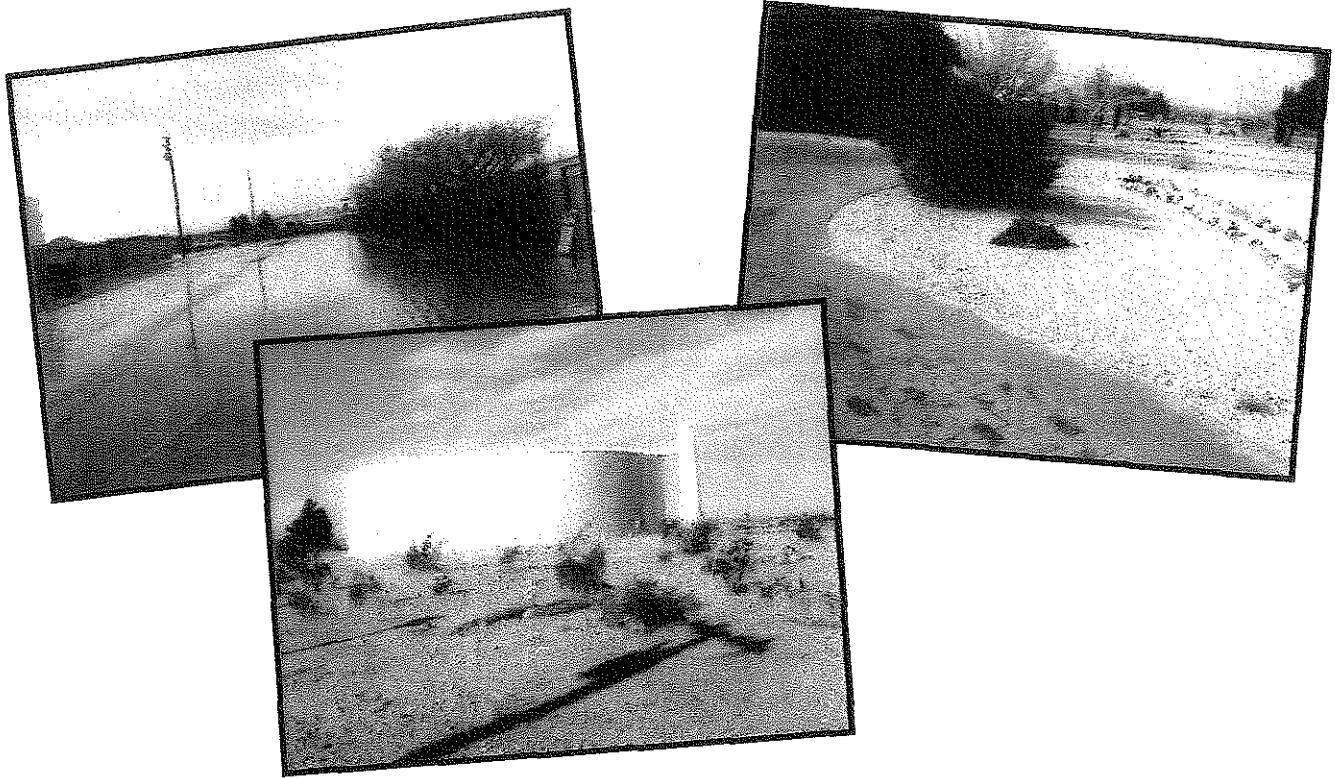

Blue Ribbon Water Committee Report

Town of Apple Valley's Best Opportunity for Affordable Water and Economic Sustainability



Local Flooding - New Water Infrastructure - Low Impact Development Design (LID)

December 12, 2011

Carl Coleman, PE, Chairman

Tel: 760-242-9900

Email: alteceng@aol.com

Part
1

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Blue Ribbon Water Committee Report

Town of Apple Valley's

Best Opportunity for Affordable Water and Economic Sustainability

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Addenda

Addendum No.

- 1 Bartle Wells Associates: Update of Feasibility Analysis of Acquisition of Apple Valley Ranchos Water System**
July 2011 (55 pages)
- 2 CPUC: Resolution W-4655**
September 15, 2011 (54 pages)
- 3 BRWC/Town of Apple Valley – Proposed CPUC Stipulations**
Oct. 20, 2011 (4 pages)
- 4 Carlyle/Park Water Co. - Opposing BRWC/Town Proposed Stipulations**
Oct. 24-2011 (7 pages)
- 5 Montana (Missoula) PUC Stipulations**
Oct. 28, 2011 (8 pages)
- 6 ALJ Long Proposed Approval of Carlyle Merger**
Nov. 1, 2011 (25 pages)
- 7 Town of Apple Valley – Opposition to Approval of Carlyle Merger**
Nov. 21, 2011 (9 pages)
- 8 CPUC Decision Approval of Carlyle Merger**
Dec. 1, 2011 (26 pages)
- 9 CPUC Administrative Law Judge's Ruling Granting Interim Rates**
Nov. 21, 2011 (3 pages)
- 10 Finance Committee Report
(Financial Analysis of Cost to Purchase AVR)**
Nov. 28, 2011 (94 pages)

Blue Ribbon Water Committee Report

Town of Apple Valley's

Best Opportunity for Affordable Water and Economic Sustainability

The Apple Valley Town Council appointed fifteen citizens to a Blue Ribbon Water Committee (BRWC) on March 30, 2011 to seek advice and assistance regarding critical water issues based on the BRWC members' collective expertise, water planning research experience, conservation and flood control issues, various reporting experience, and public service experiences. These are the three difficult tasks evaluated by the BRWC:

1) Carlyle Acquisition of Park Water Company

- To seek the advice of the BRWC in making decisions regarding the proposed acquisition of Park Water Company by the Carlyle Group (California Public Utilities Commission (CPUC) Proceeding No. 11-01-019).
- To review Bartle Wells Associates: Update of Feasibility Analysis of Acquisition of Apple Valley Ranchos Water System

2) AVR Rate Increase Requests - Does the BRWC recommend any actions in response to the request of Apple Valley Ranchos Water Company (AVR) to the California Public Utilities Commission (CPUC) for a rate increase? (CPUC Proceeding No. 11-01-001.)

3) Feasibility of Town-Owned Water Company - To evaluate all feasible alternatives regarding potential public ownership of the Apple Valley Ranchos Water Company, reported as California's largest privately-owned water company and Golden State Water Company, parent company is American States Water Company, the largest investor-owned water utility in the United States, both presently selling water to the citizens of the Town of Apple Valley.

NOTE: The Bartle Wells Associates, "Update of the Feasibility Analysis of Acquisition of the Apple Valley Ranchos Water System" (Bartle Wells Report) was forwarded in July 2011. The BRWC reviewed the report and provided a list of additional questions regarding that Report in connection with the preparation of this BRWC Report. However in late August, the Town informed the BRWC no additional information was going to be provided. Therefore, the BRWC Report was completed based on the information and financial numbers available or believed to be ascertainable, by the BRWC at that point in time. It also bears noting that this Report has now been revised numerous times in response to new information sources: Settlement Agreement issues pending before the CPUC, Carlyle Merger Application as well as other information regarding the CPUC proceedings mentioned above. Therefore, an Addendum was included in the BRWC Report to provide a concise and continuous analysis of updated information sources, as they have become available, in-lieu of making continuous adjustments to the entire BRWC Report. The BRWC makes this note to emphasize the dynamic and fluid situation presented here, and to confirm that the BRWC Report includes the Committee's recommendations only as of the date listed, December 12, 2011.

Part
3

Members

Blue Ribbon Water Committee Report

Town of Apple Valley's

Best Opportunity for Affordable Water and Economic Sustainability

The Council of the Town of Apple Valley appointed fifteen members to the Blue Ribbon Water Committee. Each of the five Town Council Members appointed two members to the Water Committee, and the Council selected the remaining five Blue Ribbon Water Committee members from written applications. All those selected were required to be residents of the Town of Apple Valley.

Committee Members

Appointers'

Carl Coleman, Chairman [AltecEng@aol.com]

Appointed at Large

Rick Piercy, Vice-Chairman [rpiercy@LCER.org]

Mayor Scott Nassif

Ron Barbieri, [rjbarbieri@earthlink.net]
Chair's Finance Committee

Mayor Nassif

John Bernier [johnpeepa1@aol.com]

Mayor Pro Tem Barb Stanton

Jim Chandler [n427c@gte.net]

Mayor Pro Tem Stanton

David Christman [dpentax@aol.com]

Appointed At Large

Jack Collingsworth [jack@bigappleautomotive.com]

Appointed At Large

Lawrence McCarthy

Council Member Rick Roelle

Bill McDaniel [bill@lomac.com]

Council Member Curt Emick

Bernadette McNulty, [bernadettecmcnulty@verizon.net]
Chair's Water Rights Committee

Council Member Roelle

Pat Orr, [pat_orrav@hotmail.com]
Chair's Public Information Committee

Council Member Emick

Wilson So, [wilsonso@saeinc.org]
Chair's Public vs. Private Ownership Committee

Council Member Ginger Coleman

Robert Lee Sturges [risturges@gmail.com]

Appointed At Large

Joseph Tartaglini [jptartaglini@aol.com]

Appointed At Large

Rob Turner [rtavca@aol.com]

Council Member Coleman

Blue Ribbon Water Committee Report

Town of Apple Valley's

Best Opportunity for Affordable Water and Economic Sustainability

As members of the Blue Ribbon Water Committee studied the voluminous documentation the Town of Apple Valley provided, it also gathered information from additional sources by reviewing numerous current and historical Mojave Water Agency Reports and the 2010 Urban Water Management Plan for the Apple Valley Ranchos Water Company. The BRWC held public meetings with community stakeholders and other interested individuals. The BRWC consulted experts in water delivery, water reclamation, ground water resources, flood control and stormwater management, water rights, eminent domain and public financing. Finally, the BRWC critically examined the financial information available and the resources needed to purchase and manage the water delivery systems now operating in Apple Valley. Quickly the BRWC began to have a better understanding of the integrated water management issues and challenges necessary to provide sustainable water supplies to Apple Valley residents for the foreseeable future and decades beyond.

Water Resources Stake Holders

There are various government entities and water purveyors engaged in the Town's water resource management that must be integrated into any sustainable future plans:

- Mojave Water Agency (MWA)
- MWA Technical Advisory Committee (MWA-TAC)
- Victor Valley Wastewater Reclamation Authority (VWRA)
- Two Privately Held Water Companies:
 - Apple Valley Ranchos Water Company (AVR)
 - Golden State Water Company (GSWC)
- Eleven Non-Privately Held Water Purveyors Serving the Town of Apple Valley
- California Public Utilities Commission (CPUC)
- San Bernardino County (SBCo)
- Town of Apple Valley (TAV)
- Town of Apple Valley Redevelopment Agency (AVRDA)
[to the extent the AVRDA remains involved consistent with recent and subsequent Legislative changes and Judicial Decisions to redevelopment agency laws]

Without affordable water, the Town will not have a sustainable economy. All citizens and taxpayers of the Town of Apple Valley are united in a water quandary that challenges the Town's elected representatives, community stakeholders and citizens, to find the best solutions that keep essential water supplies affordable and available to benefit everyone.

These include additional stakeholder groups, but not limited to the following:

- Residential Users of All Ages and Economic Circumstances
- Apple Valley Unified School District and other Schools
- Apple Valley Fire Protection District (Fire Protection Services)
- Hospitals
- Parks and Recreation
- Apple Valley Habitat Conservation Plan
- Existing Businesses, Industry, Job Providers and Workers
- Future Businesses, Industry, Job Providers and Workers
- Owners of Developed and Undeveloped Real Estate
- Agriculture including Food Production for Local Use
- Ranchers and Equestrians
- Real Estate Developers (large, medium, national, regional, local and small)
- Non-Profit Organizations
- Churches, Synagogues', Temples and other inclusive Places of Worship
- Other Regional Governmental entities
 - Lahontan Regional Water Quality Control Board
 - Mojave Desert Air Quality Management District
 - Southern California Association of Governments
 - Regional Transportation Plans
- Various Federal and State Governmental Regulatory Entities
- Non-Governmental Organizations
- Public Private Partnerships
- Other

Blue Ribbon Water Committee Report

Town of Apple Valley's

Best Opportunity for Affordable Water and Economic Sustainability

The Blue Ribbon Water Committee appointed four committees to study specific issues due to the voluminous amounts of documentation that required intense study and analysis.

Committee members engaged in discussions with CPUC staff members, various employees of Apple Valley Ranchos Water Company and Park Water Company, Mojave Water Agency staff and public testimony at various public meetings and with community stakeholders and other interested individuals.

Water Rights Committee

Chair, Bernadette McNulty
Carl Coleman
Bill McDaniel
John Bernier
Jack Collingsworth

Finance Committee**

Chair, Dr. Ron Barbieri
Joe Tartaglini
Lawrence McCarthy
Rob Turner
Carl Coleman

Public vs. Private Ownership Committee

Chair, Wilson So
Robert Sturges
Jim Chandler
Carl Coleman

Public Information Committee***

Chair, Pat Orr
Bill McDaniel
David Christman
Rick Piercy

****NOTE:** The Abstract of the Finance Committee Report is included in this section only. The Financial Analysis Report is shown in its entirety in Addendum 10 due to its length.

This Abstract delineates the various financial concerns and appurtenant issues and challenges of the financial impacts to the Town of Apple Valley, the Town's citizens; both in current financial terms and conservatively reasonable estimates of near future anticipated financial impacts.


****NOTE:** The Public Information Committee released public information in the local Daily Press and prepared the presentation to the Town Council.



Water Rights Committee

Water rights that serve the political boundaries of the Town of Apple Valley are not contiguous with the rate base of customers served by Apple Valley Ranchos Water Company (AVR), Golden State Water Company (GSWC) and some other smaller water companies. Therefore, the Water Rights Committee must consider the water rights within the larger Alto Basin, which does include the Town of Apple Valley and its sphere of influence.

Within the Apple Valley portion of the Alto Basin, there are 27,129-acre feet of water rights, which can serve the Town of Apple Valley. This includes 13,233-acre feet of water rights that were awarded by adjudication to Apple Valley Ranchos Water Company. AVR did not have to buy these water rights. They were free, so that should not add to the cost of water for customers. These 13,233-acre feet of water rights have been generally represented to the California Public Utilities Commission as being dedicated to the public use. Therefore, the owner of AVR cannot *readily* transfer or market these water rights. If Carlyle acquires AVR, the BRWC wants assurance that these water rights will not be traded on the open water market and will remain for public use of AVR customers in the Town of Apple Valley.



The Water Rights Committee has identified 8,240± acre-feet of water rights adjudicated on Apple Valley land that have been sold since 1997 to the cities of Adelanto, Hesperia and Victorville and to other out-of-state speculators (e.g. Aqua Capital Management). As a result, these water rights are no longer available to the Town of Apple Valley and are now traded as commodities in the for-profit water market. An "Implementation Plan" that keeps Apple Valley's historical water rights in Apple Valley needs to start immediately.

AVR owns the infrastructure that delivers water to its customers. Most of that infrastructure is not connected to the pipeline infrastructure of other water companies that serve Apple Valley. AVR has 13,233 acre feet of adjudicated water rights, which the Mojave Basin Water Master can (and has) ramped down 40 *per cent* due to drought and overdraft of aquifers in the past. To make up the water shortfall, AVR has the option to purchase additional water rights or annually lease water rights or purchase replacement water from the Mojave Water Agency. Since 2004, AVR has purchased a total of only 308-acre feet of water rights.

The Water Rights Committee has been scrutinizing Alto Basin water rights that serve the Town of Apple Valley and its economic interests. This committee has consulted with Mojave Water Agency representatives on numerous occasions and has received voluminous written reports from them, which the Water Rights Committee has studied. The committee has determined the owners of 27,129-acre feet of water rights that were developed through historical usage by water purveyors, farmers, recreational facilities and other Apple Valley landowners, which still own those water rights.

Water Rights Committee

The Water Rights Committee recommends that the Town of Apple Valley purchase the water rights delineated in the following chart (and any other available water rights) for the benefit of the AVR ratepayers and the Town's citizens:

Recommended Purchases of Water Rights within Alto Basin – Apple Valley Area

<u>Owner</u>	<u>Acre Feet (AF)</u>
American States Water Company	1,000
Apple Valley Country Club	709
Apple Valley Ranchos Water Company	13,233
Bastianon Revocable Trust	77
Newton Bass Trust	514
Beinscroth Family Trust	729
A.J. Beinscroth.	100
M. Cramer Irrevocable Trust	280
Dexter Family Trust	9
Golden State Water Company	940
Hamilton Family Trust	108
Hodge, Stanley	67
Hrubik, Thomas A	27
Jess Ranch Water Company	7,230
Mariana Ranchos Community Water District	245
Navajo Mutual Water Company	88
Thompson Living Trust, James & Bula	418
Thompson Living Trust, RL & RA	13
Thunderbird Water Company	118
Wagner Family Trust	<u>1,224</u>
TOTAL Water Rights within Alto Basin of Interest to Town	27,129

*Less Apple Valley Golf Course Purchased by Town in 2011 - 709

**Less Original Water Rights Adjudicated to AVR at No Cost - 13,233

***Less Original Water Rights Adjudicated to GSWC at No Cost - 940

BALANCE of Water Rights Recommended for Purchase 12,247 AC-FT

Water Rights Committee

Since 1997, more than 8,000-acre feet of water rights, adjudicated on Apple Valley land, have been sold to the cities of Adelanto, Hesperia, and Victorville, and to out-of-state speculators (e.g., Aqua Capital Management). As a result, these traded water rights are no longer available to the Town and are commodities on the for-profit water market. The following chart delineates the \$12,162,145 of water rights sold and transferred out of the Apple Valley area. In 1997, 1 acre-foot of water sold for an average of \$944. Five years later, in 2002, the price of 1 acre-foot of water sold for an average of \$1,296 (a 37% increase). In 2007, 1 acre-foot of water sold for an average price of \$3,330 (a 157% increase in 5 years). By 2010, the price of 1 acre-foot of water increased 23% in 3 years to an average of \$4,100.

The Water Rights Committee believes this is a long-term severe detrimental financial impact to the AVR ratepayers and a detriment to the Town's citizens. Furthermore, the Town of Apple Valley needs to do whatever is in its legal power to prevent this siphoning of water rights from continuing. To preserve the long-term economic viability of the Town of Apple Valley, the BRWC concludes that water must be both affordable and readily available to provide a sustainable future.

RECOMMENDATION: The Council needs to implement a plan immediately that keeps Apple Valley's historical water rights in the Town and its sphere of influence.

Water Rights Sold and Transferred out – Apple Valley Area

WATER RIGHTS Previously Purchased and Transferred out of Apple Valley				
From	To	Acre-Feet	\$/Ac-Ft	Price
Tom Hrubik	City of Adelanto	1,866	920	\$1,716,720
Tom Hrubik	Western Water Co.	280	1,000	\$280,000
J.P. Dexter	Radco Resources, LLC	500	1,000	\$500,000
R.G. Harris Co.	Radco Resources, LLC	280	0	\$0
1997 Totals		2,926	944	2,496,720
1998 Totals		0	0	\$0
Kenneth Clark	Western Water Company	59	1,300	\$76,700
Tom Hrubik	Victor Valley Water District	475		\$0
Penix Properties	Victor Valley Water District	652		\$0
Allen Taylor	Victor Valley Water District	456		\$0
Beinscroth Trust	Victor Valley Water District	100		\$0
1999 Totals		1,742	1,300	\$76,700
Apple Valley Development	Victor Valley Water District	100	1,125	\$112,500

WATER RIGHTS Previously Purchased and Transferred out of Apple Valley

Candlewood Properties	Victor Valley Water District	107	1,125	\$120,375
H.P. Development	Victor Valley Water District	480	1,125	\$540,000
Ton Hrubik	Victor Valley Water District	132	1,125	\$148,500
Tom Perry	Victor Valley Water District	30	1,125	\$33,750
2000 Totals		849	1,125	955,125
2001 Totals		0	0	\$0
Ben Hinkle	Hesperia Water Co.	68	1,250	\$85,000
LHC Alligator LLC	Hesperia Water Co.	265	1,300	\$344,500
LHC Alligator LLC	Hesperia Water Co.	539	1,300	\$700,700
2002 Totals		872	1,296	1,130,200
LHC Alligator LLC	Hesperia Water Co.	391	1,350	\$527,850
Dexter Trust	Baldy Mesa Water District	175	1,450	\$253,750
Thompson Trust	Hesperia Water Co.	35	1,400	\$49,000
Apple Valley Development	Baldy Mesa Water District	424	1,600	\$678,400
Linda Jessen	Baldy Mesa Water District	250	1,650	\$412,500
2003 Totals		1,275	1,507	1,921,500
2004 Totals		0	0	\$0
2005 Totals		0	0	\$0
2006 Totals		0	0	\$0
Apple Valley Development	Victor Valley Water District	200		\$0
Pettis Trust	City of Victorville	38		\$0
Candlewood Properties	Aqua Capital Mgmt	36	3,250	\$117,000
Desert Wind LLC	Aqua Capital Mgmt	240	3,333	\$800,000
Thompson Trust	Aqua Capital Mgmt	28	3,400	\$95,200
2007 Totals		542	3,330	1,012,200
Richard Petalski	Aqua Capital Mgmt	11	3,650	\$40,150
2008 Totals		11	3,650	40,150
2009 Totals		0	0	\$0
CalMat Company	Aqua Capital Mgmt	685	4,100	\$2,808,500
2010 Totals		685	4,100	2,808,500
2011 Totals		0	0	\$0
Grand Total		8,240		\$12,162,145

Mojave Water Agency Directors Map and other Maps

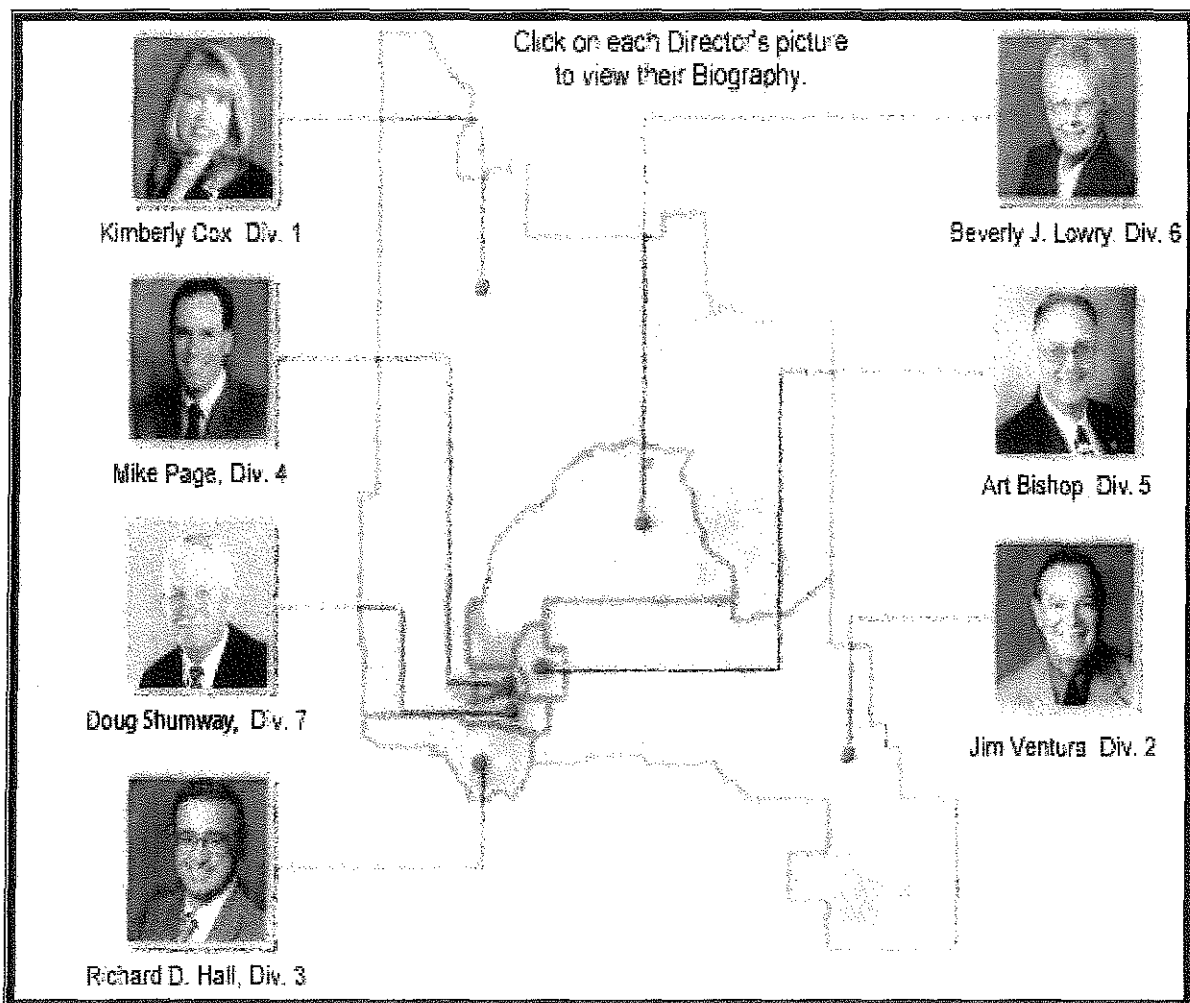
The Mojave Water Agency has a total of seven Directors; four of them represent portions of the Town of Apple Valley and its Sphere of Influence:

Division 5: Art Bishop, Board President
[Majority of the existing Town Limits]

Division 2: Jim Ventura
[Area in southern, eastern, & northern Apple Valley]

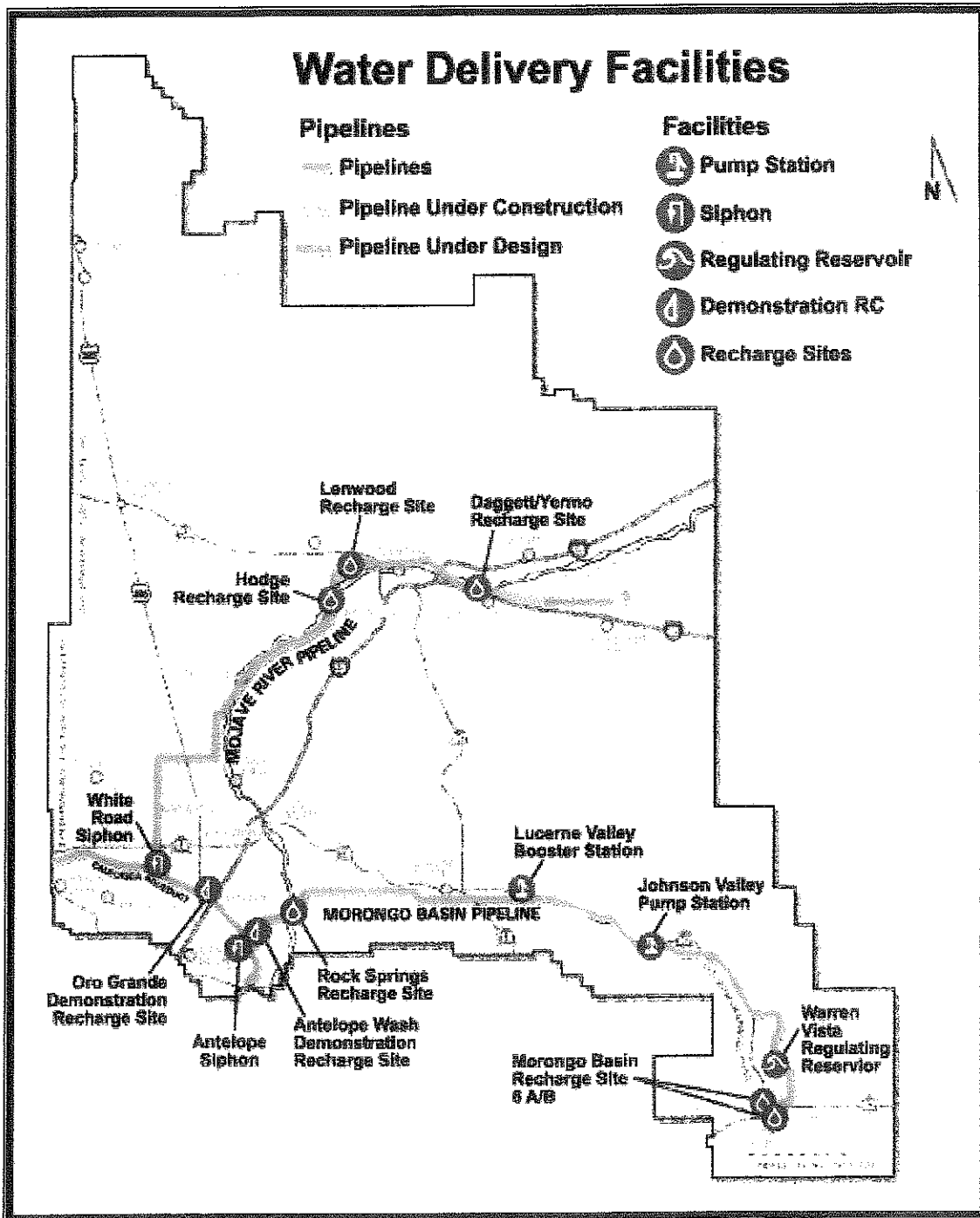
Division 6: Beverly Lowry
[Area in northern Apple Valley]

Division 7: Doug Shumway
[Area in southern Apple Valley]



Map of Mojave Water Agency Regional Infrastructure Improvements

The following Water Delivery Facilities Map delineates numerous projects throughout the MWA-managed region. The Town of Apple Valley does not have a single water delivery facility within the existing Town Limits. However, there is a water well under construction near the Mojave River and the Town's southern boundary, which is intended to provide supplemental water to AVR.



Mojave Water Agency Law Excerpts (Taxing Authority)

The following Mojave Water Agency Law Excerpts pertaining to purpose and tax authority are added to this report to provide the Apple Valley Town Council with the scope of powers and duties of the Mojave Water Agency. Currently, the MWA tax on vacant land cannot exceed 45 cents (\$0.45) per one hundred dollars (\$100) of assessed valuation. However, the "current assessed valuation" for vacant land is only \$0.10.7 (discussion with General Manager Kirby Brill and Board President Art Bishop). Thus an additional assessment of \$0.34.3 (\$0.45 - \$0.10.7) may be available on vacant lands for water management, legally mandated and related purposes -- specifically targeted for those areas without a current water purveyor. Verification of impact for areas with a water purveyor, improved property and other information will require legal counsel and ultimate policymaking decision by the MWA Directors.

EXCERPTS

www.print.westlaw.com/delivery.html?dest=atp&format=HTML&dataid=B005580000. 7/26/2005

The Mojave Water Agency is one of 29 State Water Contractors with access to the State Water Project. The MWA was created by High Desert voters in 1960. The MWA is governed by a seven-member elected Board of Directors. The Agency, in cooperation with other water districts is responsible for managing the region's water resources to ensure a sustainable supply of water for present and future use. (per Website)

§ 97-1.5. Purpose of Agency

Sec. 1.5. Within the limits of its power and Agency set forth in this act, the purpose of the Agency shall be to do any and every act necessary to be done so that sufficient water may be available for any present or future beneficial use of the lands and inhabitants of the Agency, including, but not limited to, the construction, maintenance, alteration, purchase, and operation of any and all works or improvements within the Agency necessary or proper to carry out any object or purpose of this act and the gathering of data for, and the development and implementation of, after consultation and coordination with all public and private water entities who are in any way affected, management and master plans to mitigate the cumulative overdraft of groundwater basins, to monitor the condition of the groundwater basins, to pursue all necessary water conservation measures, and to negotiate for additional water supplies from all state, federal, and other sources.

Effective: [See Text Amendments] § 97-16. Pumping assessment; rates and charges; tax levies; purposes; applicable laws

.....the board of directors shall determine the cost of construction or acquisition of necessary works, including costs of financing studies, the acquisition of options, permits, and other preliminary costs incurred or to be incurred prior to undertaking construction or acquisition of a project, as well as costs of issuing bonds, including the payment of interest, principal, and any premium thereon, secured by a pledge of the assessment against pumping or the rates and charges for water sold by the Agency, or both, and any costs relating to any other authorized purpose of the Agency. The Agency shall annually, at the time county taxes are levied, levy an ad valorem tax on land only within the Agency not to exceed 45 cents (\$0.45) per one hundred dollars (\$100) assessed valuation for the purpose of paying all other costs, expenses, and obligations of the Agency under any such contract. If an ad valorem tax on land levied at a rate of 45 cents (\$0.45) per one hundred dollars (\$100) assessed valuation will not yield adequate revenue for such purposes, the Agency shall, at the same time, levy an additional ad valorem tax on all taxable property, exclusive of personal property, within the Agency for the additional revenue required for the purpose of paying all other costs, expenses, and obligations of the Agency under any such contract. For the purpose of this section, the term "variable costs" means those costs paid by the Agency which constitute operation, maintenance, power, and replacement costs incurred in an amount which is dependent upon and varies with the amount of project water delivered to the Agency by the state.

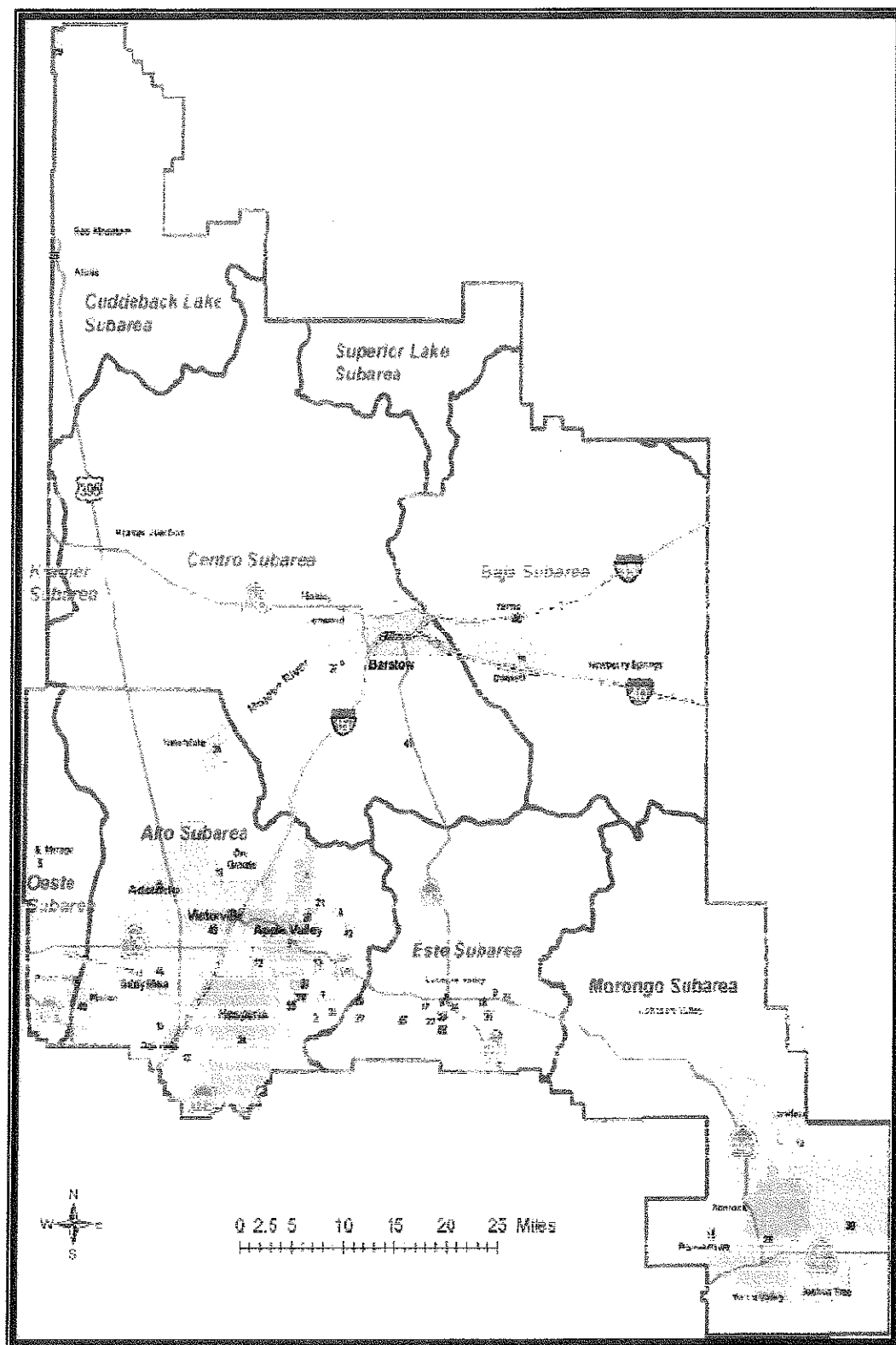
To accomplish the administration of the Agency, there shall be levied a tax not to exceed ten cents (\$0.10) on each one hundred dollars (\$100) of the assessed valuation of all taxable property in the Agency exclusive of personal property. Taxes to pay the principal of, and interest on, bonded indebtedness shall be levied on all the property in the area subject to that taxation when duly authorized by a vote of the electors. These taxes shall be levied and collected with, and not separately from, taxes for county purposes. The revenue derived from these taxes shall be paid into the treasury of the county to the credit of the Agency, and the board may control and order the expenditure thereof. The provisions of the laws of the State of California prescribing the priority, time, and manner of levying, assessing, equalizing, and collecting county property taxes, including the sale of property for delinquency and the redemption from such sale and the duties of the various county officers with respect thereto, are, so far as they are applicable and not in conflict with the specific provisions of this act, hereby adopted for the Agency and made a part hereof.....

All Mojave Water Agency Water Purveyors

The following is a list of all water purveyors within the MWA boundary. There are 11 purveyors indicated in **bold face** within the greater Apple Valley community. The Golden State Water Company serves four separate locations. The first map delineates the location of all MWA purveyors. The subsequent maps show the specific boundary for each of the Apple Valley water purveyors.

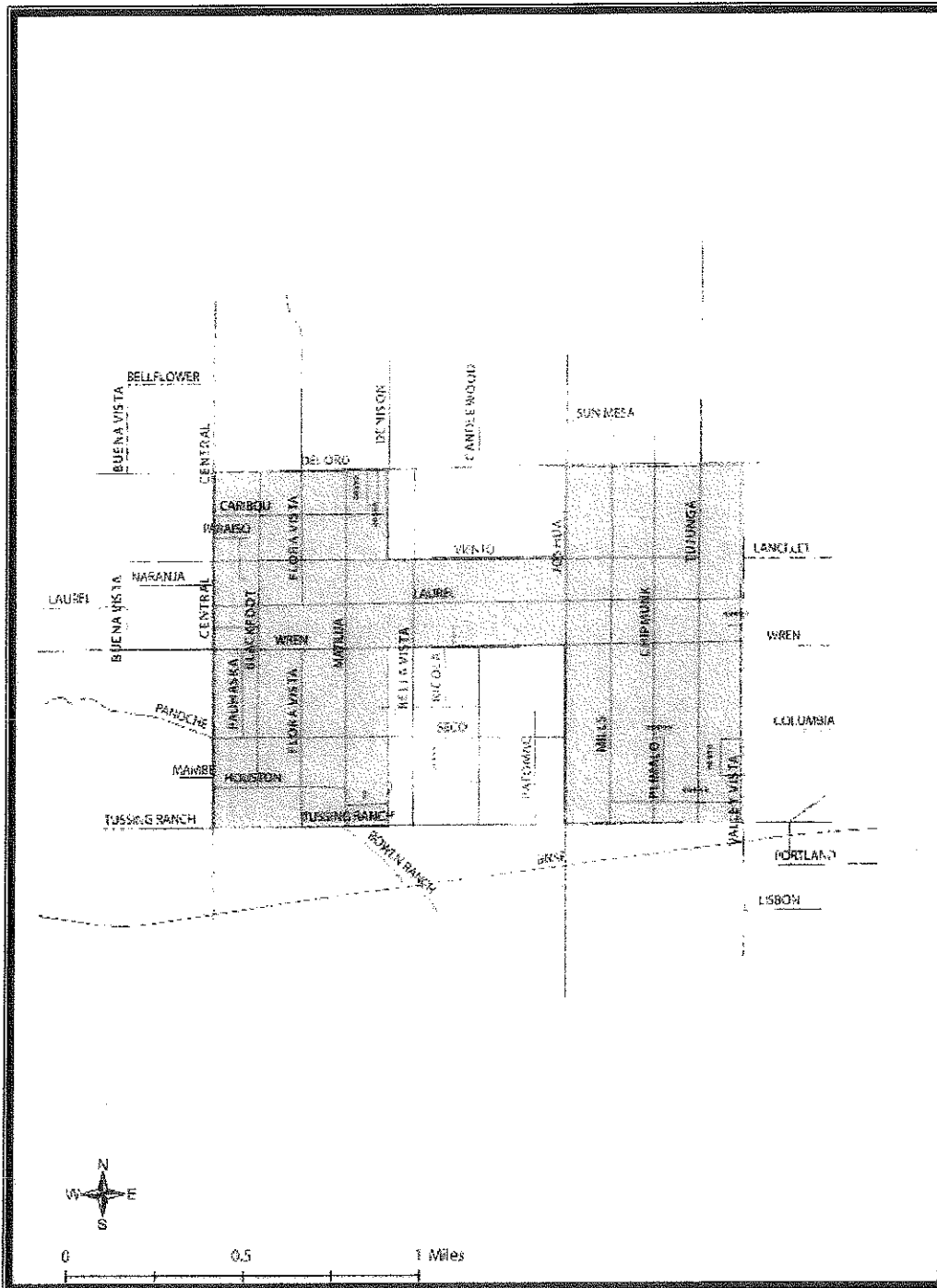
- | | |
|--|---|
| 1. Apple Valley Foothill Co. Water District | 26. Hesperia Water District |
| 2. Apple Valley Heights Co. Water District | 27. Hi Desert Mutual Water Company |
| 3. Apple Valley Ranchos Water Company | 28. Hi Desert Water District |
| 4. Apple Valley View Mutual Water Co. | 29. Indian Wells Valley Water District |
| 5. Bar H Mutual Water Company | 30. Joshua Basin Water District |
| 6. Bar-Len Mutual Water Company | 31. Jubilee Mutual Water Company |
| 7. Bighorn-Desert View Water Agency | 32. Juniper-Riviera County Water District |
| 8. Center Water Company | 33. Lucerne Valley Mutual Water Company |
| 9. Chamisal Mutual Water Company | 34. Lucerne Vista Mutual Water Company |
| 10. City of Adelanto | 35. Mariana Ranchos County Water District |
| 11. County Service Area 42 | 36. Navajo Mutual Water Company |
| 12. County Service Area 64 | 37. Phelan Pinon Hills Community Services District |
| 13. County Service Area 70 J | 38. Rancheritos Mutual Water Company |
| 14. County Service Area 70 W1 | 39. Rand Communities Water District |
| 15. County Service Area 70 W4 | 40. Sheep Creek Water Company |
| 16. Daggett Community Services District | 41. Stoddard Valley Water Company |
| 17. Desert Dawn Mutual Water Company | 42. Thunderbird County Water District |
| 18. Desert Springs Mutual Water Co. | 43. Victorville Water District Improvement District #1 |
| 19. Golden State Water Apple Valley | 44. Victorville Water District Improvement District #2 |
| 20. Golden State Water System 3 | 45. West End Mutual Water Company |
| 21. Golden State Water System 5 | 46. Yermo Water District (in escrow by Yermo Community Services District) |
| 22. Golden State Water System 6 | |
| 23. Golden State Water System Barstow | |
| 24. Gordon Acres Water Company | |
| 25. Helendale Community Services Dist. | |

Blue Ribbon Water Committee Report: December 12, 2011 ©



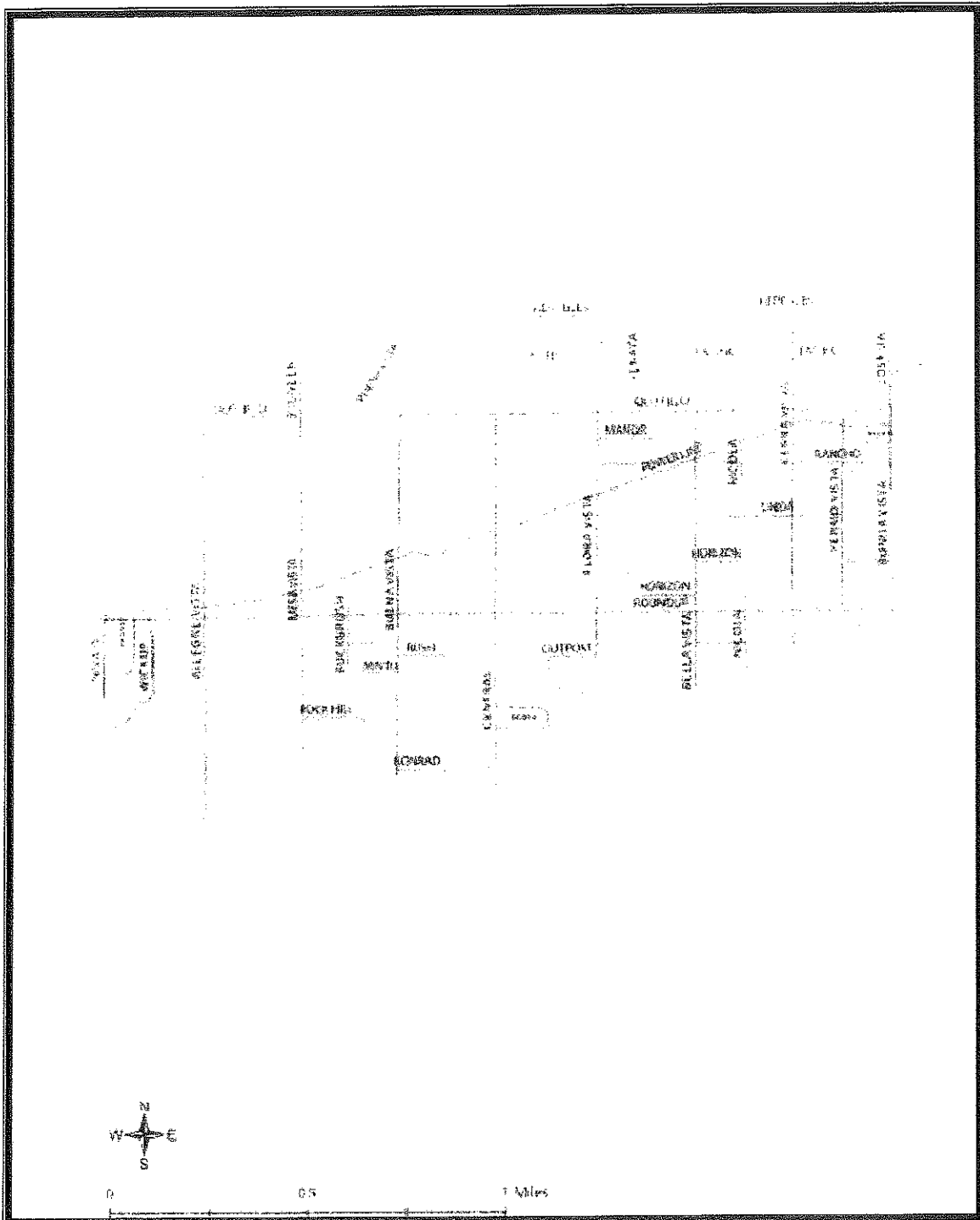
Apple Valley Foothill County Water District

22545 Del Oro Rd.
P.O. Box 914 (mail)
Apple Valley, CA 92307
(760) 247- 1101 phone
(760) 247-1101 fax
avfcwd@hotmail.com



Apple Valley Heights County Water District

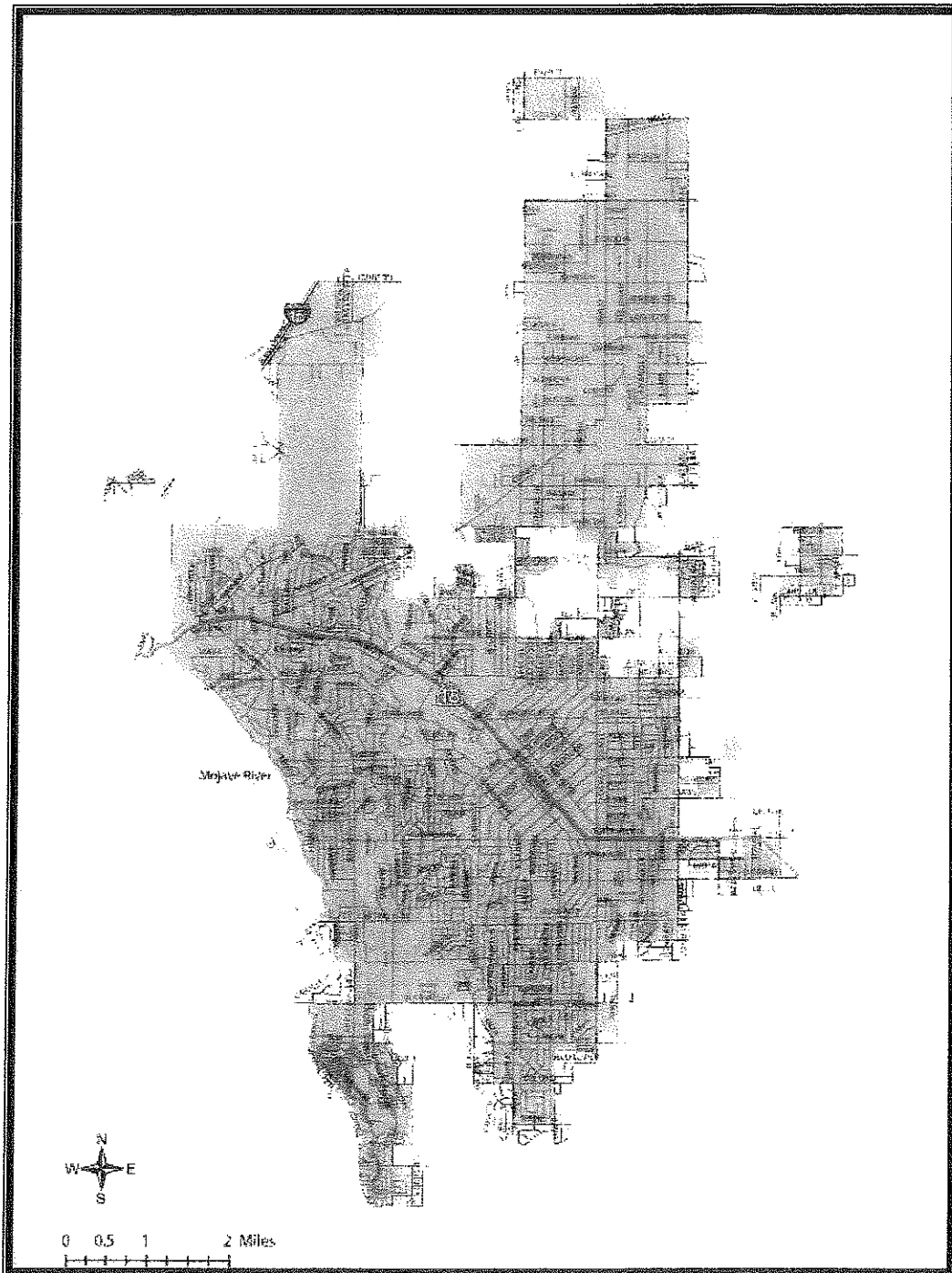
9429 Cerra Vista
Apple Valley, CA 92308
(760) 247-7330 phone
(760) 247-7721 fax
avhcwd@yahoo.com



Apple Valley Ranchos Water Company

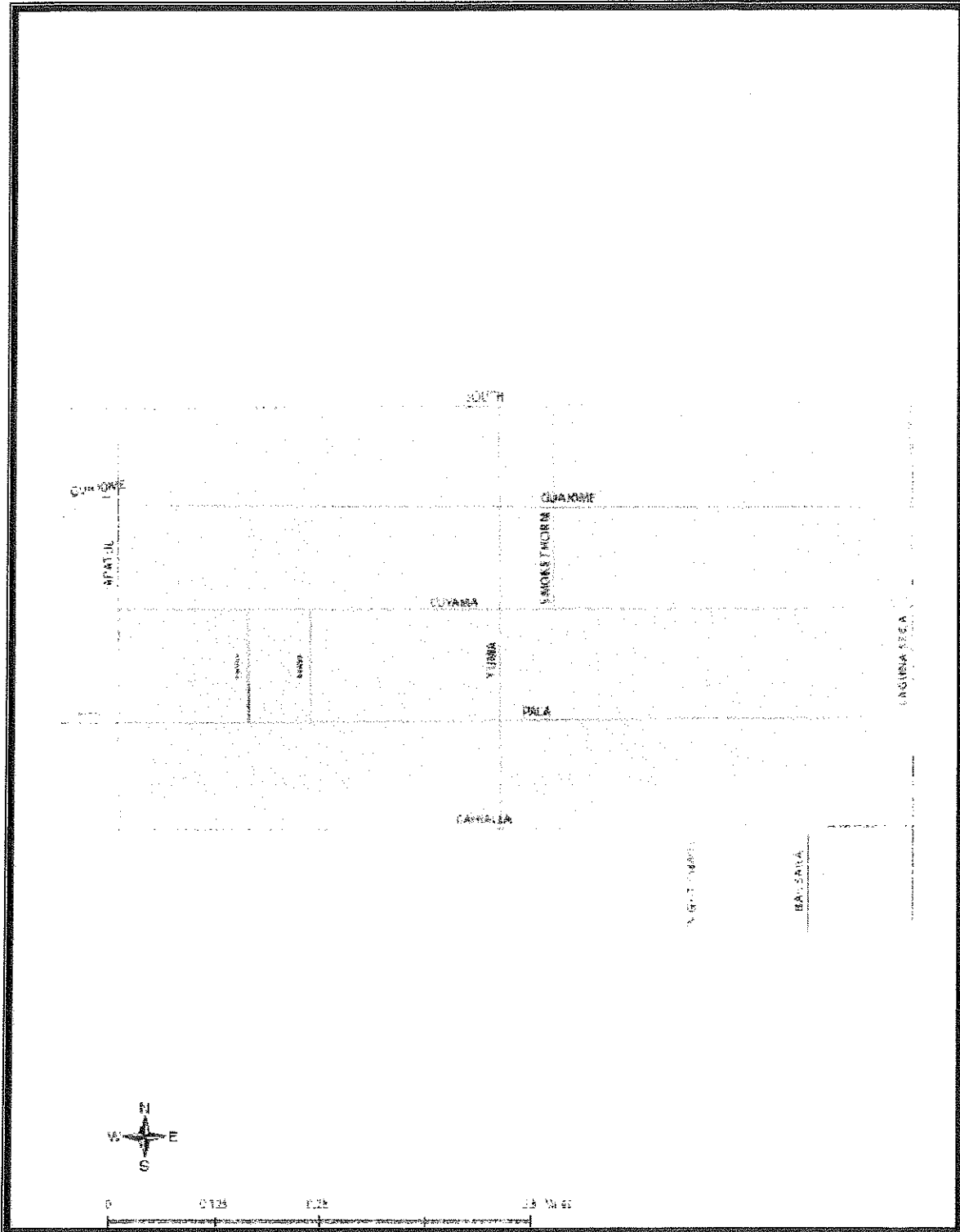
21760 Ottawa Rd.
P.O. Box 7005 (mail)
Apple Valley, CA 92307
(760) 247-6484 phone
(760) 247-3669 fax
scott@avrwater.com

(Map does not include Fairview Valley area to the east)



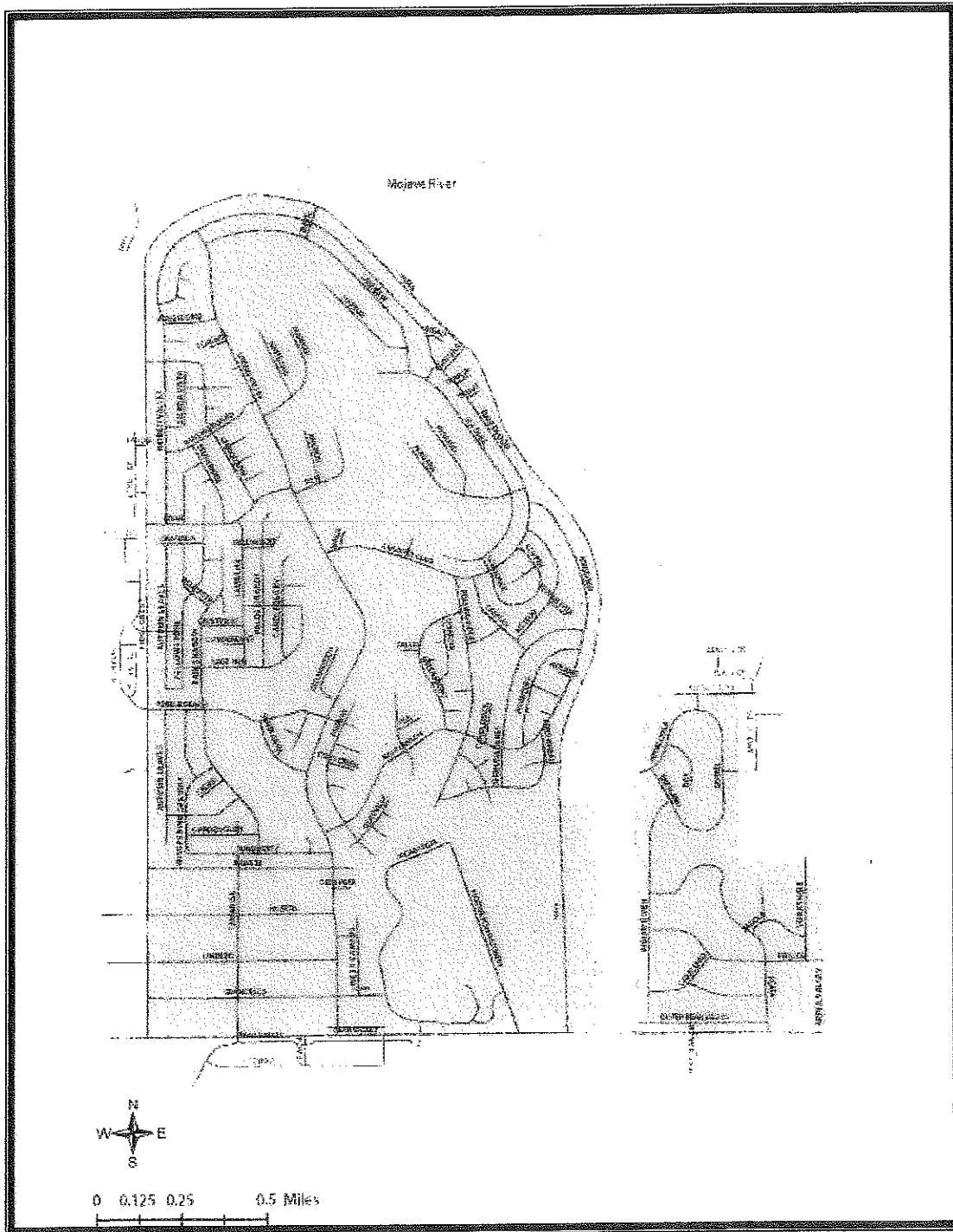
Apple Valley View Mutual Water Company

P.O. Box 3680
Apple Valley, CA 92307
(760) 247-4217 phone



County Service Area 64

12402 Industrial Blvd. Bldg. D, Suite 6
P.O. Box 5004 (mail)
Victorville, CA 92395-5004
(760) 955-9885 phone
(760) 955-9685 fax
customerservice@sdd.sbcounty.gov
www.specialdistricts.org



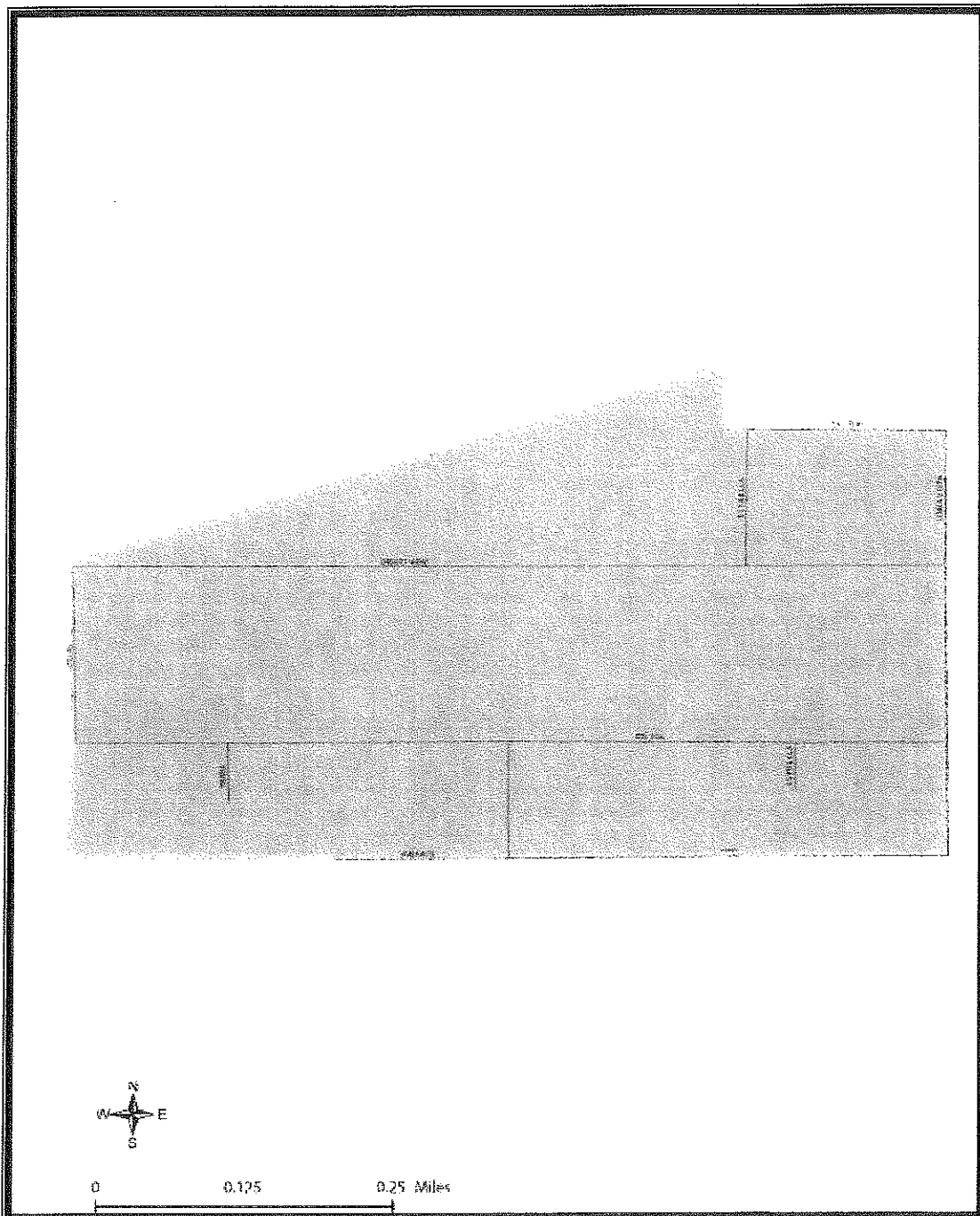
Golden State Water - Apple Valley

13608 Hitt Rd.
Apple Valley, CA 92308
(800) 999- 4033 customer service
(760) 247-7420 phone
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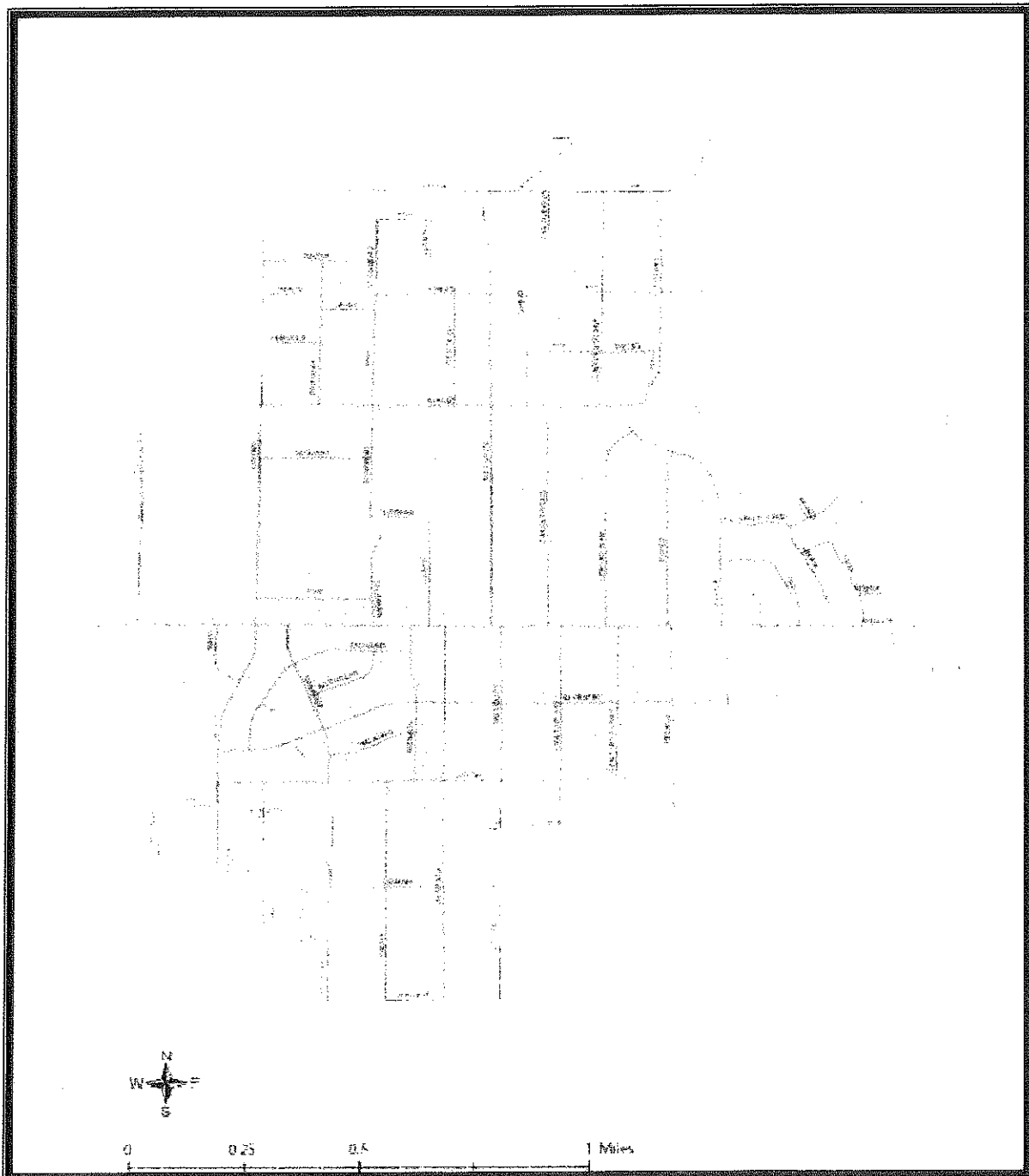
Golden State Water - System 3

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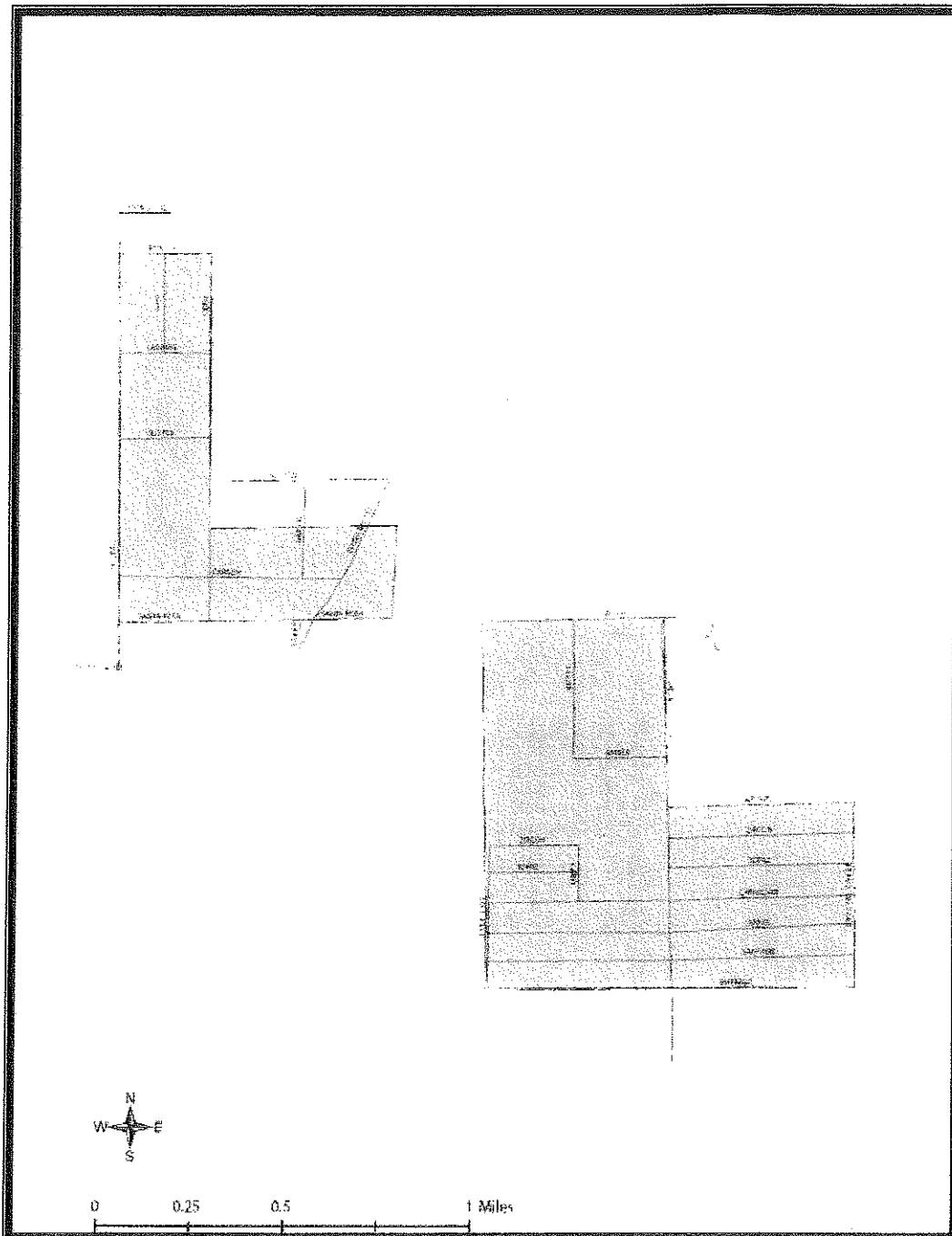
Golden State Water - System 5

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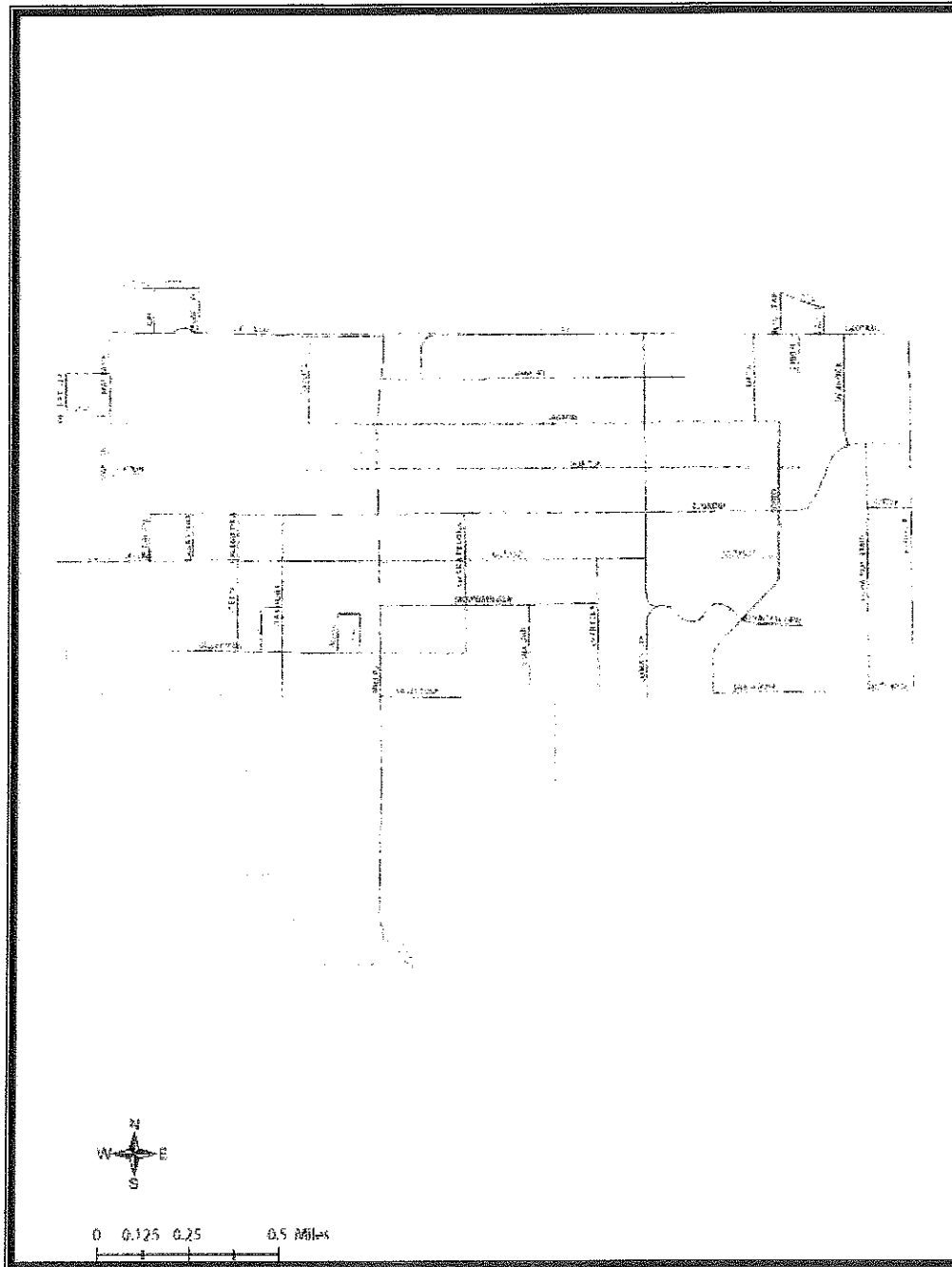
Golden State Water - System 6

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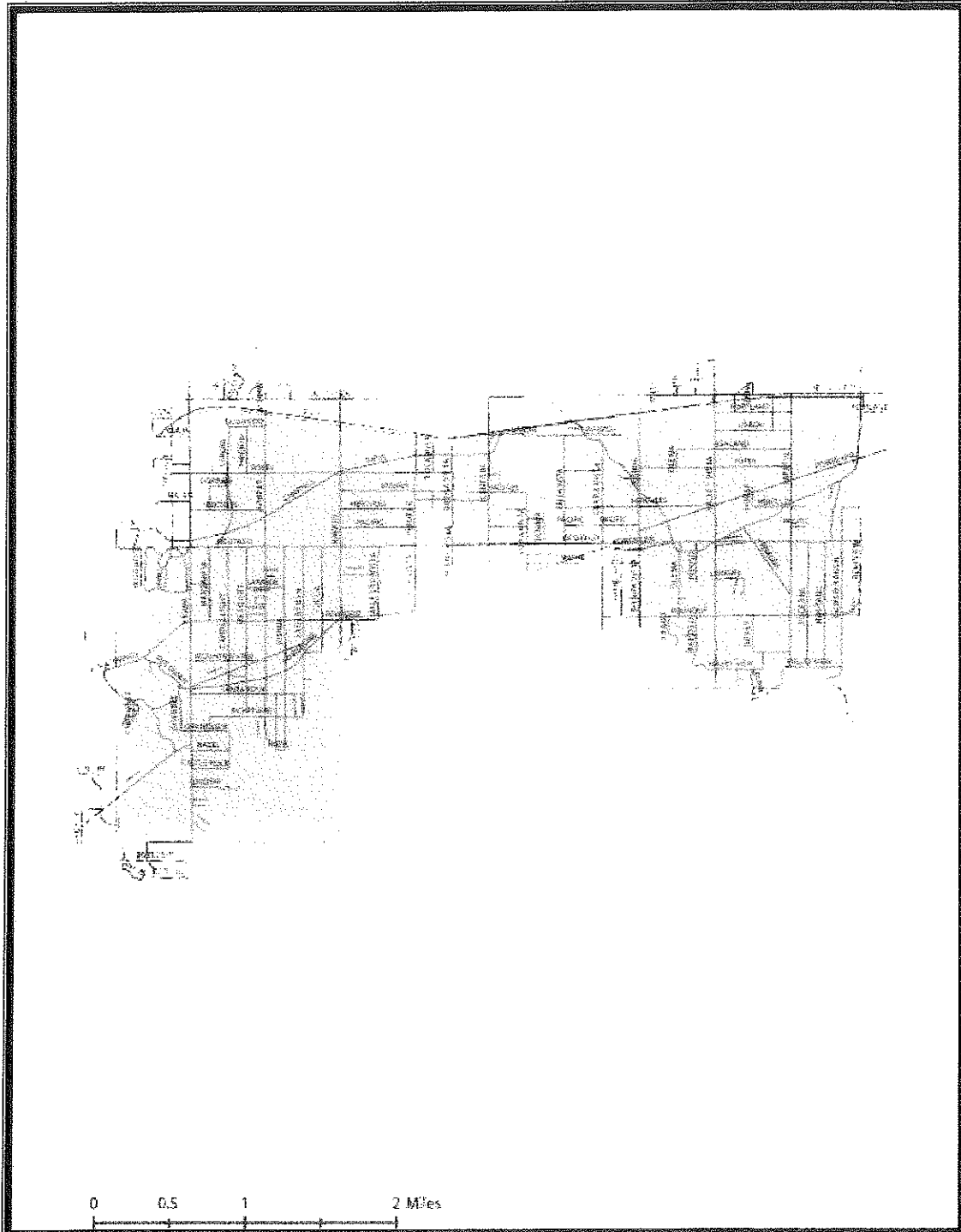
Juniper-Riviera County Water District

25715 Santa Rosa Rd.
P.O. Box 386 (mail)
Apple Valley, CA 92307
(760) 247-9818 phone
(760) 247-3974 fax
jrcwd@earthlink.net



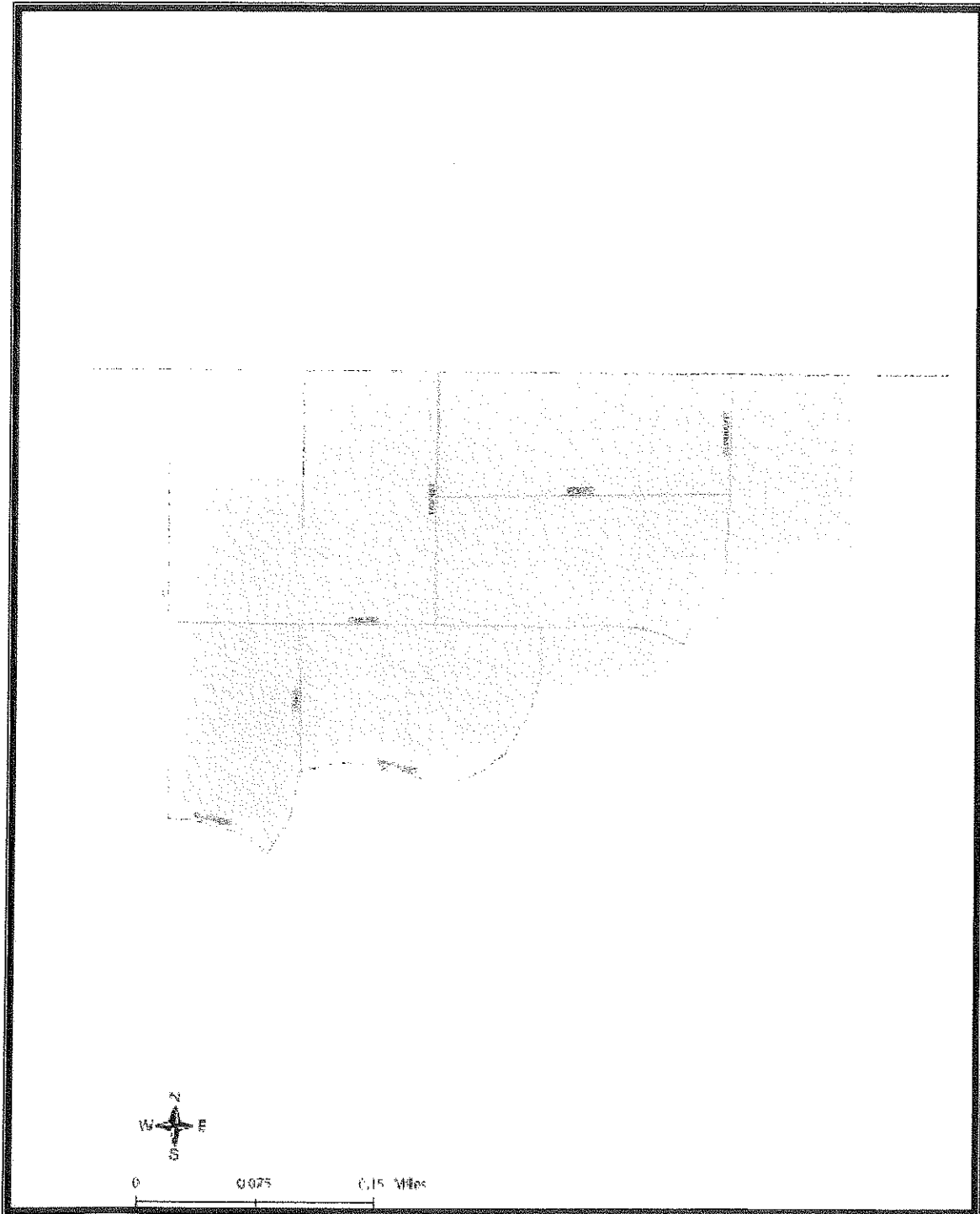
Mariana Ranchos County Water District

9600 Manzanita St.
Apple Valley, CA 92308
(760) 247-9405 phone
(760) 247-1205 fax
marianacwd@verizon.net



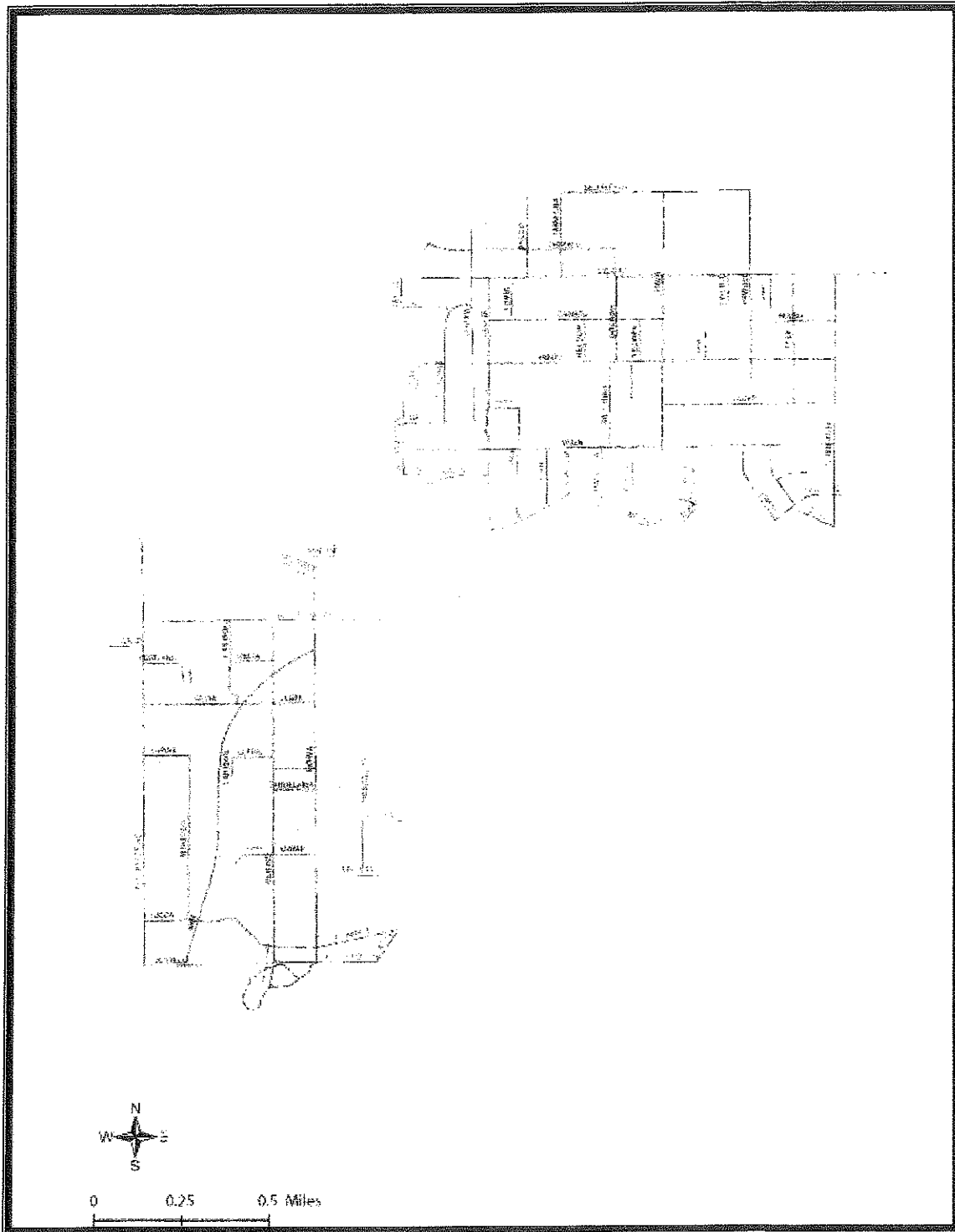
Navajo Mutual Water Company

P.O. Box 392
Apple Valley, CA 92307
(760) 954-3363 phone
jhansenjr@email.com



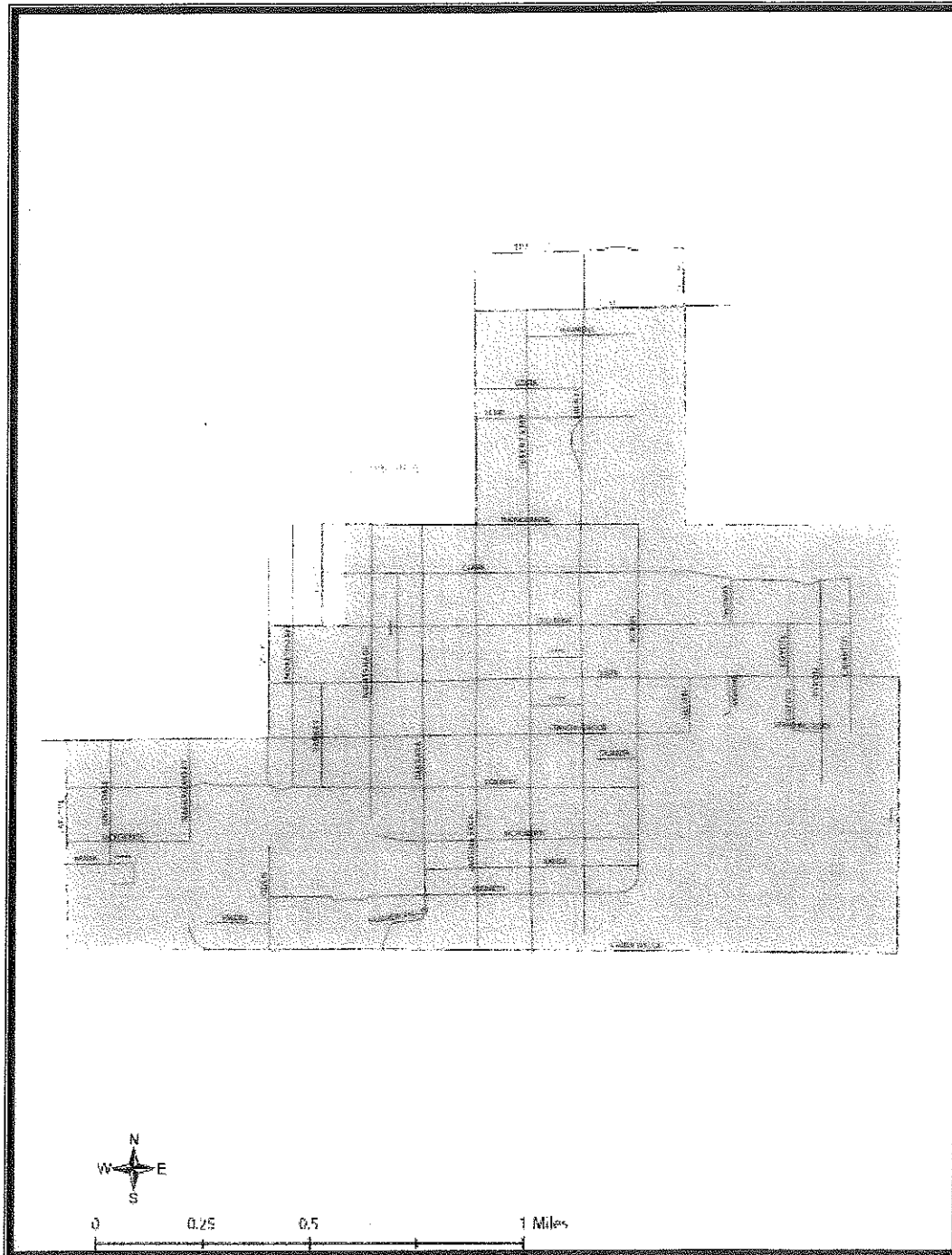
Rancheritos Mutual Water Company

P.O. Box 348
Apple Valley, CA 92307
(760) 247-3730 phone
(760) 247-3730 fax



Thunderbird County Water District

24737 Standing Rock Rd.
P.O. Box 1105 (mail)
Apple Valley, CA 92307
(760) 247-2503 phone
(760) 247-2305 fax
thunderbirdcwd@aol.com



Public vs Private Ownership Committee

Public vs Private Ownership of a Water Company [Risk-Benefit Summary of Issues]

There are both Benefits and Risks for the Town of Apple Valley to purchase and operate its own municipal water company, which are enumerated in the following two tables:

- Benefits of Public Ownership of a Water Company
- Risks of Public Ownership of a Water Company

<i>Public Entity BENEFITS</i>	<i>Discussion</i>	<i>Other Comments</i>
Local Control over the Water System allows for an improved perception to existing residents, ratepayers and future businesses	The Town needs true local control with a separate entity to ensure that water rates are under control and as low as possible	Adjacent Cities have control of their water systems which just in appearance is more competitive
Improved Business Model allows new businesses to be competitive when moving or expanding in Apple Valley	The Capital Improvement Funds for new development will be used entirely to expand and improve the existing water system	Capital Improvement Funds cannot be used for operational, emergency or any other purposes
Existing AVR Employees 1 - Hired by the Town and will become Town Employees 2 - Hire a management and operation services company similar to the existing Town Engineering and Building & Safety Dept.	Government Employees for any proposed Water Dept./Entity will have CalPers and other long-term costs	Perception: Do government employees work more or less efficiently or economically than private sector employees
Reduce Overhead Costs potential to be incurred by "Public Ownership"	The overhead under private ownership refers to the dividend to be paid to stock-holders	Perception: Does reduction in Overhead off-set any real in-efficiency in Government employees
Adjudicated Water Rights (ramp-down of 40% from Free Production) will be used entirely for existing ratepayers	Good, strong, efficient "public entity" management will be required	Need legal affirmation of existing Adjudicated Water Rights will not be sold or encumbered
Tier Water Rates	Good, strong, efficient "public entity" management will be required	Can be more sensitive to existing Apple Valley residents

Public Entity BENEFITS	Discussion	Other Comments
"Improved Reliability" and "Increased Efficiency" results	Perception: Do government employees work more or less efficiently than private sector employees	Policymaking decisions can also improve reliability and efficiency issues
Standby Fees	Policymaking can examine this and provide a nexus for fees for improved lots and unimproved land parcels	This is a small percentage of the total annual budget
Rate Stability during economic down-turns	This is debatable unless the new entity requires a significant "rainy day fund"	Providing a multi-year deficit income similar to the current 22% lower income levels is a significant management and leadership issue
Reclaimed Water from the A.V sub-regional Waste Water Plant	Coordination and better access to reclaimed water for the Town's public parks, school facilities	Coordination for potential new industrial oriented job generating businesses

Public vs. Private Ownership Committee

Public vs Private Ownership of a Water Company [Risk-Benefit Summary of Issues]

<i>Public Entity RISKS</i>	<i>Discussion</i>	<i>Other Comments</i>
Cost of Purchase	If the Town does not consider it now, the cost will keep going up, as when Apple Valley Water District or the Town of Apple Valley had prior opportunities for purchase. This will include future CPUC sanctioned rate increases regardless	The rate paying customers will continue to pay for in-efficiencies and millions in salary to owners like Co-CEO Sam Wheeler, family members and Co-CEO Schilling or the Carlyle Group which provide no added value or reduction in operational costs on a long term basis
Litigation Potential – If eminent domain is used and the Town is unable to approve a financing mechanism	This is a main reason why the BRWC recommends a separate public entity to have the effective means to sell bonds or other financing options	Creation of a larger rate paying and tax-revenue base and additional revenue sources is also recommended
Carlyle Group and Park Water Company will fight the Town	Carlyle Group and the Park Water Company may get more money due to the alternative process	Perception: Carlyle Group purchase of Park Water (plus three components of company) will be argued to what is the separate value of AVR in the baseline price in a willing seller and buyer perspective
Water Rates will not go down for a period of years	Regardless, the ratepayers will always pay for increasing Water Operational Costs The ratepayers will pay for the Purchase Price and Financing Costs for a definite period of time in any purchase	Ever-Increasing Water rates will continue with a CPUC regulated water utility. See #1 Comment, as they also govern here. There will be a point in time when rates will increase less when system is fully purchased and Best Management Practices are achieved
Carlyle Group may have other "Investment Money" to expand the AVR system into the NAVISP and other undeveloped areas of Apple Valley	The Carlyle Group would want to have extensive returns on any additional investments, making a future take-over more difficult and expensive in the future	A Public Entity (Town) can provide financing for new development via Assessment Districts, Community Facilities Districts or other entities, subject to full disclosure and required rate increases and policymaking decisions

Public Entity RISKS	Discussion	Other Comments
Carlyle Group wants continuing revenues and high-profits from AVR Purchase and Operations	A Carlyle Group system expansion is not allowed by current CPUC rules because it is considered speculative for AVR	This is the concern of the Blue Ribbon Water Committee (BRWC) The Town needs to analyze legal alternatives
Residential Ratepayers do not want to pay for future development; either water infrastructure expansion in the industrial and commercial or any other undeveloped areas	Under a Public Entity, AB-1600 connection fees by developers will cover such costs; under the private ownership concept, current ratepayers are paying for such infrastructure expansion	The Town needs to analyze this to maximize flexibility The Town needs to analyze legal alternatives
Requires an excellent Board for policymaking decisions and staff to oversee operations effectively	Current AVR Co-CEO Schilling has publicly stated he will continue to be the CEO with the Carlyle Group purchase	The Carlyle's Western Water CEO would be running AVR if current Co-CEO is replaced; a multi-national investment fund firm would appear to be a poor choice to operate a local water company or for the best interest of local ratepayers and the Town
Retain Water Rights – What happens to the existing Water Rights if the Wheeler Family is only technically selling the water production, storage and delivery systems and attempts to sell the Water Rights or attempts to financially encumber the Water Rights	Need legal affirmation of existing Adjudicated Water Rights will not be sold or encumbered; CPUC decision provided written verification that the water rights have to remain with the AVR BRWC is still concerned	The purchase of the AVR by the Town will thoroughly examine the Water Rights issues and will transfer any and all Water Rights to the Town by properly following procedures of the Water Master and the Mojave Water Agency, similar to the Apple Valley Golf Course purchase in 2011
Retain Water Rights – What happens to the existing Water Rights if the Carlyle Group attempts to sell the Water Rights or attempts to financially encumber the Water Rights	Need legal affirmation of existing Adjudicated Water Rights will not be sold or encumbered; CPUC decision provided written verification that the water rights have to remain with the AVR BRWC is still concerned	The purchase of the AVR by the Town will thoroughly examine the Water Rights issues and will transfer any and all Water Rights to the Town by properly following procedures of the Water Master and the Mojave Water Agency, similar to the Apple Valley Golf Course purchase
Loss of CPUC over-sight and Rate-Payer Advocate	Good, strong, efficient "public entity" (Town) management and staff will be required	Can be more sensitive to existing Apple Valley residents Can provide flexibility for job generating businesses in Apple Valley

Finance Committee


The Finance Committee Report is 94 pages in length and shown in Addendum 10 in its entirety. The following Executive Summary and Abstract from that Report summarizes financial concerns, impacts, and challenges confronting the Town of Apple Valley and its citizens to purchase and own a municipal water company.

Executive Summary

Acquisition of the Water Company

The Finance Committee recommends that the Town not attempt to purchase Apple Valley Ranchos Water Company (AVR) through condemnation for the following reasons (in no particular order of importance):

1. The value of AVR set by the Court may be substantially more than the Town could fund through bond financing. In the present economic climate, The Town may not be able to raise \$50 million or more through a General Obligation Bond or Specialty Tax Bond. The Bond Rating of the Town of Apple Valley along with many cities in California was reduced from A- to BBB+ in 2011.
2. The value established by the Court in a condemnation proceeding could greatly exceed AVR's real market value. The Town should not substantially overpay for AVR in any acquisition.
3. The value established by the Court could exceed a purchase price that would make economic sense to the ratepayers of AVR.
 - A. AVR water rates could increase from present levels by an estimated 46% between now and 2019. This would add \$206 to the average annual water bill of \$448. Therefore, the increases in property taxes due to bond financing for the purchase of AVR should not exceed the expected 46% increase in the average water bill over the next 8 years. The BRWC thought it would be in the interest of the ratepayers to incur this level of higher property taxes in order to avoid any future increases in water rates.
 - B. Given this limitation, (property tax increases should not exceed a 46% increase in the average water bill over 8 years): The maximum purchase price that could be funded by General Obligation Bonds is \$90 million. The Maximum amount that could be funded by Specialty Tax Bonds is \$60 million because of higher interest rates. This assumes the interest rates the Bartle Wells Report estimated (the financial markets would require for each financing option) proves to be accurate. The BRWC is concerned that the interest rates would be substantially higher should the Town attempt such a large bond issue.
4. Both bond financing options would require a 2/3 vote of approval by the voters of the Town of Apple Valley. It would be extremely difficult to get 2/3 of the voters to approve the Town's acquisition of AVR, because other than the likelihood of substantial increases in water rates, there are no serious deficiencies in the delivery of water to the AVR ratepayers.

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5. Certificates of Participation (COPs), a form of Revenue Financing, do not require voter approval in a general election, and do not count as indebtedness under the California constitutional debt limitations. Unfortunately, the Town would not be able to issue COPs to finance the purchase of AVR, because the Town-owned water company is expected to generate only approximately \$554,000 of Cash Flow in 2012 provided the water rates are not increased from 2011 levels. For example, an \$80 million COPs would require approximately \$9.9 million per year to service the debt.

The Bartle Wells Report concluded that there would be \$6 million of Net Revenue available per year to service the bond debt. This is not correct. The Cash Flow that would be available to make the bond payments would be \$5.5 million less than the Bartle Wells Report indicated.


6. If the Town of Apple Valley was not able to purchase the water company, either because it did not obtain voter approval, or because it could not obtain the bond financing, AVR and its owner, which would likely be the Carlyle Group, would sue the Town for damages. This could lead to a substantial award against the Town.
7. It would not be prudent for the Town in this economic environment to incur \$5 million or more in legal and consulting fees for a hostile condemnation proceeding, when the Town's annual budget for 2011-2012 is only \$25 million.



Ongoing Monitoring of AVR

The BRWC's fundamental concern is that the Carlyle Group through its Infrastructure Fund will purchase Park Water Company, and over time, place a substantial amount of debt either directly or indirectly on AVR for the following reasons (in no particular order of importance):

1. To the extent that the Carlyle Group over leverages the water company and pays the shareholders excessive returns, would result in substantially higher water bills compared to the present, and relative to adjacent city-owned water companies.
2. Moreover, it would likely lead to a lack of investment in system upgrades, thus inhibiting the responsible growth of the Town of Apple Valley relative to neighboring cities.
3. Accordingly, the Finance Committee recommended that the Town convince the CPUC to stipulate 12 conditions for its approval of the merger of Park Water Company and the Carlyle Group for two reasons: (1) to prevent AVR being over leveraged and (2) to require AVR to provide the Town with adequate financial information so that it can determine what AVR is doing.



The Finance Committee recommends that the Town actively monitor the activities of AVR and its interactions with the CPUC to be aware of AVR's intentions relative to rate and fee increases. This would enable the Town to take steps to minimize the extent of

AVR's Water Rate and Connection Fee increases. This would benefit the ratepayers after 2014 and curtail the increase in the market value of AVR.

Future Purchase of the Water Company




Later when the Town of Apple Valley is experiencing a sustained population growth and economic expansion, it could be advantageous for the Town to Purchase AVR for the following reasons (in no particular order of importance):



1. The Town would not have to pay Federal and State Income Taxes or Property Taxes to the County.
2. The Town should be able to reduce Senior Management and CPUC Expenses by an estimated \$1 million per year.
3. The Town-owned water company would be able to charge Connection Fees, which could be used to fund the extension of the water system and investment in new pipes and equipment. This would reduce the ongoing pressure to increase water rates.
4. After 2019, if the Town were to own the water company, the average annual water bill, plus the average additional Property Tax Assessment, could be less than the typical water bill if AVR is owned by the Carlyle Group. In the years immediately after the acquisition by the Town, the typical ratepayer would pay more, because of the additional debt service on the bonds used to fund the acquisition.
5. The Section 5 of BRWC's Report on Public vs. Private ownership describes in detail the advantages and disadvantages of a Town owned water company.
6. The Carlyle Group has publicly indicated that it intends to sell AVR after 7 years. However, the CPUC specifies ownership will dissolve no later than September 28, 2021. The BRWC recommends that the Town consider purchasing AVR when it is available for sale. The BRWC further recommends negotiating a purchase price for AVR-- rather than taking over AVR by hostile condemnation proceedings. This would enable the Town to know the purchase price before it decides to proceed with the acquisition. The BRWC recommended that the CPUC include in its approval of the merger of Carlyle Group and the Park Water Company a condition that The Town be given a first right of refusal when the Carlyle Groups sells AVR in the future, however the CPUC declined.

Abstract of the Report

The following Abstract is intended to act as a bridge between the Executive Summary and the detailed Finance Committee Report in this BRWC Final Report (Addendum 10).

1. The Bartle Wells Report projected there would be \$6,016,000 of Net Revenue generated by AVR in 2012 if it were purchased and managed by the Town of Apple Valley. The Finance Committee's analysis estimates the expected Cash Flow that would be realized in the first year after the acquisition to be closer to \$554,000. There are several reasons why the Cash Flow of the Town-owned water company would be substantially less than estimated in the Bartle Wells Report.
 - A. Actual billed Revenue is projected to be 22% or \$4,286,000 less than the budgeted Revenue of \$19,463,000 used in the Bartle Wells Report. This is because actual water usage by AVR ratepayers is projected to be 30% less than budgeted volumes. This negative impact on Cash Flow is partially offset by a \$2,015,000 reduction in projected Operating Expenses due to the delivery of less water in 2012. Hence, the Town-owned water company is expected to realize a Net Income of only \$2,580,000 compared to \$5,316,000 estimated in the Bartle Wells Report.
 - B. In 2012, AVR estimates that it would invest \$3,700,000 for Plant and Equipment, because all of these types of investments are added to the rate base. The Bartle Wells Study assumed a capital investment program of only \$2,000,000. The additional capital expenditures AVR projects would reduce the water company's annual Cash Flow by \$1,700,000; however, this shortfall will be paid back to AVR in future rate increases.
 - C. In 2012, AVR will be required to repay approximately \$795,000 in Advances, which will also negatively impact the Water Company's Cash Flow. This could be partially offset by the collection of Supplemental Water Acquisition Fees and Facilities Supply Fees.
 - D. The Town of Apple Valley would most likely be reimbursed by the Town-owned water company each year for the loss of \$186,319 in Franchise Fees and \$457,000 in Property Tax Revenue currently paid by AVR to the Town. To the extent the Town was not reimbursed, its General Fund Revenue would be reduced.
 - E. Given these and a few other minor adjustments, The Town-owned water company would realize \$554,000 in Cash Flow in its first year of operation.
2. AVR has generated Cash Flow through the collection of Supply Facilities Fees and the Supplemental Water Acquisition Fee. Part of the Supply Facilities Fee recovers the proportional cost of both existing and future capital assets such as water main extensions and the installation of new wells, required to serve the new connection. The second fee is called the Supplemental Water Acquisition Fee. It was established to fund AVR's pre-purchase of Replacement Water from MWA or to acquire water rights should such water rights become available.

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- A. Since their inception, AVR collected \$2,700,000 in a combination of Supply Facilities Fees and Supplemental Water Acquisition Fees. It purchased \$2,650,000 in pre-purchase of Replacement Water from the Mojave Water Agency or water rights.
 - B. In the current Rate Case AVR had proposed an increase in the Supply Facilities Fee from \$800 to \$900 per residential unit and an increase in the Supplemental Water Acquisition Fee from \$3,500 to \$5,000 per residential unit or residential equivalent unit. As of October 2011, the California Public Utilities Commission (CPUC) has not approved such increases.
 - C. If in the second half of this decade the level of residential, commercial, and industrial construction approached half of the average annual volumes experienced in 2004 through 2006, AVR could collect \$3,000,000 a year in such fees if the proposed higher AVR unit rates were approved by the CPUC.
3. If the Town of Apple Valley were to purchase AVR it could generate Additional Cash Flow through Connection of Fees from water company customers associated with new development projects.
- A. We strongly recommend the Town not rely upon Connection Fees to fund ongoing Operating Expenses or the debt service on bonds used to purchase AVR or any other water company. The amount of cash collected from Connection Fees depends upon the level of new construction. Hence, Cash Flow of the water company will fluctuate as new construction increases or decreases. During the years 2004 through 2006, developers on average pulled permits for approximately 1,000 single-family residential units in the Town. From 2010 through the first eight months of 2011, approximately 50 housing units were permitted each year.
 - B. We think it is unlikely the construction of new housing units will increase in any meaningful number before 2016. Consequently, such fees will not be a significant source of funds from 2012 through 2015. Connection Fees are best used to fund capital expenditures for a water system when construction levels are high.
4. If the Town of Apple Valley were to purchase AVR, it would likely not have to raise water rates, because it is expected to experience a positive Cash Flow of \$553,732 in 2012. There would however, have to be an increase in Property Taxes due to the issuance of General Obligation bonds, or Mello-Roos Bonds, in order to fund the purchase.
5. If the Park Water Company or the Infrastructure Fund of the Carlyle Group were to own AVR, it would likely receive rate increases over the next few years because of three factors.
- A. The first factor is the requirement to increase After Tax Net Income in order to compensate for increases in the AVR's Operating Costs and increases in AVR's Rate Base.

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- i. In 2012, AVR's total Rate Base is projected to be approximately \$40,500,000. The Deferred Debit Accounts are not included in the Rate Base, because they are not included in Plant and Equipment. In 2010, the CPUC determined the After Tax Annual Rate of Return that AVR must realize in 2012 through 2014 on its Rate Base would be 9.42%. Given a marginal Federal and State tax rate of approximately 40%, this is equivalent to a pre-tax Rate of Return of 15.70%.
 - ii. As of October 21, 2011, 10-Year T-Bills are earning a pre-tax return of approximately 3.0%. The interest rate on a 30-year mortgage on a single family home is 4.2%. Again, this is a pre-tax return to the investor. The CPUC only allows AVR to earn an interest rate equal to the 90 day commercial paper rate on the balance in its the Deferred Debit Accounts. That rate was approximately 1% in November of 2004.
 - iii. While a pre-tax rate of return of 15.7% would be extremely high if all the assets in the Rate Base were valued at current replacement cost; however a significant portion of the assets in AVR's plant and equipment were installed years ago. Their depreciated value is substantially below replacement costs. It is difficult to draw any conclusions regarding whether or not the Rate of Return is too high unless we have a reliable estimate of today's depreciated replacement costs. The fact that AVR's 2012 Cash Flow including Surcharges is about breakeven suggests the Rate of Return is not too high.
 - iv. A 15.7% Pre-Tax Rate of Return gives AVR an incentive to install new plant and equipment on which they can realize a high return for a low level of risk. This can benefit the Town of Apple Valley in that AVR has a built in economic incentive to invest in the extension of the Water System. On the other hand, the Town has to monitor AVR's investment program to ensure that they do not over invest and therefore raise the water rates more than is necessary.
 - v. The actual projected increase in Revenue due to increases over present water rates is 11.13% for the DRA recommended program and 14.49% for AVR's proposal in the Settlement Agreement. The CPUC approved rate will most likely be somewhere between the two.

- B. The second factor that would generate pressure for high water rates would be the downward adjustment in projected water usage if the Town's actual water usage remains near current levels rather than rebounding to more "normal" levels. If the ratepayers' level of water usage remained approximately 22% below pro-forma levels, and AVR and DRA agreed to base the water rates on actual water usage, the water rates would have to increase by approximately 17%. It is highly unlikely there would be any increase in the water rates before 2015 due to lower assumptions as to water usage.

- i. The combined rate increase for 2012, due to increases in Operating Costs and AVR's Rate Base, and the increase required to eliminate under-billing, would be approximately 30%.
 - ii. Representatives of Park Water Company would argue that the increase in rates to compensate for actual water usage should be less than budgeted, because the level of water usage is going to increase; so the shortfall will be less. Notwithstanding AVR's good intentions, we believe the combined water rate increase over present levels due to both factors would likely be in the order of 30%.
- C. The third factor that contributes to an effective increase in water rates relates to the recapture of under-billed Revenue through Surcharges. The latter does not actually increase the water rates; but it does increase the amount billed to the ratepayers. From the ratepayers' perspective, Surcharges represent a temporary (30-month) rate increase.
 - i. An annual Surcharge to the AVR ratepayers is currently approximately about \$2,100,000. It would be equivalent to an effective water rate increase of 13.51%. When the increase due to the Surcharge is combined with the regular water rate increases and the estimated increase in water rates required compensating for the lower level of water usage, the estimated increase in the typical ratepayer's water bill, above 2011 levels, would be about 43%.
 - ii. These preliminary estimates of the potential water rate increases do not include the usual cost-of-living increases of 2.5% per year that will also be incorporated into the water rates in 2013 and 2014.
 - iii. Surcharges are expected to begin to diminish within two and a half years after either water usage and/or water rates increase sufficiently to eliminate any under under-billing of Revenue. There is not likely to be any substantial reduction in the Surcharges billed to the ratepayers until after 2015.
 - iv. From the ratepayers prospective the best possible scenario after 2015 is that reductions in the Surcharges offset some of the increase in the actual water rates. While this may occur, for planning purposes the AVR ratepayers should anticipate a 40% to 50% increase from current rates after 2014.
- 6. Another significant source of Cash Flow to the water company is the collection of Supplemental Water Acquisition Fees and, to a lesser extent, the collection of Supply Facilities Fees. The collection of such fees is a nontaxable event.
 - A. After 2015, AVR could experience \$3,000,000 in additional Cash Flow less the amount used to purchase water rights and/or to pre-purchase Replacement Water; or the amount invested in Plant and Equipment. Such Fees would add 19.30% to the average water bill; but it would only be borne by new construction. Existing ratepayers would not experience any increase in their water bill.

- B. Towards the end of this decade, construction levels could reach 1,000 residential units per year. If the Supplemental Water Acquisition Fee were to remain at \$5,000 per unit, it would generate an additional \$3,000,000 in Cash Receipts.
 - C. It is also possible that, by the end of this decade, Supplemental Water Acquisition Fees could equal \$10,000 per unit. If this were the case, another \$6,000,000 would be added to the annual Cash Receipts of the water company.
 - D. The Supplemental Water Acquisition Fees and to a lesser extent the Supply Facilities Fees could substantially increase the Cash Flow of AVR without increasing its Net Income, because these fees flow through the Balance Sheet rather than the Income Statement. It is critical for the Town to review AVR's current and future request for increases in such fees to monitor the amount of funds collected and AVR's use of these funds.
 - E. We are not suggesting that this would actually occur. What we are requesting is that procedures be put in place by the CPUC to preclude this from occurring unless there is a real economic need other than excessive returns desired by the owners of AVR.
 - F. In addition, the Town of Apple Valley should be given sufficient financial information by AVR each year so that the Town can ascertain that AVR is properly investing the funds derived from the Supplement Water Acquisition Fees and the Supply Facilities Fees and to ensure that such fees will not become excessive.
7. The Water Committee's fundamental concern is that the Carlyle Group through its infrastructure Fund will purchase Park Water Company; and over time place a substantial amount of debt either directly or indirectly on AVR. To the extent, the Carlyle Group over-leverages the water company and pays the shareholders excessive returns it would result in substantially higher water bills as compared to the present and relative to adjacent cities that own water companies. Moreover, it would likely lead to a lack of investment in system upgrades, thus inhibiting the responsible growth of the Town of Apple Valley relative to neighboring cities. Accordingly, this report recommends a list of stipulations, aimed at preventing such a situation from arising, be incorporated into the resolution of the CPUC that approves the merger between the Park Water Company and the Carlyle Group's Infrastructure Investment Fund.
- A. One of the recommended stipulations is that AVR shall provide to the Town of Apple Valley a complete set of financial statements similar to the financial statements required of publicly owned industrial companies registered with the SEC. Such Financial Statements shall include a Balance Sheet, Income Statement, Source, and Use of Funds Statement in addition to supporting statements to the level of detail that would enable the Town of Apple Valley to verify that AVR is adhering to the recommended stipulations. Such financial statements shall be provided to

the Town within 60 days after the end of AVR's fiscal year. This financial information should also include a forecast for the current fiscal year.

- B. Since the adoption of Proposition 218 by the voters of the State of California, it is now extremely difficult for a city to obtain approval from two thirds of the voters to purchase a water company. AVR has a monopoly to supply water. If the ratepayers and the Town were not satisfied, it would be almost impossible for the Town to purchase AVR. In this new world of post Proposition 218, it is more critical for the CPUC to protect the ratepayers and the Town who are stakeholders in the water company without any effective recourse to purchase the water company. For this reason, it is imperative that the CPUC require AVR to provide the Town with sufficient information so that it can monitor the activities of AVR.
- 8. The value that the court would place on AVR in an eminent domain (condemnation) proceeding could vary widely. Chris Schilling has indicated that the Park Water Company's attorneys will argue the assets of AVR are worth substantially more than \$200 million dollars. Although this Sub-Committee expresses no opinion regarding whether this approximately \$200 million figure cited by Mr. Schilling is accurate, the Sub-Committee has incorporated this figure throughout the remainder of this analysis in order to provide a worst-case scenario analysis. The Town's attorneys and experts would likely make the case that the assets of AVR are worth less than that sum. However, to be conservative, the Town should be prepared to accept a potential condemnation price of greater than \$200 million even though an objective assessment of value might be much less.
 - 9. In the Bartle Wells Study, the use of \$121 million as the highest probable acquisition cost to the Town of Apple Valley and \$48 million as the lowest probable acquisition cost is acceptable even though the actual award by the court could be higher or lower. Both values are only used to estimate the service debt associated with the various types of financing. This is a reasonable range for purposes of the feasibility study and adequate for the purposes of the Finance Committee.
 - 10. The Finance Committee has not been able to reconcile the fact that AVR, which has experienced substantial negative Cash Flows since 2008 and will likely not generate a positive Cash Flow before Surcharges in 2012, could have a market value of \$121 million or even \$48 million. Such market values can only be justified if the buyer believes that it will be able to raise water rates, Supplemental Water Acquisition Fees, and Supply Facilities Fees Substantially in future years. If it is not able to convince the CPUC to approve such rates, the Carlyle Investment Group will not achieve its investment goals over the next several years.
 - 11. The value that the court would place on AVR in an eminent domain (condemnation) proceeding could vary widely.
 - A. Chris Schilling has indicated that the Park Water Company's attorneys will argue that the assets of AVR are worth several hundred million dollars. The Town's attorneys and experts would likely make the case that the assets of AVR are worth far less.

- B. To be conservative, the Town should be prepared to accept a condemnation price of greater than the \$200 million figure cited by Mr. Schilling even though an objective assessment of value may be only a fraction of this figure.
- C. If the Town is not able to purchase AVR at the condemnation price, Park Water Company has said they would sue the Town for damages.
12. The Finance Committee is also concerned that The Town could end up substantially overpaying for the water company if it purchased the water company through the condemnation process. If the court set the value of AVR at the \$200 million figure cited by Mr. Schilling the Town would be substantially over paying for the water company.
13. The relevant transaction costs are those associated with the acquisition of AVR through condemnation. The Park Water Company have made it clear that the Town will have to acquire AVR through a condemnation proceeding.
- A. Within the condemnation, proceedings there would most likely be two trials. The first trial would determine whether the Town had the "right to take" AVR from the Park Water Company. The Town would have to demonstrate to the court that there is a real benefit to the Town or the ratepayers to be able to condemn the water company. The court may not agree that the Town has the right to take AVR and the condemnation procedure would be terminated. Ultimately, the Town is likely to be able to establish that the acquisition of AVR's system is in the public benefit. However, there is always some risk that the Town may incur substantial cost preparing for the first trial and not be able to purchase AVR.
- B. If the court determines the Town has a right to take AVR from the Park Water Company or the Carlyle Group's Infrastructure Fund there would be a second trial to determine the purchase price.
- C. The Bartle Wells Report estimated that the total transaction costs would be \$4,248,000. This includes a cost allowance of \$1,000,000 for fees paid to the Condemnation attorney and trial costs. Litigation costs usually exceed initial budgets. For planning purposes, the Financial Analysis Subcommittee assumed the costs would be \$2,000,000. Hence, the total transaction costs associated with the purchase of AVR would be budgeted at \$5,248,000.
14. Bartle Wells Associates evaluated four major financing options that are available to the Town of Apple Valley for acquiring the AVR system. Financing would include funding the purchase of water facilities and land and the funding of transaction costs. The four methods of financing that Bartle Wells Associates investigated include:
- General Obligation Bonds
 - Mello-Roos Community Facilities District (Special Tax) Bonds
 - Assessment Bonds

- Revenue-Supported Borrowing

15. The following Table summarizes the annual estimated Debt Service payment required for each of the four financing options given the four assumed purchase prices for AVR that ranged from \$48 million to \$200 million. The General Obligation Bonds would require the lowest level of Debt Service. Special Tax Bonds are second. Certificates of Participations actually rank third. Their Debt Service payments appear to be less than Special Tax Bonds; however, it does not include the \$10 million in additional reserves that were factored into the other financing options. The lease desirable from a cost prospective is Assessment Bonds. The annual debt service range from a low of \$4.6 million for a General Obligation Bond associated with a \$48 million purchase price, to high of \$21 million for the use of Assessment Bonds to finance a \$200 million acquisition. Again, the Finance Committee expresses no opinion regarding whether the \$200 million figure cited by Mr. Schilling is accurate, but the Finance Committee has used that number to provide a worst-case scenario analysis and assure that this report's conclusions are conservative.

APPLE VALLEY RANCHOS WATER COMPANY SUMMARY OF ANNUAL DEBT SERVICE BY FINANCING OPTION November 14, 2011				
	Stock Price Lower Est.	Medium Price Estimate	RCNLD High Estimate	Very High Price Estimate
AVR Purchase Price	\$ 48,000,000	\$ 80,000,000	\$ 121,000,000	\$ 200,000,000
Annual Debt Service - General Obligation Bonds	\$ 4,622,160	\$ 6,949,861	\$ 9,932,228	\$ 15,678,739
Annual Debt Service - Special Tax Bonds	\$ 5,790,721	\$ 8,672,275	\$ 12,362,570	\$ 19,467,840
Annual Debt Service - Assessment Bonds	\$ 6,269,243	\$ 9,374,388	\$ 13,354,929	\$ 21,023,545
Annual Debt Service - Certificates of Participation	\$ 4,961,743	\$ 7,927,145	\$ 11,723,448	\$ 19,038,386

16. The only two viable financing options that could be used to purchase AVR: General Obligation Bonds and Special Tax Bonds. The use of any form of Revenue financing such as COPs would necessitate a 37% increase in water rates (if the purchase price were \$48 million) to 153% (in the case of a \$200 million acquisition price). The substantial increase in water rates would be counter to the primary goal, which is eliminating increases in water rates.
17. Dividing the projected level of Billed Revenue in 2012 at current rates, estimated to be \$15,540,237, by the number of Equivalent Meters, the average annual Revenue per meter would be \$448 or \$74.67 per meter every two months. This is close to AVR's Average bimonthly water bill of \$71.05 that was presented to the Water Committee.
- A. Water rates are expected to increase by approximately 18% by 2014 from present levels. This would increase the average household annual water bill by \$81. In 2015, water rates will be increased by an additional 13% or \$58 to adjust for the fact that actual water usage will continue to remain

below budgeted levels over the next three years. The combined annual increase for probable increase would be \$139.

- B. Our review of the economics of AVR also suggests water rates would increase an additional 15% during the period 2016 through 2019. This would add another \$67 to the annual average water bill. By 2019, the average water bill is likely to increase by \$206 or 46% from 2011 levels.
18. It may be in the economic interest of the ratepayers for the Town to purchase AVR if the price was less than \$90 million. At that price, the annual debt service per Equivalent Meter would be less than the expected increase in the average ratepayer's water bill. A higher price may possibly be justified if consideration was given to the potential reduction in the water rates after 2020 due the collection of Connection Fees.
 19. The use of a General Obligation Bond would result in all the property owners in the Town sharing in the cost to purchase AVR and fund any reserves that are included in the bond issue. Consequently, the owners of vacant land within the incorporated area of the Town of Apple Valley would bear a portion of the cost for improving the water utility company. This is justified because it would increase the value of their land.
 20. If Special Tax Bonds are used to finance the purchase, the annual debt service per equivalent meter ranged from \$167 if the purchase price for AVR was \$48 million to \$562 for a \$200 million purchase price.
 - A. This suggests that the acquisition of AVR using the Special Tax Bond option would benefit a typical ratepayer so long as the purchase price did not exceed \$60 million. If the purchase price exceeded that level, the average annual debt service per household would exceed the expected increase of \$206 in the average water bill by 2019.
 - B. Again, a higher price may possibly be justified if consideration was given to the potential reduction in the water rates after 2020 due the collection of Connection Fees.
 21. The use of a Special Tax Bond (e.g., Mello Roos) could require all the current landowners, not just the ratepayers, within the boundaries of AVR to bear the cost to purchase AVR. Additionally, the issuance of these bonds will require reserves for capital improvements for water infrastructure. Presently, the current owners of vacant land within the boundaries of AVR do not pay for any of the various costs to improve or maintain the water utility company. This gives those owners of vacant land a free ride until the property is developed.

Blue Ribbon Water Committee Report

Town of Apple Valley's

Best Opportunity for Affordable Water and Economic Sustainability

The Town of Apple Valley appointed fifteen citizens to the Blue Ribbon Water Committee because of the appointees' collective experience. The Town Council seeks the Committee's conclusions and recommendations regarding critical water issues. These three difficult issues and the BRWC's recommendations regarding each are summarized below:

- 1) **Carlyle Acquisition of Park Water Company** – The BRWC was asked to make recommendations related to the Carlyle Group's proposed acquisition of Park Water Company, the parent company of Apple Valley Ranchos Water Company.

During the Carlyle merger, the BRWC Chairman sent a letter to the Carlyle Group (Exhibit 1) seeking to determine whether the Town of Apple Valley could negotiate the purchase of AVR or have a First Right of Refusal. The BRWC received no response.

BRWC recommendations include:

- Generally the BRWC and Finance Committee believes there is a lack of financial accounting transparency from the AVR and CPUC review processes and this places any and all analyses into question. It appears that the Carlyle Group, with tacit permission from the CPUC, plans to increase the ultimate burden laid on the AVR ratepayers. Therefore, the BRWC recommended that the CPUC place 12 stipulations on the Carlyle Merger. Due to the hearing deadline, those proposed stipulations were submitted to the CPUC prior to the completion of this Report. However, CPUC's Administrative Law Judge summarily dismissed BRWC's request for stipulations. In addition, Apple Valley Ranchos fiercely opposed the proposed stipulations.
- The BRWC recommends renewing the submittal of revised stipulations as other opportunities to do so become available.
- The BRWC further recommends that a Town representative attend any further public meetings and/or hearings held by the CPUC in order to oppose, actively, the Carlyle Merger. It is imperative that attendance at such meetings and timely correspondence be provided in order to expose publicly the abuse being perpetrated on the ratepayers of Apple Valley.

The CPUC approved the Carlyle Merger on Dec. 1, 2011. The dissolution of the Carlyle Partners Infrastructure L.P. is designated on or before September 28, 2021 and the CPUC is to be notified 18 months prior for a CPUC approved dissolution plan.

- 2) **AVR Rate Increase Requests** – The BRWC was asked to make recommendations regarding AVR's proposed rate increase.

BRWC recommendations include:

- Continue actively to oppose all agreements, including CPUC agreements, for rate increases by the Apple Valley Ranchos Water Company and/or its parent company.
- 3) **Feasibility of Town-owned Water Company** – The BRWC was asked to make recommendations regarding the feasibility of alternatives that might allow for public ownership and control of the privately owned water companies presently selling water to the citizens and taxpayers of Apple Valley.

BRWC recommendations include:

- Based upon investigations and financial analysis, the BRWC concludes there are minimal current financially feasible methods or positive voter-approval enabling the Town to afford the purchase of either AVR or GSWC. This conclusion is predicated upon the current conditions in any of the conventional financing methods outlined in the Bartle Wells Report using eminent domain or other processes. Accordingly, the BRWC recommends against the Town's sole acquisition of AVR or GSWC by eminent domain, at this time. However, future financial conditions may change to alter this conclusion.
- 4) **BRWC Makes an Additional Water Rights Recommendation:**
- Additionally, the BRWC strongly recommends that the Town immediately create the legal mechanism and requirements for any new development to provide the correct (Nexus Study) amount of "Water Rights". Also for these "Water Rights" to be transferred to the Town for "Permanent Ownership" in exchange for any jurisdictional approvals required for the specific purposes of reducing the current financial impact to the existing AVR ratepayers (i.e., the Town would require 0.80 acre-feet of Water Rights per residential unit or equivalent for commercial and industrial uses).

The purpose of the Town's buying water rights is to prevent new development within the AVR boundary that will increase water rates for existing AVR ratepayers. For example, two master planned communities have already been approved by the Town of Apple Valley, and a third is pending within County jurisdiction, that will necessitate AVR's purchase or lease of substantial water rights to serve over 4,000 new residences. This will substantially raise water rates for existing AVR ratepayers, who will subsidize the cost to purchase or lease water for these new developments. The only way to remedy this endless financial burden on AVR ratepayers is fundamentally to change water policy: (1) Change CPUC rules and regulations that favor new development at the expense of existing ratepayers. (2) Require new development within AVR boundaries (including areas within San Bernardino County jurisdiction) to purchase and provide permanent water rights to the Town of Apple Valley prior to any jurisdictional approvals and construction activities.

The BRWC does not believe that the CPUC rules and regulations can be easily changed. Therefore, our only available remedy is to require new development to purchase permanent water rights and transfer the water rights to the Town. The BRWC believes the AVR will continue its primary strategy of leasing water rights annually, because leasing costs are tied to endlessly increasing the company's water rates and are passed on to existing ratepayers.

A more detailed discussion of each of the above three recommendations follows below:

1) **Request Stipulations on the Purchase of Park Water Company by the Carlyle Group.**

In 2011, Henry "Sam" Wheeler, the current majority shareholder of Park Water Company, of which Apple Valley Ranchos Water Company is one component, decided to sell Park Water

Company to the Carlyle Group for \$102,000,000 and apparently, as the BRWC has been told, an assumption of \$40,000,000 in indebtedness. Although the Apple Valley citizens would prefer that Mr. Wheeler had offered to sell AVR to the Town, instead he chose to sell his entire company intact in a single transaction to the Carlyle Group. The BRWC has asked Christopher Schilling, Co-CEO of Park Water Company, whether it would be possible for the Town to purchase AVR at this time. He advised us that Mr. Wheeler declines to sell the Town AVR and wants to sell Park Water Company in one piece to Western Water Holdings, a subsidiary of Carlyle Infrastructure Partners.

That sale requires the approval of the CPUC. Public hearings have been held in Apple Valley regarding the transaction, and a CPUC administrative law judge is deciding the matter. Meanwhile, the CPUC Division of Ratepayer Advocates and AVR negotiated a Settlement Agreement on September 15, 2011, of contentious issues regarding the company's request for a 20% rate increase. The parties have resolved most matters pertaining to the rate case. While DRA and AVR agree on the impacts the Carlyle transaction will have on the company's anticipated expenses for 2012 through 2014, they still disagree on how to deal with the contingency that the acquisition would not be completed by January 1, 2012. However, the parties agree that ratepayers of Park Water Company and AVR shall not incur any direct or indirect costs or other liabilities or obligations arising from the Carlyle transaction (such as outside legal expense and travel costs).

Stipulated Considerations

The BRWC recommends continued opposition to the purchase of Park Water Company by the Carlyle Group. The BRWC requested CPUC-mandated stipulated considerations, as originally delineated in Addendum 3 filed with the CPUC on October 20, 2011, and again revised pursuant to Missoula Montana stipulations and delineated in Addendum 8 within the Opposition to the Carlyle Merger filed with the CPUC on November 21st, 2011, all filed by the Town. The BRWC had previously concluded that continued litigation regarding this matter would be costly and probably be ultimately ineffectual and unproductive. Instead of costly legal confrontation, the BRWC thought a better solution would be for the Town to request the following considerations for its cooperation with the Carlyle transaction. Although these concerns were filed on October 20, 2011, to the CPUC proceeding with the intent to be considered as part of the record, these concerns (as briefly stated below) were summarily dismissed by the CPUC's administrative law judge:

- As a condition of acquisition of AVR by Carlyle (and a stipulated requirement by the Division of Rate Payer Advocates), the BRWC wants CPUC assurance that the 13,233 acre feet of water rights awarded by adjudication to AVR at no cost to the company--**and represented to the CPUC as being dedicated to the public use**--remain for the use of all AVR customers in the Town of Apple Valley.
- Negotiate the purchase of Apple Valley Ranchos Water Company at a future date with the Carlyle Group, or whatever entity becomes the eventual owner, consistent with what Park Water Company agreed to as between its subsidiary (the Mountain Water Company) and the city of Missoula, Montana and the Montana Department of Public Service Regulation (equivalent to the CPUC).
- Negotiate a "First Right of Refusal", or other preferred legal mechanism, to purchase AVR at a pre-determined time in the future.
- Negotiate a pre-determined purchase price evaluation scheme (i.e., based upon AVR's present stock valuation) for Apple Valley Ranchos Water Company.
- Negotiate a joint strategy with the Town of Apple Valley, or other designated entity, as the lead agency to negotiate with Carlyle Group to purchase all existing portions of the existing

Park Water Company serving the Town of Apple Valley in the future. Subsequently, and/or concurrently, the Town of Apple Valley will create an agreement with both the City of Missoula, Montana and Golden State Water Company to work out a financing and purchase program for all components of Park Water Company. The objectives of this cooperation would have three basic components. The City of Missoula to acquire Mountain Water Company and Golden State Water Company to receive the remaining management holdings of Park Water Company in Los Angeles County. The Town of Apple Valley to acquire Apple Valley Ranchos Water Company and all of the Golden State Water Company within the Town of Apple Valley Sphere of Influence.

2) Oppose Excessive Rate Increases by Apple Valley Ranchos Water Company.

The BRWC recommends that the Town of Apple Valley continue to oppose requests by Apple Valley Ranchos Water Company for unreasonable rate increases. As it has in the past, the Town (involving, as necessary, its legal counsel) must be vigilant and aggressive in representing water ratepayers before the California Public Utilities Commission to keep water affordable in the Town. Safe, readily available, affordable water is essential for the Town's continued fiscal viability as well as any future economic growth to provide high quality local jobs.

The BRWC commends the Town Council, Town staff and Best, Best & Krieger LLP for their concerted efforts that resulted in the CPUC holding two public hearings in 2011 at the Apple Valley Conference Center—instead of the CPUC San Francisco headquarters. As a result, Apple Valley citizens were able to testify before two judges regarding their unaffordable escalating water costs, their contention that water is their "God-given right" and should not be a commodity "sold for profit" at their expense and to their financial detriment. Many preferred local control of "their water rights." Some blamed CPUC-mandated tiered water pricing and new water meters as the cause of their inflated water bills. Many members of the Blue Ribbon Water Committee attended these hearings, and some testified regarding their personal experience as AVR's customers. This report reflects the consensus of the Blue Ribbon Water Committee—not any one opinion expressed by a member at the CPUC public hearings.

Apple Valley Ranchos Water Company is a privately held, currently family owned, for-profit water company being purchased at this time by the Carlyle Group. American States Water Company owns Golden State Water Company. This is a publicly traded water company and another water company currently serving portions of the Town. On November 1, 2010, AVR requested that the CPUC grant the company a 20.0% rate hike beginning in 2012. If approved, this would have increased AVR's annual revenue in the amount of \$3,896,586. However, the CPUC Division of Ratepayer Advocates recommended only a 5.7% increase over the actual revenue the company received in 2010, which was a CPUC rate estimate of \$19,500,000. The for-profit AVR estimated that its proposed rate increase would provide returns of 10.2% on equity and a 9.12% on revenue in 2012.

Settlement Agreement

After months of costly legal wrangling, public hearings, expert opinions, customer letters to the CPUC, the Town of Apple Valley's creation of a Blue Ribbon Water Committee, and extensive scrutiny by the DRA in the public interest, the parties renegotiated their water rate expectations. AVR reduced its rate increase request from 20.0% to 14.83%. The DRA increased its rate increase recommendation from 5.7% to 11.44%. The BRWC recognizes the DRA proposed 11.44% rate increase as a reasonable compromise and opposes a rate hike of almost 15%. However, the BRWC does not agree that a 9.12% to 10.2% or higher rate of return for investors is reasonable or feasible in the present depressed economy when the average ratepayer is earning less than 1.0% on bank interest and the current CPUC system guarantees a profit at "No Risk".

On September 15, 2011, a Settlement Agreement was negotiated between the Division of Ratepayer Advocates and Apple Valley Ranchos Water Company following extensive negotiations at arm's length over the course of many weeks. The Settlement Agreement considered the facts, the relevant law, and balanced various interests to reach reasonable compromises on most issues. If the CPUC adopts the Settlement Agreement, it will result in increased "reasonable rates to customers while providing adequate funding to AVR to ensure safe and reliable water service to those customers." In addition, CPUC "adoption of the Settlement will provide speedy resolution of contested issues, which will conserve Commission resources." The Settlement Agreement meets all standards for CPUC approval. Therefore, the Blue Ribbon Water Committee believes the CPUC will adopt the Settlement.

The 54-page Settlement Agreement (Addendum 2) presents some detailed information about AVR business operations and accounting methods, to which the BRWC did not have previous access. It is too lengthy to summarize; however, the BRWC offer the following that reflect the contents of the document:

Contested Issues

The Settlement still has not resolved disagreements between the DRA and AVR regarding the following issues:

- What rate increase will the CPUC adopt? The BRWC recognizes the DRA proposed 11.44% rate increase as a reasonable compromise and opposes a rate hike of 14.83% that AVR wants.
- AVR proposed a new office expansion project, but DRA has not agreed that it is necessary or affordable now.
- DRA has declined AVR's request to create three new positions: Water Audit Conservation Specialist, Water Quality Specialist, and Asset Management Project Coordinator. The BRWC recommends that if AVR wants to hire three new employees, the company needs to find the money by reducing payroll and benefit expenses among its existing executive workforce.
- Some payroll issues are still in dispute: AVR's request for merit pay, bonuses, and other benefit issues concerning medical and dental insurance, 401K and EAP/Wellness, and group pension. DRA and AVR agree that a regulatory account for group pension is appropriate but disagree on whether it should be a Balancing or Memorandum Account.
- DRA and AVR do not agree on the escalation year methodology AVR proposed for healthcare and retiree healthcare.
- The need for a Pressure Reducing Valve Memorandum Account AVR proposed is in dispute.
- The \$4,300 of new development fees need to be clarified on where they actually go or went.

Uncontested Issues

The DRA and AVR agreed on the following matters:

- In four categories, the number of customers anticipated to exist in 2012, 2013 and 2014 is not in dispute and will not increase or decrease during the next three years [an assumption agreed upon for rate case purposes and a consensus opinion of the BRWC]. The four categories of static growth are Industrial (2 customers), Public Authority (42 customers), Irrigation - Public Authority (5 customers) and Irrigation - gravity (1 customer).

- Water sales to residential users (CCF = hundred cubic feet per customer) was determined using different methods by DRA and AVR. However, they agreed to use AVR's estimated value of 233.2 CCF each year during 2012, 2013, and 2014.

Resolved Issues

The DRA and AVR agree to use the number of residential customers proposed in the DRA Report. For business, private fire, and pressure irrigation customers, the parties agree to average the five-year average increase from 2005 to 2010. For temporary construction customers, the parties agree to use the estimated customer growth in the business customer class. The Apple Valley Golf Course will be included as a separate customer class as proposed by the DRA.

3) At this time, Should the Town Acquire Any Water Company serving Apple Valley?

At this time, the BRWC analyzed whether the Town of Apple Valley should acquire Apple Valley Ranchos Water Company and/or Golden State Water Company's operations in Apple Valley, or any of the other eleven water purveyors serving the Town. The BRWC based its evaluation of whether the Town can specifically afford to acquire Apple Valley Ranchos Water Company on the following sources of information:


- The Bartle Wells Associates July 2011 "Update of Feasibility Analysis of Acquisition of Apple Valley Ranchos Water System."
- The CPUC issues, such as the proposed Settlement Agreement, Interim Rate Increases and pending contested issues before the CPUC in the Matter of the Application of Apple Valley Ranchos Water Company for Authority to Increase Rates Charged for Water Service.
- The BRWC Chairman appointed certain BRWC members to various committees and specifically a Finance Committee that includes two Members who have extensive experience evaluating financial data concerning the purchase and sale of companies: Dr. Ron Barbieri and Joseph Tartaglini. Addendum 10 is the Finance Committee's independent investigation, financial analysis, and committee report.
- All members of the BRWC reviewed the Bartle Wells Report, Settlement Agreement, and Addendum 10 to come to a consensus and make the conclusions and recommendations presented in this "BRWC Report".
- Various BRWC members and community stakeholders have reviewed a variety of other large planning Documents/Reports/Maps regarding various components relative to long-term water resource conservation and flood management purposes.

CONCLUSION: Based upon diligent investigations and review of all known relative reports and substantial financial analysis, the BRWC concludes that it is not currently financially feasible for the Town to acquire AVR. In the present uncertain economy, the acquisition of Apple Valley Ranchos Water Company and its continued operation by the Town is not feasible based upon existing financial information, as briefly stated for these reasons:

Other Relevant Issues for consideration by the Town of Apple Valley

Decreasing Population

There has been an exodus of residents from the Town of Apple Valley since 2007 so that the population has declined from 75,000 to 69,000 people—reducing the number of water customers and a loss of 1,600+ students in the Apple Valley Unified School District. In fact, it is possible that there will not be much population growth or commercial and residential




development in the High Desert and the Town of Apple Valley for the majority of the remaining decade. This scenario assumes there will not be much employment growth in Southern California and the Inland Empire, because the out-migration of businesses and jobs will continue for the majority of the remaining decade.

Water Conservation Trends

Over the last few years, AVR customers have been using substantially less water to compensate for rapidly rising water rates and the economic decline in the High Desert. Some individuals and organizations, including the CPUC, believe the decline in water usage is temporary and expect water consumption to rebound to the pre-recession levels of 2007. Others, including members of the BRWC, believe there has been a paradigm shift in customer attitudes about water consumption. The BRWC thinks an increasing percentage of AVR customers will continue to conserve water with xeriscape, rock-scaping, no landscaping, ornamental landscaping conversion to native plants and local native plant landscaping.

As a result of increasing water costs and CPUC-mandated tiered water pricing, AVR customers have been forced to use less water. To reduce their water bills, they will continue to remove lawns, mature trees, and other landscaping. They have replaced gardens with rocks and drought-tolerant desert plants. Many have drained their swimming pools, take fewer showers and baths, and flush toilets less often. To reduce their increasing water costs, AVR customers will continue to conserve water. Moreover, the existing base of AVR water ratepayers has already shrunk below 19,500. The BRWC thinks the number of customers will remain flat or could even decrease for the majority of the remaining of the decade.

Public versus Private Ownership



Public financing of a water utility is very complex, and there are advantages and risks for the Town of Apple Valley to own a water company (as discussed in the Public vs. Private Ownership Committee report previously presented). With Town ownership of Apple Valley Ranchos, the California Public Utilities Commission would no longer regulate the water company's operations. The Town would assume all these responsibilities and uncertainties. The CPUC's large staff of experts (including the Division of Ratepayer Advocates, engineers, accountants, judges and attorneys) would no longer decide water rates or protect the public interest. Instead, potentially the Town Council's five elected members would be the policymakers and Town Staff would run the Water Department or another designated entity (i.e. Water or Utility Dept.). They currently have little experience operating a municipal water company of this size (and potentially much larger in the future) and they would have to hire a Manager and support staff to assist them.

Blue Ribbon Water Committee Report

Town of Apple Valley's Best Opportunity for Affordable Water and Economic Sustainability

The Town of Apple Valley ultimately needs to control its own water destiny. Consolidating the operations of the existing 11 water purveyors in the Town's Sphere of Influence under a single public water entity is a worthy long-term objective.

Various water and environmental laws, conservation issues and constraints will continue to be a larger consideration for any issues affecting the future of the Town.

The vast majority of the Town of Apple Valley's Sphere of Influence of 200± square miles has no water purveyor and specifically needs the best possible long-term plan to improve this deficiency for approximately 130± square miles.

The primary intent in taking steps to keep water affordable is essential to the economic sustainability of the Town of Apple Valley, future creation of new high-quality local jobs for the Town's citizens and their grandchildren and truly living the Town's motto of "A Better Way of Life".


The BRWC also wants publicly to thank the citizens and other community stakeholders who have attended the various BRWC meetings and additionally for providing any information resources and discussions for the BRWC's use in creating this Final Report.

Specifically, the BRWC also formally wants to thank the Town Council members for their foresight and patience on this ongoing and important water mission. Additionally, the BRWC wishes to express its thanks for the Town Council's support of the Apple Valley Blue Ribbon Water Committee and providing Town resources – including legal resources, Town administrative staff, and facilities - for the benefit of the public in the form of noticed, public meetings where the citizens had the opportunity to observe and participate.

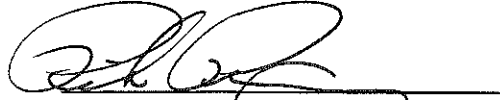
Should Council members wish to pursue any proposed alternative solution(s), please feel free to call upon any of us individually or collectively and other community members as you see fit.

Chairman and Committee Respectfully submitted this 12th day of December, 2011

Carl Coleman, Chairman



Rick Piercy, Vice-Chairman



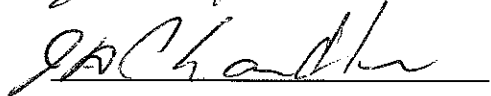
Ron Barbieri,
Chair's Finance Committee



John Bernier

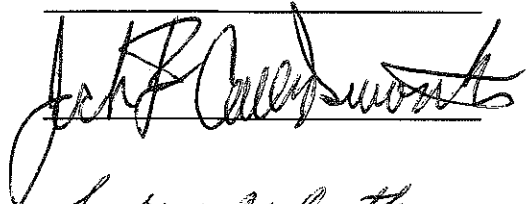


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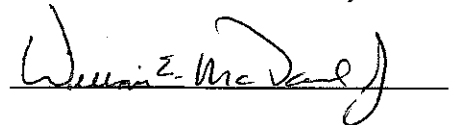
Jack Collingsworth



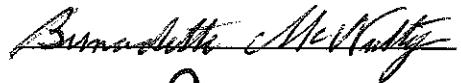
Lawrence McCarthy



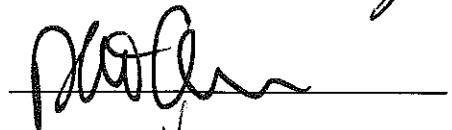
Bill McDaniel



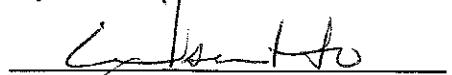
Bernadette McNulty,
Chair's Water Rights Committee



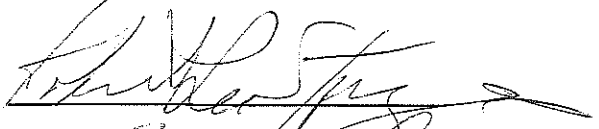
Pat Orr,
Chair's Public Information Committee



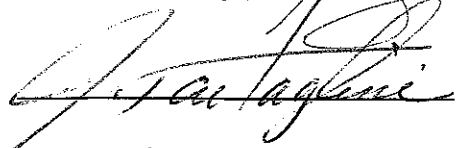
Wilson So,
Chair's Public vs. Private Ownership Committee



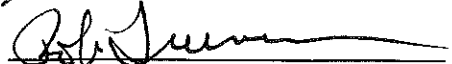
Robert Lee Sturges



Joseph Tartaglini



Rob Turner



Blue Ribbon Water Committee Report

Town of Apple Valley's
Best Opportunity for Affordable Water and Economic Sustainability

Exhibit No.

1 Letter to The Carlyle Group from Blue Ribbon Water Committee

Exhibit 1

Letter to: The Carlyle Group from Blue Ribbon Water Committee

Via Email: John.Flaherty@carlyle.com

THE CARLYLE GROUP
C/O JOHN FLAHERTY, PRINCIPAL
1001 PENNSYLVANIA AVENUE, NW
WASHINGTON DC 20004-2505

AUGUST 19, 2011

RE: Carlyle Group 2010 Corporate Citizen Report & Purchase of Park Water

Dear Mr. Flaherty:

I received the Corporate Citizen Report from Best, Best & Krieger (BB&K) and Robert Dove in May. I personally worked with Jim Krieger of BB&K as the General Manager of the Mojave Water Agency in the 1960's and 70's in regards to adjudicated water rights and long-term wholesale water supply management regarding the California Water Project. Congressman Jerry Lewis's first bill as a California Assemblyman was regarding the Mojave Water Agency and I have a picture with then Governor Ronald Reagan signing it and personally it is good to see that BB&K acquired Miller & Van Eaton in DC as a strategic expansion in July.

The Town appointed a 15 member Blue Ribbon Water Committee in which I am Chairman of and last evening we had another committee meeting and two specific questions came up again that are appropriate for your company to provide potential answers instead of Chris Shillings comments to these and other issue of concern. Therefore, on behalf of the BRWC, I respectfully request The Carlyle Group provide the following:

- Would The Carlyle Group be willing to provide the Town or its utility entity a "First Right of Refusal", or other preferred legal mechanism from your company's viewpoint, to purchase the Apple Valley Ranchos Water Company in the future? As I have heard, the City of Missoula has a similar request regarding the Mountain Water Company in their community.
- Would The Carlyle Group provide the Town with a time frame for when you would be willing to negotiate a sale of the Apple Valley Ranchos Water Company? Having a preliminary time-frame would afford both Apple Valley and Missoula time to work out a financing and purchase program for all components of Park Water, at your designated time of disposition.

Personally, I have 50 years of experience in California water supply and management issues and I know this is a complicated and time-consuming process and I would appreciate The Carlyle Group affording the opportunity for the Town of Apple Valley to continue to discuss this process at your convenience.

Thank you for your cooperation, and on behalf of the Town, we look forward to working together.

Carl Coleman, Chairman

RECEIVED NO WRITTEN OR EMAIL RESPONSE