenses of $13,800 are reasonable. For future years, this amount is increased based on escalated compensation recommended by the DWA.

Credit Card Charges

The Water Company's budgeted and actual expenses are $1,500 and $2,069 respectively for FY 2013. Staff recommends that these expenses should be disallowed as no justification for these charges are provided.

Legal Consulting

The Water Company's budgeted and actual legal costs are $30,900 and $37,800, respectively, for FY 2013. The Water Company provided redacted copies of legal bills which cannot be used to determine appropriateness of the claimed expenses.

In response to Staff data request, the Water Company indicates that it expects ongoing legal expenses of $2,992 for FY 2013 and similar costs in FY 2014. The Water Company also expects legal fees for collection and possibly compliance matters. The total budgeted amount for legal fees is $28,500. This does not include legal fees for Complaint Case C. 12-03-017 or A.13-09-023 as such fees should be non-recurring.

Staff recommends legal fees of $10,000, $6,000, $6,096 and $6,291 for FY's 2013, 2014, 2015 and 2016 for ongoing water company related and compliance related matters.

Uncollectible Expenses

The Water Company did not request an allowance for uncollectible expenses. Staff recommends that approximately 1% of total revenue requirements (base revenue requirement plus special assessment for the engineering study) should be added to Revenue requirements for uncollectible expenses.

Professional Consulting

The Water Company's budgeted and actual Professional consulting costs are $48,875 and $8,028 respectively for FY 2013. A review of invoices submitted by the Water Company indicates that most of the expenses associated with this item were incurred for surveying and other related matters. Staff recommends that $8,028, $8,156, $8,336 and $8,603 for FY's 2013, 2014, 2015 and 2016 are appropriate for this item.

Taxes and Licenses

The Water Company's budgeted and actual expenses for taxes and licenses are $3,708 and $2,460, respectively, for FY 2013. Staff finds $2,460 as reasonable.

Member Communications

The Water Company's budgeted and actual expenses for member communications are $3,499 and $2,131, respectively, for FY 2013. Budgeted amount for FY 2014 is $2195. The amounts were spent for printing and mailing newsletters to park residents. Staff believes that $1,000 is sufficient to keep members abreast of developments in the water system. The Water Company is encouraged to make extensive use of the internet, bill inserts and its regular Board meetings to communicate developments in the Water Company to its membership.

Water Administration Consulting

The Water Company budgeted $36,000 for Water Administration consulting. Actual amount reported was $20,040.[31] Staff recommends $16,100 [32] and $16,200 [33] for FY 2013 and 2014, respectively.

Maintain Water System

The Water Company's budgeted and actual costs are $39,140 and $44,550 plus a capital expenditure of $4,882 for FY 2013. The capital expenditure was unbudgeted and no justification was provided for this cost. Staff recommends $39,038, $39,625 and

[31] Comprised of $1,187 for supplies and $18,853 for outside services.

[32] Comprised of $1,100 for supplies and $15,000 for outside services.

[33] Comprised of $1,200 for supplies and $15,000 for outside services

$40,500 should be used for FY 2013, 2014 and 2015 for maintenance of the water system.

Water Testing

The Water Company's budgeted and actual expenses for water testing are $8,240 and $2,847, respectively, for FY 2013. Staff recommends $2,850, $2,896 and $2,950 respectively for FY 2013, 2014 and 2015.

Purchased Power

The Water Company's budgeted and actual expenses for purchase power are $16,000 and $7,600, respectively, for FY 2013. Staff recommends $7,600, 7,722, $7,891 and $8,065 for FY 2013, 2014, 2015 and 2016.

Water Tank Check Valve

Water Company budgeted $9,000 for a Water Tank Check Valve. The Water Company did not perform this repair. Staff recommends this amount should be removed for FY 2013, 2014 and FY 2015 budgets pending a recommendation resulting from the engineering study described above.

Other Expenses

Easement leases

The water company paid $500 for easement to 6 miles of pipes. Budgeted amount was $39,600. In addition, the Water Company paid $50,683 for easement leases for two wells, six water tanks and access to the same. The budgeted amount for this was $39, 140. Since the pipes, grounds, wells and tanks all belong to the OFRA, there is no reason for the Water Company to pay easement lease payments to access its distribution system. In any case, the Water Company can use its right to condemn the properties and take over all access under eminent domain.

As a backup to its water supply, the Water Company would purchase water from Sugar Pine Creek for which the Recreation Association is retaining water rights. This arrangement places the Water Company in a vulnerable position with regard to a backup water supply. Staff recommends that, to ensure viability of the water system in the future, the Recreation Association should transfer necessary water rights for Sugar Pine Creek to the Water Company.

Reserves

Water Company proposes a reserve of $20,000 for unanticipated water system costs. This should be rejected as no justification was provided for this reserve account.

Funds for special study

Staff recommends that for FY 2014 the Water Company should budget $15,000 for an engineering study to survey and evaluate the existing water distribution system, installation of meters in the development and recommend a capital expenditure plan. For FY 2015, Staff recommends $25,000 for detailed design for implementation of the projects. The special study should be funded by a special per lot assessment of $41.21[34] and $68.68[35] for FY 2014 and 2015. This amount should be billed as a separate line item from base rates established for each lot in the development. The costs and revenues for this study should be tracked in a special memorandum account subject to refund. The Water Company may claim reimbursement of these expenses through a Tier 3 Advice Letter after completion of the study. The Water Company can then request Commission review of engineering study's recommendations during its next GRC.

(END OF ATTACHMENT)

[34] $15,000/364 lots = $41.21 (approximately.)

[35] $25,000 / 364 lots = $68.68 approximately)