APPRAISAL SUMMARY STATEMENT
Town of Apple Valley, California
APPLE VALLEY RANCHOS WATER COMPANY

BASIS OF VALUATION:

The fair market value for the property proposed to be acquired is based upon an appraisal prepared in accordance with generally accepted appraisal principles and methodologies.

Code of Civil Procedure Section 1263.320 defines Fair Market Value as follows:

a) The fair market value of the property taken is the highest price on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy but under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available.

b) The fair market value of property taken for which there is no relevant, comparable market is its value on the date of valuation as determined by any method of valuation that is just and equitable.

Section 1263.330 provides that the fair market value shall not include an increase or decrease in value attributable to the project for which the property is to be acquired.

DATE OF VALUATION: The fair market value of the property was estimated as of March 24, 2015.

BASIC PROPERTY DATA:

Public use for which the property is to be acquired: To provide water service to the public currently within the Apple Valley, California service area currently served by Apple Valley Ranchos Water Company ("AVR").

Location and extent of property to be acquired: The Apple Valley Water System is located in San Bernardino County, California and serves the majority of the Town of Apple Valley and portions of the surrounding area. See the attached map of AVR's service area.

Interest to be acquired: All tangible and intangible assets (i.e., operating assets) used to provide water services within AVR's service area (i.e., the AVR Water System).

Zoning: Not applicable under CPUC jurisdiction.

Present use: Public water utility.

Highest and best use: Highest and best use is the most reasonably probable and legal use of a property, which is physically possible, appropriately supported, financially feasible, and that results in the highest value. The highest and best use of the AVR Water System is its current use—to provide water utility service.

VALUATION:

FAIR MARKET VALUE ANALYSIS: In a business valuation, two frameworks could be used—an accounting framework and an economic framework. The accounting framework uses financial data found in a water utility's financial statements. In contrast, the economic framework analyzes a utility's value added (or lost) as the result of earning profits above (or below) the industry's average. We used both frameworks in our analysis and they provided mutually supporting results.

There are three generally accepted approaches to estimating the value of property: (a) the cost (asset) approach, (b) the income approach, and (c) the market approach. Under the cost approach, the value of the property is based on the premise that an informed buyer would pay no more than the cost of producing a substitute property with the same utility as the subject property. Under the income approach, the value of the property is estimated by capitalizing or determining the present worth of the prospective economic benefits from the property. The market approach assesses value based on: (a) recent fair market sales of similar facilities under similar circumstances (i.e., merger and acquisition method), or (b) the capital market method (i.e., market prices of similar publicly-traded water utilities).

All three approaches—cost, income and market were considered in performing the appraisal.

THE FOLLOWING INFORMATION IS BASED ON THE ENTIRE PROPERTY:

1. The sales comparison approach is based on the consideration of comparable land and improved sales. In this approach, given the wide disparity in: (a) location of water utilities, (b) terms included in the sales (e.g., debt and equity financing), (c) size of the utilities, and (d) when the transactions occurred, the market approach was not relied upon.

2. The cost approach is based on the premise that an informed buyer would pay no more than the cost of producing a substitute property with the same function or utility as the Subject Property. When valuing public utility assets, five frequently used methods under the cost approach are considered. These are: (a) reproduction cost new less depreciation (RCNLD), (b) replacement cost new less depreciation, (c) original cost less depreciation (OCLD), (d) asset accumulation, and (e) rate base (i.e., the utility's operating assets and liabilities recognized by the California

Public Utilities Commission as being "used and useful" and "prudent" in providing service to the Company's customers).

The reproduction new less accumulated depreciation method provides the estimated cost to reproduce existing properties in their current form and capability at current cost levels, less depreciation. OCLD is defined as the original cost of the property when it was first put into service as a public utility, less accumulated depreciation. The replacement cost new less depreciation method provides an estimate of the cost to replace the existing facilities (either as currently structured or as redesigned to embrace new technology) with facilities that will perform the same functions. The reproduction and replacement cost new less depreciation methods were not used because they are both costly to implement and controversial.

The OCLD value is an estimate of the net book value of the property, which is used to determine the rate base value of public utility property for ratemaking purposes. The rate base method is being considered for purposes of evaluating fair market value and is estimated as follows:

Apple Valley Ranchos Water System
Estimated Rate Base
as of March 24, 2015

Description	Rate Base ($)
Net Plant in Service	86,491,033
Materials & Supplies	363,850
Cash Working Capital	2,267,680
Deferred Taxes and Tax Credits	-12,174,055
Construction Work in Progress	569,952
Contributions in Aid of Construction	-2,246,671
Customer Advances	-29,008,109
Total Rate Base	$46,263,680

3. Typically, the income approach estimates the value of the operating assets by: (a) capitalizing economic benefits derived from the assets (possibly

with or without a growth factor) and/or (b) using the enterprise discounted cash flow (DCF) method. This method is widely used in practice and reflects capital provided by both debt and equity owners. In this method, a discount rate is used for a discrete period (e.g., 10 years) and a terminal period (i.e., years 11 to infinity). The discount rate represents the risk associated with the future flows of economic benefits.

Under the enterprise DCF method, the direct economic benefits derived from continued ownership of the system are expressed in terms of free cash flow, which represents the total cash flow generated by the going concern that is available to the providers of both debt and equity capital.

The enterprise DCF model used to estimate the value of the AVR Water System is essentially an after-tax free cash flow model over a ten-year period beginning with fiscal year 2014 and ending with fiscal year 2023; and a terminal value. The calculation of free cash flow is illustrated as follows:

Annual Operating Revenues	
Less:	*Annual Operating & Maintenance Expenses*
Equals	*Earnings Before Interest, and Income Taxes (EBIT)*
Less:	*Cash Income Taxes*
Equals:	*Net Operating Profit Less Adjusted Taxes (NOPLAT)*
Plus:	*Depreciation and Amortization*
Equals:	*Gross Cash Flow*
Less:	*Gross Investment*
Equals:	*Operating Free Cash Flow (also Called Free Cash Flow to the Firm)*

The next table shows the calculation of the income value for the AVR Water System using the enterprise DCF method. Annual revenues and expenses, gross investment, and cash income taxes paid by AVR were projected based on data from a variety of reliable sources, including rate (and revenue) changes necessary for the Company to achieve its average earned rate of return on rate base of 7.56% for the five-year period (2009-2013).

Enterprise DCF
Valuation Summary ($000, rounded)

Row	Description	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	
1	Operating revenues		21975	22563	23589	24001	24436	24882	25344	25827	26325	26840	
2	Operating expenses		11720	11984	12254	12529	12811	13099	13394	13695	14003	14318	
3	EBIT		6978	7297	7499	7706	7928	8152	8383	8626	8875	9132	
4	Cash Inc. Tax		1310	994	1342	1444	1549	1655	1763	1874	1986	2101	
5	NOPLAT		5668	6303	6156	6263	6378	6497	6620	6752	6888	7030	
6	Gross cash flow		8664	9299	9701	9730	9771	9817	9870	9933	10004	10082	
7	Gross investment		-7378	-7378	-7382	-7387	-7391	-7395	-7399	-7403	-7407	-7411	
8	Free cash flow		1286	1921	2318	2343	2380	2422	2471	2530	2596	2671	
9	Terminal value												35107
10	Present value factor		0.929	0.864	0.803	0.746	0.693	0.644	0.599	0.556	0.556	0.556	
11	Value of operations	50595	1195	1659	1861	1748	1649	1560	1479	1407	1444	14486	
12	Value of other investments	0											
13	**Total Entity Value**	**50595**											

4. The following table summarizes the indicators of value developed for the Subject Property:

Apple Valley Water System
Summary of Indicators of Value
As of March 24, 2015

		Indicators of Value ($)
Cost Approach:		
	Rate Base	46,263,680
Income Approach:		
	Enterprise Discounted Cash Flow	50,595,427
	Economic Value Added	46,244,166
	Capitalized Income (no growth)	48,026,937
	Capitalized Income (.95% annual growth)	54,880,469
Market Approach		Not Relied Upon

The income approach reflects the going concern value of the AVR System as a whole, including all assets that are part of the System and used to provide water service to AVR's customers. The highest price for the AVR System that would be agreed to by a willing seller and willing buyer is equal to the value indicated by the income approach. If the prospective buyer were to pay an amount greater than the income value, the buyer would be unable to earn its desired return on invested capital.

From indicator of value for the enterprise (DCF) model listed above, we deducted 10% as the result of a marketability/liquidity discount.

Based on the results of the analyses described in this appraisal report, and the relative strengths and weaknesses of the indicators of value developed herein, the estimated fair market value of the AVR Water System is $50.6 million less $5.06 million or:

Estimated Fair Market Value as of March 24, 2015 $45,540,000

SEVERANCE DAMAGES

The AVR Waster System is a self-contained system. There are no identifiable severance damages or benefits.

TOTAL JUST COMPENSATION FOR ACQUISITION: $45,540,000

MAP OF AVR'S SERVICE AREA