

Exhibit F



Cost of Capital

**Direct Testimony of Thomas F. Smegal
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March 2017

Table of Contents

I.	INTRODUCTION	1
II.	QUALIFICATIONS	1
III.	CAPITAL STRUCTURE	4
IV.	CREDIT DOWNGRADE RISK	15
V.	CONTINUING WRAM/MCBA BALANCES.....	17
VI.	CAPITAL INVESTMENT PROGRAM.....	19
VII.	WATER COST OF CAPITAL MECHANISM	21

1 **I. INTRODUCTION**

2 **Q. What is the purpose of your testimony in this proceeding?**

3 A. I am testifying in support of California Water Service Company's ("Cal
4 Water") requested capital structure and projected average cost of debt, integral
5 parts of the overall cost of capital. I am also testifying about certain factors that
6 I believe the Commission should consider as additional risks in determining the
7 cost of equity applicable to Cal Water in this proceeding. I am not seeking
8 additional return adjustments for these additional risks at this time, but point
9 them out to fully inform the Commission of the operating, financial, and
10 regulatory risks facing Cal Water.

11

12 **II. QUALIFICATIONS**

13 **Q. What are your qualifications for this testimony?**

14 A. I am Vice President and Chief Financial Officer of Cal Water. In that role, I
15 have responsibility for debt and equity financing, maintaining and monitoring
16 operating budgets, SEC financial reporting, and investor relations. I was
17 appointed to the position in October 2012. Since my appointment, it has been
18 my responsibility to monitor and manage the company's capital structure. In
19 2013, as part of these responsibilities, I led a secondary stock offering for the

1 California Water Service Group (“CWSG”). In 2015, I led a private placement
2 debt offering for California Water Service Company (“Cal Water”). I lead CWSG’s
3 cash management and financing strategies and am therefore the most
4 appropriate person at the company to testify on these subjects.

5

6 **Q. What is your educational background?**

7 A. I received a Bachelor of Science degree in Civil Engineering and a Bachelor
8 of Arts Degree in History from Stanford University in 1990. I completed two
9 years of graduate study focusing on water resources management at the
10 University of California at Berkeley’s Energy and Resources Group.

11

12 **Q. Do you hold any professional certifications?**

13 A. I am a licensed Civil Engineer in the State of California.

14

15 **Q. Please summarize your business experience.**

16 A. After graduating from Stanford University in 1990, I worked for the
17 California Public Utilities Commission (“Commission”) until 1997. During that
18 time I worked for the Water Division and the Commission Advisory and
19 Compliance Division, mainly processing rate case requests for small Class B, C,
20 and D water utilities. Since joining Cal Water’s Rates Department in May 1997 as

1 a regulatory analyst, I was promoted to Manager of Rates in 2001, was later
2 promoted to Vice President of Regulatory Matters in 2008, and was promoted to
3 Chief Financial Officer in 2013. I have testified on numerous occasions before the
4 Commission.

5

6 **Q. Can you summarize Cal Water's request in this proceeding?**

7 A. Cal Water is seeking a return on common equity of 10.75%, with a cost of
8 debt of 5.51%, a 53.4% equity capital structure, and an overall weighted return
9 of 8.31%. As described by Dr. Michael Vilbert, Cal Water's financial modeling
10 witness, the recommended return on equity is necessary to maintain access to
11 capital. Dr. Vilbert's Return on Equity calculations are based in part on Cal
12 Water's proposed capital structure. I describe below the need to maintain a
13 capital structure similar to that last adopted by the Commission. I also describe
14 Cal Water's proposed regulatory treatment of the Water Cost of Capital
15 Adjustment Mechanism ("WCCM"). In his Direct Testimony, Mr. Paul Townsley
16 describes Cal Water's requested treatment of any revenue requirement increase
17 which might be incurred as a result of this application. According to Cal Water's
18 calculations, the requested rate of return on capital necessary to ensure

1 continued availability of capital would increase revenue requirements in Cal
2 Water's Class A ratemaking districts by between 0.76% and 3.6%.¹

3

4 **Q. Are you sponsoring any informational exhibits in this testimony?**

5 A. Yes, I am responsible for Cal Water's financial statements and other data
6 which are included as a separate Exhibit A, and Exhibit I in compliance with
7 either the Commission's rules of practice and procedure or the minimum data
8 requirements established in D.07-05-062.

9

10 **III. CAPITAL STRUCTURE**

11 **Q. What capital structure is Cal Water requesting?**

12 A. Cal Water is requesting a return on Common Equity of 10.75% for the
13 period from January 1, 2018 through December 31, 2020 covered in these
14 proceedings. Cal Water is providing workpapers and testimony to support this
15 request. Cal Water projects maintaining its capital structure of 53.4% equity and
16 46.6% debt, which is the previously Commission-approved capital structure.²

17

¹ Cal Water also has a Class D ratemaking district, Grand Oaks (near Cal Water's Antelope Valley systems).

² D.12-07-009 at 2.

1 **Q. Please explain why Cal Water is proposing to adopt this capital**
2 **structure.**

3 A. A capital structure of 53.4% equity and 46.6% debt has allowed the
4 Company to maintain an A+ (stable) corporate rating from Standard & Poor’s
5 (“S&P”). Achieving and maintaining this rating from S&P allows the Company
6 access to lower cost debt, with the benefits of this lower cost of debt flowing to
7 the ratepayer. If the Commission were to force Cal Water’s future financing to a
8 greater proportion of debt, this may have the unintended consequence of
9 increasing the cost of that debt. A company’s leverage is a key criterion within
10 the credit rating process of S&P, and as such, higher percentages of debt
11 financing would be expected to negatively impact a firm’s rating.

12
13 **Q. What is the company’s current and forecasted capital structure through**
14 **2020?**

15 A. Cal Water is forecasting the year-end capital structure for each year in
16 Table 1 below:

17 **Table 1**

	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>
Common Equity	55.2%	48.6%	53.8%	56.0%
Long-Term Debt	44.8%	51.4%	46.2%	44.0%

18

1 **Q. What does the company anticipate its capital structure will be for the**
2 **test year 2018?**

3 A. Cal Water anticipates for this application a \$200 million debt offering in
4 October 2018 to “clean out” its line of credit, and in anticipation of the 2019
5 expiration of \$100 million in first mortgage bonds. Thus since there is an
6 expected change in capital ratio during the year, I forecast the 2018 capital
7 structure using a quarterly weighting. I forecast quarterly structures, and then
8 for the year, used an average of the quarterly percentages within the year as
9 reflected in Table 2 below.

10 **Table 2**

	<u>As of</u> <u>3/31/18</u>	<u>As of</u> <u>6/30/18</u>	<u>As of</u> <u>9/30/18</u>	<u>As of</u> <u>12/31/18</u>
Common Equity	\$615M	\$619M	\$637M	\$639M
Long-Term Debt	\$495M	\$493M	\$493M	\$690M
Total Capital	\$1,110M	\$1,112M	\$1,130M	\$1,328
Equity %	55.4%	55.6%	56.3%	48.1%
Debt %	44.6%	44.4%	43.7%	51.9%
Average Equity For Year	53.8%			
Average Debt For Year	46.2%			

11
12 The figures reflect the large 2018 debt offering in the fourth quarter of
13 2018 and resulted in an average structure in 2018 of 53.8% equity and 46.2%
14 debt. As the calculated amount is very near Cal Water’s currently authorized
15 capital structure, the company requests the same structure adopted in D.12-07-
16 009.

1

2 **Q. How would the capital structure look as a result of the proposed 2018**
3 **borrowing in 2019 and beyond?**

4 A. After the estimated \$200 million debt offering in 2018, Cal Water will
5 retire a \$100 million series of ten-year first mortgage bonds in late 2019. As can
6 be seen in the Table 1 above, this change, plus the anticipated accrual of
7 retained earnings, brings the capitalization ratio back above the requested
8 53.4% equity by the end of 2019.

9

10 **Q. How would changing the capital structure to a higher debt ratio impact**
11 **the Company?**

12 A. As a greater percentage of a company's capital structure is comprised of
13 debt, the firm's equity investors, as residual claimants, are burdened with
14 greater financial risk. As stated by Dr. Michael Vilbert in his testimony on behalf
15 of Cal Water, "the higher the percentage of debt the greater the financial risk
16 imposed upon the equity investors and the higher will be the required ROE."³

17 Stockholders, or equity investors, face a risk in their investment, from a
18 firm's operations. This business risk comes from uncertainty in projections of
19 future operating income. Financial risk comes from using debt to fund

³ Appendix E, Direct Testimony of Michael J. Vilbert, page 1, lines 13-14.

1 operations. The use of debt for financial leverage adds a financial risk layer to
 2 the business risk that equity investors already face. The business risk inherent in
 3 projections of future income is not reduced by leveraging more financial risk, but
 4 rather the business risk is increased for the equity investor through the
 5 amplification effects of leverage. Using more debt increases a firm's financial
 6 risk and magnifies the inherent business risks to the equity holder. The
 7 compounded effect of a higher debt ratio results in an even higher level of risk
 8 for equity investors. The higher compounded business and financial risk
 9 requires higher return on equity that is commensurate to the risk in order to
 10 attract investors.

11

12 **Q. What have been the recorded capital ratios during the last three years**
 13 **and what has been the effect in terms of Cal Water's ability to finance debt?**

14 A. From 2014 through 2016, the Company had a capital structure as follows:

15

Table 3

	2014	2015	2016
Secured Long-Term Debt*	40.5%	45.2%	46.0%
Other Long-Term Debt	1.6%	1.3%	1.2%
Total Long-Term Debt	42.1%	46.5%	47.2%
Common Equity	57.9%	53.5%	52.9%

* Calculated as First Mortgage Bonds less Unamortized Debt Premium and Expense

16

17 While the company has tried to maintain its capital structure at the
 adopted ratios, there are unavoidable variances resulting from the timing and

1 size of financing activities and the amount of retained earnings on an annual
2 basis. Larger offerings of debt or equity allow the company to reduce costs for
3 ratepayers through the realization of economies of scale in transactional costs
4 (fees paid to investment banking firms and outside counsel). Cal Water's last
5 three debt financing offerings were \$150 million in 2015, \$100 million in 2010,
6 and \$100 million in 2009. CWSG's last equity offering in 2013 was over \$100
7 million. These sizes of offering also attract better pricing as many institutional
8 investors have minimum investment size policies. Thus Cal Water (for debt) and
9 CWSG (for equity) continue to use lines of credit and other cash management to
10 allow for greater competition among investors. As long as they are considered
11 by the investment community as transitory events with the expectation that Cal
12 Water is targeting the approved capital structure, these fluctuations within the
13 capital structure do not create negative ramifications for the company's credit
14 rating or its cost of capital.

15

16 **Q. Has the company taken actions, other than the issuance of large debt**
17 **tranches referenced above, to reduce the cost of debt financing?**

18 A. Yes. Most recently, the company used a broad Request for Proposal
19 ("RFP") process to select the method of its 2015 debt issuance and select a
20 banking partner. As a result of that process, Cal Water used a private placement

1 because, for the size contemplated, it gave the lowest transaction cost along
2 with a broad market of buyers to ensure a low coupon rate.

3

4 **Q. How did you forecast debt costs?**

5 A. Forecast debt costs are a weighted average of principal balances as of
6 12/31/2018 for all existing debt, plus the cost of an anticipated 2018 debt
7 issuance of \$200 million. Cal Water's existing first mortgage bonds have "make
8 whole" provisions, meaning if they are redeemed prior to the due date, Cal
9 Water would have to pay future interest to the due date. Therefore, I have not
10 contemplated early refinancing of any existing Cal Water debt. The rates consist
11 of the bonds' coupon rate, plus any unamortized issuance costs. The forecast
12 2018 debt offering of \$200M has an assumed coupon rate of 4.85% and a cost of
13 issuance of \$1.15M.

14 For Cal Water, the resulting weighted average cost of debt forecast as of
15 year-end 2018 is 5.51%

16

17 **Q. How does Cal Water forecast its incremental cost of borrowing in 2018?**

18 A. Cal Water forecasts the coupon rate as a spread over a forecast Treasury
19 rate and estimates the cost of issuance as a percentage of the issuance amount.

20

1 **Q. How did you estimate spread to treasury?**

2 A. The spread was estimated using recently reported spreads for investment
3 grade utility debt offerings over Treasury rates, per the Wells Fargo Securities,
4 U.S. Utility & Power Debt Capital Markets Weekly Market Update. These
5 reported spreads were confirmed against the company's most recent issuances
6 for reasonableness. We determined that a spread over the forecast Treasury
7 rate of 100 basis points was appropriate.

8

9 **Q. What is your source for treasury forecast at the time of issuance in**
10 **2018?**

11 A. Cal Water used the Philadelphia Federal Reserve Bank's Survey of
12 Professional Forecasters, which reports an expected average rate of 3.86% on
13 the 10 year Treasury over the next ten years. This rate was published on
14 February 10, 2017 and can be found at:
15 [https://www.philadelphiafed.org/research-and-data/real-time-center/survey-of-](https://www.philadelphiafed.org/research-and-data/real-time-center/survey-of-professional-forecasters/2017/survq117)
16 [professional-forecasters/2017/survq117](https://www.philadelphiafed.org/research-and-data/real-time-center/survey-of-professional-forecasters/2017/survq117).

17

18 **Q. How did you develop the effective tenor?**

19 A. The expected tenor of the forecast 2018 debt offering was assumed to
20 approximate the money weighted average tenor of the company's 2015 first

1 mortgage bond placements which, for the four bond series placed, had an
2 average tenor of 24 years. Cal Water has recently tried to avoid placing single,
3 large bond series with 'bullet maturities' in order to avoid building a single, large
4 debt maturity in any one year, as will unfortunately happen in 2019. Cal Water
5 prefers to place multiple bond series with staggered maturities, thereby avoiding
6 the risk of having an extremely large debt maturity in a single year.

7

8 **Q. How do you estimate the cost of issuance for the 2018 debt?**

9 A. Cost of issuance was forecast as a percentage of the expected amount to
10 be raised. Specifically, the cost of issuance was assumed to represent 0.6% of
11 the \$200 million forecast debt offering, or \$1.15 million. The cost of issuance as
12 a percentage of the amount raised would be slightly lower than the cost realized
13 with the 2015 first mortgage bonds placed. As the forecast 2018 bond offering is
14 anticipated to be slightly larger, it is assumed that some financing efficiencies
15 will be realized.

16

17 **Q. What guidance has the Commission offered on debt/equity structures**
18 **for water utilities, and what structures have most recently been adopted for**
19 **them?**

1 A. In May 2013, Decision 13-05-027, adopted the following capital
2 structures.

	Debt	Preferred Stock	Equity
Park/Apple Valley/Ranchos Water Companies	43.0%		57.0%
San Gabriel Water Company	37.0%		63.0%
Suburban Water Systems	37.0%	3.0%	60.0%
Great Oaks Water Company	30.0%		70.0%

3

4 The Commission has in the past recognized that equity investors bear
5 significant risk:

6 Generally, long-term debt is the least expensive form of capital but
7 the utility must ensure that it timely meets every interest payment
8 and maintains any required terms or conditions of the loan
9 agreements or mortgage indentures, and that it can refinance or
10 refund the debt when it matures. Preferred stock is generally
11 more expensive than debt and may or may not have a maturity or
12 refund provision. Interest may usually be deferred but it then
13 accumulates and takes preference over payment of dividends to
14 common equity owners. Thus, equity owners assume more risk
15 than either debt holders or preferred stock owners, including the
16 risk of losing their entire investment, and therefore equity
17 investors require the highest return over the long run.⁴

18

19 The Commission has also acknowledged that the financial risk that utilities
20 face is determined in part by the debt and equity ratio. Because of the
21 significant risk borne to equity investors, adopting a sufficient and fair equity
22 ratio is critical “to maintain reasonable credit ratings and to attract capital

⁴ D.10-10-035 at 19.

1 without incurring unnecessary costs for an excessive amount of expensive
2 equity.”⁵

3

4 **Q. Would ratepayers benefit from a deviation in the proposed capital
5 structure?**

6 A. Not necessarily. While a short-term calculation would lead to a
7 conclusion that revenue requirement is reduced through a lower equity ratio, in
8 the long-term the ratepayer may not be better off. As the percentage of debt
9 used within the capital structure is increased in an attempt to take advantage of
10 lower-cost financing, it is counterbalanced by increases within the required
11 return on equity and the cost of debt for incremental debt offerings in the
12 future. It may be counterproductive to modify the existing capital structure in
13 favor of more debt. Such efforts potentially make it more difficult for Cal Water
14 to raise future financing, thereby placing Cal Water’s capital investment program
15 in jeopardy and raising the cost to ratepayers.

16

⁵ *Id.*

1 **IV. CREDIT DOWNGRADE RISK**

2 **Q. Does Cal Water face a risk of a credit downgrade From Standard and**
3 **Poors (“S&P”)?**

4 A. Yes, Cal Water faces a real and quantifiable risk of a credit downgrade
5 from S&P. In the summary of S&P’s latest credit grading of Cal Water, S&P made
6 the following statement:

7 We could lower the ratings on Cal Water over the next 24 months
8 if the financial risk for the company increases, such that funds from
9 operations (FFO) to debt weakens to a level that is consistently
10 lower than 15%. This could occur if the company experiences
11 adverse regulatory outcomes that inhibit it from generating close
12 to its authorized return on equity.⁶

13
14 Furthermore, S&P calculates Cal Water’s FFO/debt for 2016 at 17.2% in
15 the report. This FFO/debt ratio can be affected by cash flow issues, such as a
16 continued or increasing receivable balance in the Water Revenue Adjustment
17 Mechanism/Modified Cost Balancing Account (“WRAM/MCBA”)⁷ decoupling
18 account, or it can be affected by taking on more debt. Cal Water previously had
19 this issue in 2011 through 2013, as its FFO/debt ratio slipped below 15% due to

⁶ March 31, 2017, Standard and Poor’s credit research summary of California Water Service Company (emphasis added).

⁷ The WRAM/MCBA was implemented to decouple water sales from the company’s recovery of fixed costs.

1 the 2009 and 2010 bond issuances and the growing receivable balance in the
2 WRAM/MCBA decoupling balancing account.

3

4 **Q. Please explain the FFO to debt ratio that S&P references.**

5 A. Funds from Operations (“FFO”) are a financial metric used by investors to
6 understand a company’s cash flow. FFO is typically calculated by taking a
7 company’s annual earnings, then adding annual amortization and depreciation.
8 There are also other adjustments in this calculation, including working cash,
9 deferred taxes, and non-cash components. In order to calculate the FFO to debt
10 ratio the company’s FFO is divided by its long-term debt. S&P publishes this
11 ratio quarterly.

12

13 **Q. How does the FFO get affected by delays in WRAM recovery?**

14 A. On a monthly basis, Cal Water compares adopted quantity revenue to
15 actual quantity revenue. Where actual quantity revenue is lower than adopted,
16 a credit is booked under Generally Accepted Accounting Principles (“GAAP”) on a
17 monthly basis to the WRAM ledger. Where actual quantity revenue is lower
18 than adopted revenue, a debit is booked to the WRAM ledger. The MCBA also
19 compares adopted production expenses to actual production expenses and
20 books a monthly entry. Cal Water has filed annually for recovery of under-

1 collected revenue or return of over-collected revenue. At the end of 2016, Cal
2 Water had an accumulated net balance of under-collected revenue of \$37
3 million. This uncollected balance resulted in a reduction in cash flow from
4 operations and thus reduces the FFO to debt ratio.

5

6 **V. CONTINUING WRAM/MCBA BALANCES**

7 **Q. What was Cal Water’s net receivable balance in the WRAM/MCBA**
8 **decoupling account at the end of 2010, and at the end of 2016?**

9 A. At the end of 2010, the receivable balance was \$28 million. At the end of
10 2016, the balance was \$37.3 million. In the intervening years, the WRAM
11 balance has been as high as \$51 million, but the receivable was brought down
12 significantly by drought “over-budget” surcharges paid by customer in 2015 and
13 2016.

14

15 **Q. Besides the FFO issue, what is the significance of this continuing WRAM**
16 **balance?**

17 A. Ultimately, as it relates to financial health, the WRAM issue comes down
18 to investor trust in Cal Water’s ability to earn its authorized rate of return on
19 equity. Because the WRAM receivable deducts from cash available to fund other
20 operations and capital, Cal Water isn’t as capital-efficient as others in the

1 industry nationwide. Naturally, this increases the cost of capital for Cal Water
2 compared to non-decoupled peers.

3 While the conservation rates implemented in 2008 are providing the
4 appropriate pricing signals to customers to reduce water usage, the
5 effectiveness of the corresponding regulatory mechanism – the WRAM/MCBA
6 mechanism – which was intended to offset the risks to the company posed by
7 those conservation rates, is insufficient. In part, this has been due to the decline
8 in water sales from 2008 to present that continues to be difficult to forecast.
9 The balances have remained as large receivables also due to factors surrounding
10 the Commission procedures for recovering them from ratepayers. These include
11 a 10% cap on the WRAM surcharges that can be recovered each year, and the
12 fact that the WRAM surcharge calculation itself is based on previously-
13 forecasted volumetric sales. As the anticipated sales fail to materialize due to
14 ever-increasing conservation, WRAM surcharge revenues come up short as well.

15

16 **Q. Hasn't the Commission corrected some of these factors in D.16-12-026,**
17 **its recent decision in the Balanced Rates OII?**

18 A. Yes, however most of those changes will not go into effect for Cal Water
19 until 2020, well after the cost of capital is set in this case. The Commission will
20 allow companies to move back to a rate design that targets recovery of at least

1 40% of revenues through the service charge, rather than the previous target of
2 30%. The Commission will also allow broader Sales Reconciliation Mechanisms
3 and a wider range of sales forecasts in expectation that future sales can be
4 forecast more effectively. Because each of these mechanisms can only be
5 implemented for Cal Water through a general rate case, the earliest they can go
6 into effect is January 1, 2020, the first test year of Cal Water's 2018 GRC. In
7 addition, the Commission declined to remove the 10% cap on WRAM surcharges,
8 continuing the delay in WRAM revenues collection that, in some districts, may
9 only be resolved through a special condition request in a GRC (the approval of
10 which still could not take effect until 2020).

11

12 **VI. CAPITAL INVESTMENT PROGRAM**

13 **Q. Are you responsible for financing Cal Water's capital investment**
14 **program?**

15 A. Yes.

16

17 **Q. Does Cal Water have significant infrastructure needs in the covered**
18 **period 2018-2020?**

19 A. Yes, Cal Water is operating with a Commission-approved capital program
20 of \$659 million of plant in service additions from 2016 through 2018, including

1 advice letters. This compares to \$447 million authorized in rate base for the
2 2013-2015 period.

3 While no general rate case covers the period beyond 2018, Cal Water has
4 good reason to expect continuing capital expenditures in that range in future
5 rate cases.

6 The bulk of Cal Water's approved budget are replacement-cycle
7 investments in mains, services, motors, control equipment, and other water
8 distribution facilities. Cal Water expects to make similar requests for
9 replacement cycle items in its 2018 general rate case and must also begin, at
10 some point, to address the replacement of groundwater wells in California. As
11 described in Mr. Tim Treloar's testimony, wells lose capacity over time and must
12 be rehabilitated (or replaced). The average age of Cal Water's wells is now over
13 forty years.

14

15 **Q. What are the major capital needs identified in Cal Water's Water Supply**
16 **& Facility Master Plans for the next 20-25 years?**

17 A. Most of the infrastructure in Cal Water's systems was constructed in the
18 post-World War Two period, meaning that much of the infrastructure is now 50-
19 60 years old. Our primary concern for infrastructure of this age is the condition
20 of wells, supply facilities, and pipelines. There is also a continuing need to invest

1 in water treatment facilities in order to continue to meet current and future
2 drinking water quality standards.

3

4 **Q. Does the amount of needed capital contribute to the need for a**
5 **competitive rate of return?**

6 A. Yes, Cal Water's increased Commission-approved capital budgets mean
7 that the company will need large amounts of additional financing in the next few
8 years. It is important that the Commission allow a reasonable return that will
9 allow Cal Water to compete in the marketplace for debt and equity investors.

10

11 **VII. WATER COST OF CAPITAL MECHANISM**

12 **Q. What is Cal Water proposing for the Water Cost of Capital Mechanism?**

13 A. The RCP directed companies to include in their 2008 cost of capital
14 applications a proposal for adjusting the authorized cost of capital between cost
15 of capital applications.⁸ In D.09-07-051, the Commission approved a settlement
16 agreement among the parties in A.08-05-002 (including Cal Water and DRA) that
17 proposed a Water Cost of Capital Mechanism ("WCCM") to adjust the base year
18 2009 return on common equity to reflect any significant changes in interest rates

⁸ D.07-05-062 at 15.

1 that may occur in 2010 and 2011.⁹ The settlement stated:

2 While this settlement does not bind the Commission
3 in future proceedings, the Parties agree that a similar
4 adjustment to the cost of capital should be made
5 following the adoption of a base year cost of capital
6 in subsequent cost of capital proceedings for CWS,
7 California American, and Golden State. In those
8 future cases, the Parties envision the Commission
9 setting a base year cost of capital and adopting a
10 similar adjustment mechanism that would be
11 recalibrated to reflect the new cost of capital.¹⁰

12
13 In D.12-07-009, the Commission adopted a settlement continuing the
14 WCCM. The adopted base year return on equity for 2012 (9.99%) was therefore
15 subject to possible adjustment in 2013 and 2014 using the new benchmark
16 period of October 1, 2010 through September 30, 2011.¹¹ The WCCM was
17 triggered in 2012, lowering Cal Water's rate of return from 8.24% to 7.94% due
18 to a 56 basis point decrease in the return on equity to 9.43%.¹²

19
20 **Q. What is your request with regard to the WCCM?**

21 **A.** Cal Water proposes to retain the WCCM for years 2019 and 2020, using
22 the base year 2018 that will be adopted in this proceeding, with a new

⁹ D.09-07-051 at Ordering Paragraph 1.

¹⁰ D.09-07-051, Attachment A (Settlement Agreement) at 3-4 (emphasis added).

¹¹ D.12-07-009 at 13.

¹² Cal Water Advice Letter 2088 (filed October 15, 2012).

1 benchmark period of October 1, 2016 through September 30, 2017.

2

3 **Q. Does this conclude your direct prepared testimony?**

4 A. Yes, it does.