



TOWN OF APPLE VALLEY

TOWN COUNCIL STAFF REPORT

To: Honorable Mayor and Town Council **Date:** April 22, 2014
From: Frank Robinson, Town Manager **Item No:** 5
Town Manager's Office
Subject: PRESENTATION REGARDING THE APPLICATION OF APPLE VALLEY RANCHOS WATER COMPANY TO INCREASE WATER RATES

T.M. Approval: _____ **Budgeted Item:** Yes No N/A

RECOMMENDED ACTION

This is an informational item only. The purpose is to inform the Town Council and residents about Apple Valley Ranchos Water Company's application to increase water rates.

DISCUSSION

On January 2, 2014, Apple Valley Ranchos Water Company ("AVR") filed its application for a General Rate Increase with the California Public Utilities Commission ("Commission"). AVR is a Class A Public Utility Water Company that is regulated by the Commission and provides water service in the Town of Apple Valley ("Apple Valley"). It is a wholly owned subsidiary of Park Water Company, a California corporation that is wholly owned by an arm of the multinational financial asset management firm, The Carlyle Group.

In its application, AVR requests a revenue increase of \$3,127,463 or 14.88% for 2015. AVR has not requested specific rates for subsequent escalation years; however, it anticipates requesting increases of \$2,056,455 or 8.48% for 2016, and \$2,160,731 or 8.19% for 2017.

AVR's application indicates that it will file advice letters setting out its calculations and supporting analysis for the escalation year rates forty-five days prior to the first day of each escalation year. If AVR's application is granted, AVR estimates that the requested increase will produce a rate of return on equity of 9.79% and a return on AVR's estimated rate base for 2015 of 9.07%. AVR asserts that the requested rate increase is necessary because present rates are insufficient to produce enough revenue to yield to

AVR a reasonable return on capital invested and to be invested in plant, property and other equipment devoted to providing utility service.

AVR states that the proposed rates are increased over those presently in effect for the following reasons:

1. Low present rate revenues due to a decrease in estimates of consumption per customer compared to those adopted in the prior General Rate Case.
2. Additional revenues to produce a fair rate of return on capital invested in property dedicated to providing utility service.
3. Increase in unit cost of production.
4. Inflationary increases anticipated during 2014 and the Test Year.

Projected water sales for the period 2015 to 2017 are significantly below the projected water sales used to develop the current 2014 rates. The majority of the proposed increase for 2015 is requested because current rates, when applied to the lower projected sales for 2015, generate revenues that fall below the Commission-authorized 2014 revenue. Consequently, the percentage increase in rates necessary to generate the requested 2015 revenues is significantly higher than what would have resulted if sales forecasts had remained at 2014 levels. By way of example, the average annual residential water usage assumed for 2014 for current rates was 233 hundred cubic feet (Ccf) per year and the projected annual usage for 2015 is 199 Ccf per year, or a 14.59% decrease.

In terms of average residential customer bill impacts, AVR presents the following estimates:

**Rate Impact on Average Residential Customer's Bi-Monthly Bill
(assuming AVR's proposed rate increase is approved)**

<u>Year</u>	<u>Current Bill</u>	<u>Increase</u>	<u>New Bill</u>	<u>% Increase</u>
2015	\$130.15	\$17.95	\$148.10	13.79%
2016	\$148.10	\$11.74	\$159.84	7.93%
2017	\$158.84	\$12.13	\$171.97	7.59%

As set out in this table, the average residential customer's bill will increase from a current level of \$130.15 to a projected 2017 level of \$171.97, approximately 32% higher than the current level. These calculations do not include surcharges.

In terms of the requested revenue rate increases by customer class, AVR presents the following table:

**Requested Revenue Rate Increase for AVR in Years 2015-2017
(Dollars in Thousands)**

<u>Customer Class</u>	<u>2015 Increase</u>		<u>2016 Increase</u>		<u>2017 Increase</u>	
Residential	\$2,250.5	15.18%	1,522.3	8.93%	1,593.8	8.59%
Business	\$463.0	13.62%	308.1	7.92%	321.1	7.60%
Industrial	\$0.7	14.04%	.5	7.92%	.5	7.60%
Public Authority	\$158.9	16.28%	90.6	7.91%	94.6	7.59%
Private Fire Service	\$52.1	14.92%	38.2	8.98%	42.6	8.66%
Public Authority Irrigation	\$4.4	12.41%	3.1	7.93%	3.3	7.61%
Irrigation Pressure	\$162.6	15.94%	96.3	7.92%	102.5	7.59%
Irrigation Gravity	\$22.5	11.45%	1.0	0.44%	2.5	1.12%
Temporary Construction	\$5.7	9.81%	5.0	7.94%	5.2	7.62%
Apple Valley Golf Course	\$20.6	18.40%	10.5	7.91%	10.9	7.58%
Total Water Revenues	\$3,140.9	14.97%	2,075.6	8.58%	2,176.9	8.26%

As reflected in the table above, all customer classes will be required to contribute significantly more revenue at the rates proposed by AVR's application.

In terms of system improvements, AVR describes a number of main replacement projects in its Main Replacement Program and it has budgeted \$4,985,153 in 2014, \$5,791,591 in 2015, and \$6,007,083 in 2016 for this purpose. AVR's capital budget for 2014 includes, among other things, \$2,300,000 for a new 1.5 million gallon Bell Mountain Storage Tank, and its capital budget for 2015 includes \$2,353,892 for a new 1.5 million gallon Stoddard Storage Tank.

The Office of Ratepayer Advocates (ORA) has intervened in AVR's General Rate Case and it is protesting the following issues:

1. Proposed adjustment to AVR's sales forecasting methodology.
2. Proposed treatment of balancing accounts
3. The appropriate historical averaging periods used for developing forecasts of expenses.
4. The reasonableness of forecasted pension, Benefit and medical costs.
5. The reasonableness of AVR's request for increases in administrative and general expenses.
6. Proposed increases in payroll and related expenses.
7. Proposed increases to General Office expenses.
8. Proposal to implement a Sales Reconciliation Mechanism.
9. Proposed depreciation rates.
10. Proposed modification to the Water Revenue Adjustment Mechanism/Modified Cost Balancing Account to include gravity irrigation customers.

11. Proposed modifications to revenue lag calculations used to determine Working Cash Allowance.
12. Proposal to change residential rate design.
13. Proposal to increase Low-Income Assistance Program service charge.
14. Proposed capital improvement projects.

The Town of Apple Valley has also intervened in the process to protect its own and its residents' interests. The Town of Apple Valley's motion for party status was granted by the assigned Administrative Law Judge ("ALJ") and the Town echoed the concerns of ORA.

In terms of timing, the parties to the proceeding are awaiting a final ruling from the assigned ALJ, but it is anticipated that important events will occur on or about the following dates:

- **April 30, 2014** – Two Public Participation Hearings will take place at the Town of Apple Valley Town Center (1:00 p.m. and 6:00 p.m.). AVR customers will have the opportunity to present comments to the assigned ALJ regarding AVR's proposed rate increase.
- **May 9, 2014** – ORA and the Town will serve testimony on AVR regarding the application.
- June 16-20, 2014 – Hearings
- October 8, 2014 – ALJ's Proposed Decision will be mailed to parties.
- November 20, 2014 – The Proposed Decision will go to the full Commission for consideration and approval.

Town staff will continue to keep the Town Council and the residents informed as this case develops.

FISCAL IMPACT

None. This is an informational item only.

ATTACHMENTS

None. A presentation will be given at the Town Council meeting, a copy of this presentation will be made available on demand following the meeting.