

ORIGINAL

Decision No. 28595.

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

The City of National City,
a Municipal Corporation,

Complainant,

vs.

The Sweetwater Water Corporation,
a corporation,

Defendant.

Case No. 3475.

City of Chula Vista, a Municipal
Corporation,

Complainant,

vs.

The Sweetwater Water Corporation,
a corporation,

Defendant.

Case No. 3479.

In the Matter of the Investigation on
the Commission's own motion into the
rates; charges, service, rules, regula-
tions, classifications, contracts,
practices, and operations, or any of
them, of the water works owned and
operated by The Sweetwater Water Cor-
poration, a corporation operating in
the Cities of National City and Chula
Vista and vicinity, County of San
Diego, California.

Case No. 3534.

O.C.Ludwig, for complainant, City of Chula Vista.
J.A.Isaacson, for complainant, City of National City.
H.T.Sutliff, for various consumers.
Robert B.Burch, for Sweetwater Fruit Company.
Bacigalupi, Elkus and Salinger, by Charles L. Elkus
and Claude N. Rosenberg; Philip S.Thacher; and
Loveland Engineers, by Chester H. Loveland and
Fred M. Faude, for defendant The Sweetwater Water
Corporation.

WARE, COMMISSIONER:

OPINION

In this proceeding three cases involving the rates and

service of The Sweetwater Water Corporation have been consolidated. The Cities of National City and Chula Vista first complained that the rates are unjust and unreasonable, and that they produce an excessive return on the utility capital investment; and secondly generally assailed the service of the Corporation, charging in a supplemental complaint:

1. Defendant's failure to make promised improvements.
2. Inadequate pressure.
3. Filthy, unpalatable, unwholesome domestic supply.
4. Injurious irrigation supply.
5. Obsolete undependable equipment.

Thereupon, to broaden the scope of the proceedings, the Commission instituted its investigation upon its own motion into the rates, charges, service, rules, regulations, classifications, contracts, practices and operations of the utility involved.

Upon all these questions the defendant has joined issue, alleging that the rates in effect were established by the Commission, that they are comparable to those charged for similar service in other San Diego County localities, and that they fail to produce a reasonable return upon investment.

Historical Statement.

This water system was installed to serve a large subdivided area with water for domestic and irrigation purposes. It originated as a subsidiary and stimulus to an incorporated and prosperous land selling project. Being conducted and controlled for many years by the directors of this realty promotion, the water company found hard usage and in 1895 it passed through its first receivership. From successive ownership and managements it has grown in strength and value to its present status of a money-making utility. Characteristic of its origin, it is today one

of eight utilities owned and dominated by Western Utilities Corporation, a holding corporation.

Construction commenced in 1886 and in 1888 the Sweetwater Dam, a 30-inch transmission main on the south side of the Sweetwater River, and a distribution system had been completed and placed in service. In 1895 a 24-inch transmission main was installed on the north side of the Sweetwater Valley from the dam and connected with the distribution system.

Originally the dam was seventy feet high and the reservoir stored 18,000 acre feet of water. In 1895 the dam was raised five feet, and in 1911 another fifteen feet, to its present height of ninety feet. At this height the reservoir stored 36,000 acre feet. Natural flood deposits have reduced this storage to its present capacity of 29,000 acre feet.

The system obtains its water by impounding the surface flow of the Sweetwater River and its tributaries.

The dam is of the gravity arch type and is constructed of concrete and rubble masonry. The crest of the structure is 700 feet in length and the spillway lip is 110 feet above the lowest point of its foundation. It is located in a gorge of the Sweetwater River approximately four miles east of the easterly limits of the cities of National City and Chula Vista. Water at present is conveyed from the dam by two transmission mains, one, twenty-four inches in diameter, 27,029 feet long, and located on the north side of the valley; the other partly thirty-six and partly thirty-inches in diameter, 29,886 feet long, located on the south side of the valley. These two mains are connected to the distribution system consisting of 559,668 lineal feet of mains, varying in diameter from twenty-four inches to three-quarters of an inch.

The system embraces 5,060 services and supplies water

to a gross acreage of approximately 5,300 acres. Water is furnished for domestic, irrigation and commercial purposes. Within the confines of the complaining cities and adjacent unincorporated areas throughout the Sweetwater Valley, approximately sixty-six per cent of the company's gross revenue is produced from the irrigation deliveries, thirty-one per cent from domestic users and three per cent from municipal use. All of the water is measured and delivered under pressure.

The rates now in effect were established by this Commission in its Decision No. 20499, dated November 16, 1928, (32 C.R.C. 428) and are as follows:

Monthly Minimum Charges:

For 5/8-inch meter - - - - -	\$1.50
For 3/4-inch meter - - - - -	1.80
For 1-inch meter - - - - -	2.40
For 1 1/2-inch meter - - - - -	3.60
For 2-inch meter - - - - -	4.80
For 3-inch meter - - - - -	8.40
For 4-inch meter - - - - -	14.40

Monthly Quantity Rates:

From 0 to 1,000 cubic feet, per 100 cubic feet - -	\$ 0.30
Next 1,000 cubic feet, per 100 cubic feet - -	.18
Over 2,000 cubic feet, per 100 cubic feet - -	.18
Over 2,000 cubic feet, per 100 cubic feet (irrigation use only) - -	.06
Over 2,000 cubic feet, per 100 cubic feet (industrial use only) - -	.18

Fire Hydrants:

Each, per month - - - - -	\$ 3.00
Street and road sprinkling, per 100 cubic feet - -	.18
Minimum charge for each street sprinkling hydrant -	2.00*

* Commission's Decision No. 20499 fixed a three-dollar (\$3.00) charge but changed at the request of the company.

Prior to this proceeding The Sweetwater Water Corporation, or its predecessors, have been before this Commission four times, - always requesting and receiving increased water rates.

For supplemental details to the history and description of this water system reference is made to these four cases:

- I. App. 312, Decision 2802, October 2, 1915.
(8 C.R.C. 232)
- II. App. 3249, Decision 6236, April 24, 1919.
(16 C.R.C. 693)
- III. App. 6715, Decision 9514, September 14, 1921.
(20 C.R.C. 562)
- IV. App. 14195, Decision 20499, November 16, 1928.
(32 C.R.C. 428)

Heretofore it was never necessary for the Commission to find a rate base and fix rates determinative of a fair return upon such base. The instant proceeding renders this responsibility unavoidable for the first time.

In 1928, somewhat by agreement, a 20 per cent increase in water rates was ordered by the Commission. There seems to have been an implied understanding upon the part of consumers that if this increase were authorized, certain considerable improvements would be effected in water service.¹ As a matter

1. That the consumers in 1928 were led to believe the defendant would enlarge and improve its service following the 20 per cent rate increase is patent from the record.

Mr. Elkus of counsel for defendant read from the record of the 1928 Rate Case (32 C.R.C. 428) the commitment of Attorney Frank Austin, also of Counsel for defendant, relative to the correlation of the anticipated 20 per cent rate increase (which became effective December 1, 1928) and the contemplated additions and improvements to service unrealized to date. Mr. Austin:

(Tr. 1109) "We would not be justified, under the money market that has prevailed or is now prevailing, in making any hard-and-fast agreement that those improvements should be put into the order, as a condition that any rate increase would be granted, thereby making it obligatory upon us to make the improvements. We do not wish to appear here as making any such proposal. Now, we want to state to the consumers that is our intention to make the improvements." * * *

(Tr. 1113) "Now, as to the improvements, we intend to proceed with them as we have in the past year towards which we have expended for this purpose approximately \$100,000 out of the total of approximately \$1,000,000, and that has been done voluntarily without any rate increase being granted, and without any agreement with the consumers regarding any future increase."

(Tr. 1115) "Another point we desire to make clear is, that not all of the improvements contemplated by us are intended

of fact no appreciable part of these improvements have actually become effective. In that decision (32 C.R.C. 428, supra) it was indicated that the rates approved would produce a net return of 6.4 per cent on the estimated original cost as found by the Commission engineers, and 5 per cent on the reproduction cost less depreciation submitted by the company based on 1927 operations.

Service Factor

Preliminary to a determination of the major issues involved herein it is worthy of note that this proceeding was thoroughly if not exhaustively heard. Eighteen hundred and forty-four pages of transcript span the testimony of twenty days of hearing and numerous night sessions. Forty-six witnesses, some of them requiring days upon the stand, and thirty-nine exhibits, afford the testimony adduced during the six weeks required. It is neither necessary nor possible, within the limits of a decision, to discuss all the devious and strangely varying testimony with which this record bristles. Hereinafter we shall meet and conclude, in the order of their appearance in the record,

1. (Continued)

to be limited alone to the present consumers, but we intend also to increase our service area for the benefit of the community in general as well as for that of our present consumers. This rate increase of 20 per cent would by no means be adequate to provide for the financing of the projected improvements." * * *

(Tr. 1116) "This statement is made for the purpose of definitely placing into the record our position, in order that our consumers may have no doubt as to our sincere desire to cooperate with them to the uttermost extent in maintaining and improving the company's present high standard of service." * * *

(Tr. 1123) "We will make those improvements, Mr. Examiner", * * * "but we don't want any definite commitment in the order of the Commission."

The witness C. D. Eddy testified (Tr. 140) that the "agreement" of 1928 was induced by the threat of Mr. Rice, the company superintendent, "If we didn't enter into this agreement the rate would be raised very much more, and we would take it whether we liked it or not."

the major factors and subjects of controversy that require the consideration of the Commission. First of these is the service of the defending water company.

The protests and complaints of 28 consumers on the subject of service required the first four days. Their testimony varied only to the extent of their ability to describe conditions which, to them, were wholly unsatisfactory and displeasing.

The spacious auditorium of the Sweetwater Union High School was taxed to capacity with spirited and vehement protestants. Their testimony was characteristically vigorous and severe. Comment upon the testimony of a few will illustrate and suffice.

Mr. Oscar F. Weissgerber (Tr. 36, 37, 42, 43, 44, 62 and 65), City Engineer and Street Superintendent of Chula Vista, described the water as "black" and "filthy"; 3,000 feet of distribution mains in Chula Vista as having "just about reached the end of their usefulness", and the pressure as often seriously inadequate. He testified there were 200 breaks in mains within a two years period resulting in torn and obstructed streets and affording during the hours, and sometimes days, required in effecting repairs, no water for fire fighting in the easterly section of Chula Vista. Nearly a year before his testimony he notified the company to replace a troublesome pipe, with no avail. In one instance of aggravating and localized street leaks, he observed four patches in a piece of pipe twelve feet long. He has heard many and frequent protestations from householders against lack and total loss of pressure, rendering unavailable their toilets and bath tubs.

Mrs. Hal E. Hallett (Tr. 79, 82, 85) (and numerous others) offered convincing evidence that the water furnished their homes

was alive with exceedingly alert and numerous crustaceans, water fleas and cyclops, visible to the average eye.² She described it as full of mud, silt, rust and debris; all water used for cooking and the washing of teeth required preliminary boiling; and prolonged spells of filthy water rendered bathing difficult, unpleasant and infrequent.

Mr. Richard M. Allen (Tr. 99, 105, 111) described breaks on transmission main as occurring on a monthly average, necessitating stoppage of service ranging from a few hours to three days, and depicted the mains as being obsolete and ready for replacement.

Mr. B. C. Zackweiler, Chief of Division of Sanitation of San Diego County, disclosed through Exhibit 14 the presence of B Coli in the specimens of water examined. Dr. Alexander M. Lesem, Health Officer of the City of San Diego, "would assume from tests made of the water" pollution and contamination and said "the water would be regarded with suspicion." Dr. Carl Wilson, Bacteriologist and Technician in the defendant's employment for many years, admitted that when B Coli are found in such a supply the "water indicates a potential possibility it may carry disease."

Others brought forth from the system lengths of pipe,

2. Service.

144 members of The Olivewood Club and 25 members of The Friday Club (Federated Womens Clubs of National City) complained "of the quality of the water delivered by The Sweetwater Water Company, charging: First -- that it is unfit for drinking purposes because it contains living organisms large enough to be visible to the naked eye; because the bacteriological count is too high, (according to the County Health Officer) and because at certain seasons of the year it contains mud, silt, etc. Second -- That it is unfit for laundry purposes because the addition of chemicals (supposedly to kill bacteria) renders the water hard, and Third -- That it is, at certain seasons, unfit for bathing purposes because of the mud and silt that it contains.

"We ask that immediate relief be afforded us, inasmuch as many people are now buying bottled water to drink at a large expense; and also inasmuch as a much greater number, who are financially unable to buy bottled water, are compelled to drink this undesirable Sweetwater water; and also because our schools are supplied only with Sweetwater water and hundreds of children must daily drink this water or go without any -- either course endangering their health."

rotten with rust and holes and jammed full with roots; more than a score of colorful, odorous and organically infested samples of water were produced; a protesting petition signed by approximately 3,400 water users was filed; and the complainant witnesses assailed the service of the company generally and severely, and specifically attested to the five service charges embraced in the supplemental complaint tabulated in the first paragraph of this opinion. Frequent reference was made to the fact that every company manufacturing and selling bottled water within the service area of this defendant had been actively soliciting and doing business and that all consumers, financially able, purchased and used bottled water for drinking and cooking purposes.

Much of the protesting force was directed against the company for having allured the consumers into believing, prior to the rate increase of 1928, that comprehensive additions and betterments to the scope and quality of service would follow such rate increase. They complain bitterly of the non-fulfillment of these pledges. In this connection, we refer again to Footnote 1. The financial and economic calamity suffered since this rate increase, and the contemporaneous disappointment of the company patrons, afford us ample sympathy and understanding for both factions in this controversy.

It is likewise manifest that the irrigationists, who account for approximately 66 per cent of the business of this company, neither require nor could they practicably receive filtered water. The same transmission mains afford the supply for domestic, industrial and irrigation purposes. The irrigation rates would become prohibitive under a maximum development and refinement of service.

The company reposed its defense to service solely upon the shoulders of Dr. Carl Wilson, who testified at length of his wide experience in the technical and hygienic supervision of water

supplies. He considered the water in all ways suitable and safe for domestic purposes and discounted the multitudinous and disparaging complaints registered in the testimony. These he described as the natural and inevitable expression ever present in the ranks of patrons wherever water companies are concerned. His testimony presents a thesis from which he invites the conclusion that the service, pressure, volume and quality of the water afforded is comparable to that of any other trustworthy and commendable utility.

Taking the testimony on service far and wide, there is merit to the expressed grievances of these householders and patrons of domestic supply. We believe that the service of this company must be carefully watched in the future; that rotten and obsolete transmission and distribution mains should be replaced as soon as practicable; that at frequent and regular intervals all dead-end pipe lines should be flushed; that wherever practicable distribution mains be cross-connected to provide the most effective circulation of water; and that increased vigilance be practiced in the chlorination and purifying treatment of the waters.

The present deficient service justifies an appropriate reduction in rates. In determining their amount and spread, we shall endeavor to distribute the measure of reductions so that the greater benefits will enure to those consumers who suffer the greater annoyance from the existing service. The domestic consumers will enjoy the greater reduction. While improvements to service are desirable, the rate structure will not permit the necessary expenditure to effect the ultimate realization of improved service. The rate structure will permit vigilance and attention to the foregoing directions, and simultaneously affords a proper and an immediate relief in reducing rates, hereinafter referred to.

RATE BASE

Historical vs. Reproduction Values.

We believe historical rather than reproduction values should determine the rate base herein.

In this proceeding the company offered two estimates of cost of reproduction new and cost of reproduction new less depreciation, one by Peter A. Nenzel; the other by Edward R. Bowen. The Commission staff also prepared an estimate of cost of reproduction new and cost of reproduction less depreciation. These figures may be compared as follows:

	<u>Cost of Reproduction New.</u>	<u>Cost of Reproduction Less Depr'n.</u>
Bowen	\$3,112,990.	\$2,471,491.
Nenzel	2,950,763.	2,453,113.
Commission Staff	2,068,182.	1,316,726.

The company urges the use of the Nenzel figure for cost of reproduction new and the Bowen percentage of depreciation, developing a rate base in the following manner:

Rate Base:

Company

Reproduction Cost (Nenzel)	\$2,935,763.
Accrued Depreciation (79.39% condition)	<u>605,061.</u>
	\$2,330,702.
Land	487,983.
Organization Expense	15,000.
Franchises,	<u>5,000.</u>
	\$2,838,685.
Original Cost (Land at present market)	<u>2,542,560.</u>
(Divide by 2)	<u>\$5,381,245.</u>
Average	\$2,690,622.
Going Concern	200,000.
Water Rights	250,000.
Materials & Supplies	26,000.
Cash Working Capital	<u>10,000.</u>
Total	\$3,176,622.

There is an irreconcilable conflict between the reproduction estimates of the company and that of the Commission staff. Neither should be controlling in fixing a rate base in this proceeding.

The estimates of the company are based on unit prices as of 1927 on the theory that cost of reproduction must be considered in finding a rate base and that the costs used in such estimate should look to the future. The company contends that it is the avowed policy of the National Administration to raise prices to the 1926 level. Prices in 1927 were slightly below those of 1926. Therefore by the use of 1927 prices the company has given consideration to present low prices and the prices which may be expected to obtain in the future. This is wholly speculative and there is neither certainty nor indication that the Administration expects to bring construction costs to the level of 1926. Any commitments that have been made, and all of these commitments are made subject to change, have been intended solely to bring the general price level to that of 1926. It may be stated, in passing, that this hoped-for event is still awaiting a distant realization.

In detail, there are certain defects in the company's estimates that make them nebulous and too speculative as a basis for fixing rates.³

3. The record reveals many inaccuracies and discrepancies with reference to testimony on reproduction values. Following are among those appearing in the testimony of Engineer Bowen:

(a). (Tr. 1491, Walter W. Cooper):

"Q. Now, the result of your detail regarding concrete was \$10.25 and you used \$10.50 a yard, that is correct?

A. That is correct.

Q. What is that 25 cents per yard that you have added there intended to cover?

A. Well, after getting through I thought it would be better to round the figure out to \$10.50.

Q. For what reason?

A. Because I thought it more nearly represented the cost.

Q. You thought \$10.25 was too low?

A. Evidently, yes.

Q. What items entering into that \$10.25 did you feel were deficient?

A. Well, I don't know as I could put my finger on a specific item and say, "I think this item is deficient." Had I felt that way about it I would have changed the item. But I think that \$10.50 is all right."

(b). (Tr. 1494, Walter W. Cooper):

"Q. Would it make any difference in your figure if it should develop that the reinforcing used in the main dam, for example,

The company has a considerable mileage of distribution main constructed by the placing of a concrete coating around old steel pipe. This steel pipe had been in the ground, in some instances, since 1888, and required replacement.⁴

3. (Continued)

"was not new steel, but rather secondhand rail?

A. Yes, I think so.

Q. Do you know whether it is a fact that there is a considerable amount of reinforcing in the dam which is secondhand rail?

A. I could not tell you." (Second hand rail was used.)

(c). (Tr. 1503, Walter W. Cooper):

"Q. You can not give me the detail on the \$7.59 in the same manner, can you?

A. No, I can not. The detail that I have here amounts to a total of \$7.35 and I have used \$7.59."

(d). (Tr. 1518 and 1578)

The witness Bowen in relating his reproduction cost values stated that the same were based on values as of December 31, 1932, but all of his figures and calculations were read from a compendium prepared in 1927.

(e). (Tr. 1533)

Bowen's "reproduction of office equipment was \$17,000."

He admitted this figure included value of maps, and that said maps were made and paid for out of operating expense.

(f). An amazing conformity with the Nenzel figures is thus illustrated:

(Tr. 1540, Walter W. Cooper):

"Q. You are aware of the fact, are you, that every other account appearing in your Exhibit 34 your condition per cent is in precise agreement with Mr. Nenzel's condition per cent on every one of those accounts aside from those four you mentioned?

A. That appears to be the fact. I think that is perfectly all right."

(g). (Tr. 1533)

Bowen gives a 90 per cent condition to pipe 13 years old.

(h). (Tr. 1563)

Bowen gives a 60 per cent condition to pipe installed in 1888.

(i). (Tr. 1566)

Bowen gives a 95 per cent condition to meters.

4. Testimony John Edw. Cooper (Tr. 1026).

The pipe that was concreted was "approximately 29 years old. The company itself stated as to that pipe, * * * if it were not concreted it would be immediately renewed."

At the time replacement was contemplated, pipe costs were high and to avoid the purchase of new steel or cast iron pipe the company placed a concrete shell around this old steel pipe. In other instances such concrete shell was placed about steel pipe under streets then being covered with paving to avoid the possibility of having to renew these pipes within a few years after the paving of the street.

In applying prices to pipe of this kind, Mr. Nenzel assumed the concrete to be placed around steel pipe just as installed so that his cost includes new steel pipe plus a concrete shell. In depreciating such pipe he deducted 10 per cent for depreciation to account for the fact that the steel pipe was not actually new. Between various kinds of pipe treated in this way, but of the same size, there is considerable variation in price, although it was admitted that after being so treated one kind of pipe was no more valuable than another kind.

The Bowen method of pricing this pipe was to take one-half of the cost of the steel pipe in place and add to that the cost of opening a trench and placing the concrete shell around the old steel pipe, then covering it again. He admitted that this process resulted in paying for excavation and backfill one and one-half times. Messrs Nenzel and Bowen naturally agreed that such concrete pipe was much less satisfactory than new cast iron pipe, yet both of their methods produced costs for this pipe greatly in excess of the cost of new cast iron pipe.

Cost of reproduction is of little use or help in determining a rate base unless it is such a reproduction as a reasonable person would undertake. As was said by Mr. Justice Hughes (230 U.S. 352, 452) in the Minnesota Rate Cases "The cost of reproduction method is of service in ascertaining the present value of a plant, when it is reasonably applied and when the cost of reproducing the

property may be ascertained with a proper degree of certainty, but it should not justify the acceptance of results which depend upon mere conjecture."

The Sweetwater dam was constructed piecemeal over a period of 29 years and was of three types of material, i.e. grouted rock, rock masonry, and concrete. It was reproduced by the Company witnesses in their reproduction testimony exactly as it stands, notwithstanding their admission that if the dam were constructed today it most certainly would not be part masonry and part concrete. To reproduce this structure today in kind would be an extremely expensive and improvident procedure. Hence its reproduction value bears little, if any, relation to present value.

With respect to the Commission engineer's reproduction cost estimate, it was shown that certain items of property had been omitted. It was claimed that insufficient overheads were allowed. It was also claimed that 1932 prices were altogether too low for appropriate use in such an estimate looking to the future.

As may be seen, the testimony on reproduction cost less depreciation ranges from \$1,316,726. (Commission estimate) to \$2,471,491. (Company estimate). Obviously, both of these amounts can not represent present value, and it is probable that neither of them does.

Neither the estimates of the company nor the Commission with respect to reproduction cost of the dam should be determinative in fixing a rate base because they are both unsound and impracticable. Major consideration should be given to the historical cost of the property. With respect to historical cost, the company

estimated such cost, including land at present market values but excluding working capital and material and supplies, at \$2,542,560, and excluding land at \$2,054,577. The Commission staff estimated the historical cost, including land at original cost, at \$2,136,123.71, and excluding land at \$1,924,860.85.

In the 1921 proceeding Mr. Faude, then one of the Commission's hydraulic engineers, prepared an estimate of the historical cost of the Sweetwater property, totaling \$1,714,450. At the same time the company was offering its property and business for sale to an irrigation district for \$850,000. The decision (20 C.R.C. 562, 565, supra) indicated that a reasonable rate base lay somewhere between these two figures, the average, including \$9,000 for working capital, being approximately \$1,300,000. However, the rates fixed at that time were not correlated with any particular return on any given rate base, although the rates fixed were considerably below the rates sought.

In the 1928 proceeding Mr. William Stava, then and now a Commission hydraulic engineer, and a witness herein, took the historical cost prepared by Mr. Faude in 1921 and brought it forward to that date. The defendant company now contends that the Commission is committed to the use of the Faude appraisal brought down to the current date and criticizes the Commission staff for departing from the Faude figure and developing a figure on a new basis. Gross errors and discrepancies in the company records, both antedating and following the Faude estimate of 1921, were discovered by the present Commission staff in their recent research. These errors will suffice at this juncture to dispel the defendant's criticism of the course pursued in the instant case by the Commission witnesses.

The Commission's historical cost was derived by using the Mashet audit⁵ of 1913, plus book additions since that date, less certain excessive overheads charged to construction based upon bills rendered by the management corporation (Loveland Engineers, Incorporated).

The Commission's staff presented a statement of actual cost based upon an analysis of the books. A write-down of Capital in 1920 and a write-up of capital in 1927, each taking place at a time of transfer of the property, have been reversed. Also unreasonable charges from holding companies spread to capital by the present owner during the period 1927 to date have been omitted. This statement relies upon the sworn statements submitted to this Commission since the beginning of 1913. And the company in 1912 completed an elaborate audit of all its expenditures up to that date in order to arrive at an accurate statement of original cost as a basis for its 1913 and subsequent returns. Said statement of actual cost, including land, is \$2,136,123.71, and excluding land is \$1,924,860.85. From a study of the record in this matter we are convinced the actual cost of the property is very close to this amount.

5. At the request of the utility the Mashet Audit Company prepared and in 1911 completed an audit of expenditures to that date and in such manner determined the amount actually spent for capital. The amount so determined was presented by the company in its rate case of 1912 before the Commission (Application 312) as representing the original cost of the property (8 C.R.C. 234). The amount was brought forward to the end of the year 1912 and in such form was the amount submitted by the company in its first sworn statement to this Commission, at the end of 1912 as the actual cost of its property to that date. The net additions and betterments of subsequent years were added and in such manner the return has been made in the subsequent annual reports up to 1920.

(Testimony of John Edw. Cooper, Tr. 1101): The witness adopted Mashet audit because "it correctly represents the original cost of the property," and because "in 1912 the company submitted that figure to the Commission in its Annual Report, sworn to as representing the original cost of the property, and has continued to build up on that base the investment in this property from year to year, which investment has been reported to the Commission in its sworn reports as being the original cost of the property. I took those things into consideration in arriving at my conclusion."

Due consideration being given to each of these groups of figures, we arrive at the conclusion that the historical cost should be the fundamental basis in finding the rate base, and for this purpose a figure of \$2,000,000. will reflect our judgment. To this must be added land at its present market value.

Before determining land values and before disposing of the "intangibles," we pause in comment upon the methods used by the company in keeping records. Its records upon "Historical Cost" are illustrative. The 1926 estimate made by Mr. Faude, then in the employ of the company, in the sum of \$2,986,861.37 was written into the company's records in 1927, and this same figure is the amount shown for capital as of December 31, 1932. It is passing strange that the company does not point to this latter amount for historical cost but instead selects an estimate made by the Commission staff in 1920, and which brought up to date amounts of \$2,568,035., including land or \$2,054,577., excluding land, working capital and material and supplies.

We thus find this company ignoring the record of cost in 1927 in order to write⁶ into its records an estimated cost at an increase of almost a million dollars and in 1932 presenting another amount as historical cost some half million dollars lower. This situation is not surprising if books are to be kept by such approximate methods. Fortunately, they are not. This company has been filing under oath annual statements with this Commission since

6. (Tr. 355, John Edw. Cooper)

"In 1919 the company was transferred to the Sweetwater Water Corporation. At that time the capital was written down in the amount of \$97,162.55. This write-down was for the purpose of adjusting the assets with the purchase price of the property.

"In 1927, at the time the present corporation acquired property, that corporation wrote upon its books an amount for fixed capital determined by a valuation which resulted in a write-up of capital in the neighborhood of a million dollars."

1913. During that time the actual expenditures have been recorded in conformity with classification of accounts prescribed by this Commission. While most expenditures are specifically cared for in this classification, others, of more general nature, can be included in either capital or expense. The judgment of the officers must govern the allocation of such expenditures and their decisions must vary as time works its changes. The bold manner in which this company attempts to dispose of these records of actual cost, accounted for in the manner described above, and to substitute therefor first one and then another estimate indicates an ignorance of the value of records that cannot be excused. The books of this utility must be properly kept and entries must not be made therein to be later erased and ignored, but must reflect actual expenditures sincerely accounted for.

Land Values:

In determining values of lands, and rights of way, we have endeavored to arrive at the fair, present market value. The cities presented one group of witnesses, chief of whom was Frank Simmonds; the company another led by A. M. Fuller. Their conclusions present an amazing conflict and disparity in land values; the former aggregating \$149,851.45, the latter \$479,327.

Through a careful scrutiny of the methods and reasoning followed by these witnesses, and the apparent absence or presence of bias, we are compelled to accept, generally, the Simmonds conclusions. As to his values, we agree. Upon his determination of "operative" and "non-operative" lands, in some instances we disagree. We regard as "operative", (contrary to his "non-operative" conclusions) all reservoir marginal lands which he accurately valued

at \$9,883.50. We regard as non-operative (in accordance with his conclusions) four parcels, towit:

1. That certain lot in National City known and used as "The Dump" which affords the community a refuge for auto bodies, carrion and fresh garbage.
2. The vacant lot at Fifteenth and B Streets, National City.
3. Land at "Sweetwater Falls" located several miles above the reservoir.
4. "Judson Basin" lands aggregating 117.82 acres.

Each of these four parcels perform no utility function, useful or otherwise. The "Judson Basin" acreage, (reasonably valued by Simmonds at \$50 an acre - \$5,893.) was acquired since the 1928 rate case to afford an additional reservoir, and as a part performance of the 1928 avowed intention of the company to increase and improve its storage, pressure and service. If utilized for this purpose, the site would doubtless prove satisfactory, and its acquisition a justifiable increase to investment. But it has remained wholly undeveloped and useless and is today a rough, barren, hilly and rocky waste, without water, untilled and unoccupied.

Hence, we arrive at the acceptance of Simmonds Values applied to our conception of operative lands in the sum of \$141,458.45. He gave no estimate of rights of way values. We shall add to his land values the conclusion of the company witness Fuller for rights of way in the sum of \$8,656. Our total determination of the fair, present market value for operative lands and rights of way is \$150,114.45.

In embracing the Simmonds conclusions, to the exclusion of Fuller's, it is proper to observe that in every instance the

Simmonds values were founded upon sound and convincing reasons, and were supported by a satisfactory corroboration borne of other testimony and a careful inspection of the properties. His direct examination showed an impartial, diligent and reliable study of values. He was exhaustively cross-examined by Mr. Philip S. Thacher, of counsel for defendant, and a sage in realty values in San Diego County. It was this thorough and severe testing of the Simmonds conclusions that rendered his testimony on values wholly acceptable.

The company witnesses re-echoed the testimony of Fuller whose apparently defective preparation, and disproportionate range, lost the necessary credence which becomes convincing testimony.

Illustrated, Mr. Fuller finds himself in the record, standing somewhere along the northerly marginal lands of the Sweetwater Reservoir, and gazing southeasterly, over a vast stretch of water, approximately a mile in an air line to the abrupt marginal hills ascending into barren heights and affording the southeasterly section of the reservoir property. With no other approach, he evaluates this distant land, wholly without water and heretofore untilled, steep and practically barren, as worth \$250. an acre for the prospective cultivation of avocados. Equally unpersuasive is his estimate of the Judson Basin lands at \$250. an acre.

Intangibles:-

A. Water Rights.

B. Going Value.

(A. Water Rights): The company has claimed an addition of \$250,000 for water rights in the rate base. Nenzel testified to this figure. Bowen testified that the fair value of these water

rights was \$450,000. He admitted that no sum in excess of \$20,000 had ever been expended in the acquisition and protection of these rights.⁷ In his testimony (Tr. 1704) he stated: "The bare bones of the property included the water rights." In our foregoing analysis of historical value, we have accounted for and duly appraised the "bare bones." The outside allowance allowable for water rights is \$20,000., a sum which is supported by the record, and which we hereby find appropriate.

(B. Going Value): The company has claimed an addition of \$200,000 for going value. This is Nenzel's estimate. Again, Bowen was higher with the figure of \$225,000. Both figures may be analyzed with ease and readily vanish upon dissection.

Mr. Nenzel showed a lack of qualifications to justify any reasonably informed judgment as to going value.

Bowen's conception of going value in 1921, before the countryside had been aroused and inflamed over rates and service, was \$100,000. (Tr. 1608). We do not comprehend any reason for this strangely timed boost of 125 per cent.

It is noteworthy that both witnesses failed to show that anything had ever been paid on account of this intangible element. Bowen was admittedly employed by the company in rate proceedings in 1921 and 1928, and at a time when this property changed hands; yet in these vital transfers he appears to have lacked sufficient

7. (Bowen; Tr. 1377):

"It is doubtful if a total sum in excess of \$20,000 has been expended in the acquisition of these rights and their protection by the corporation or its predecessors."

(Bowen, Tr. 1384): "Broadly viewing the entire question and being mindful of the above discussion, particularly the record of values in the San Diego area, I am of the opinion that the developed water rights of the Sweetwater Water Corporation, situated as they are and under all the circumstances surrounding them, have a fair value of not less than \$450,000."

curiosity to ascertain, either the price paid by the purchaser, or the amount allowed for going concern. The decision of 1921 (20 C.R.C. 562, supra.) shows that the company was willing to sell the property at that time for approximately 1/2 of its estimated historical cost. Indeed, anything that could be said for "going value" at that time was extremely "intangible".

In disposing of this alleged factor we deem it timely to quote from the testimony of the witness Bowen:

(Tr. 1632-3) " * * * in dealing with a public utility property you are dealing with a property that is under the regulation of a regulating Commission and * * * dealing in a commodity which is essential to the habitation of the region so that it is not a question of volition on the part of the customers at all. It occurs to me that a customer is virtually compelled to take service from the company."

"COMMISSIONER WARE: Irrespective of service?

A. Well, to some extent.

Q. Irrespective of rates?

A. Well, I would think this. that in a community -- we will take a community like -- yes, like National City or some densely built-up community -- I have in mind the business district in San Diego or Los Angeles -- I would think that a consumer there, would be simply essential for him to take service no matter what the service was nor the price he had to pay for it; he just has to have it in order to carry on. Now, it is assumed, of course, and properly so, that both service and price of commodities, such as that sort and public utility service of that sort, his service is absolutely adequate -- is adequate and the rates are reasonable and proper, so that under that conception I do not see that good will enters into the picture at all."

The last sentence of the witness can neither efface nor soften his previous declarations which we have underscored. They deserve repetition in this opinion because they accurately and frankly reflect the defendant's regrettable conception of service and the correlation of utility and consumer. Mr. Bowen was absent during those days devoted to testimony affecting service, when the auditorium of the Sweetwater Union High School was crowded with protesting consumers. The chill of his testimony

on going value would have been agreeably tempered by the warming atmosphere of these occasions. The company should realize that its equipment, service, rates, and practices have been dangerously near the line of tolerance, and that one justifiable and highly sanctioned method of fixing rates revolves around the single proposition "reasonable value of the service rendered". While the conclusions reached in this decision are justified upon the other method of rate fixing, to wit: A rate designed to return unto the utility its operating expenses, depreciation, and reasonable return on "investment", the same conclusions are abundantly reinforced by the record's showing that they definitely afford "reasonable value of the service rendered". It is recommended that this utility hereafter conduct its enterprise consonant with the precept that the consumer is first entitled to satisfactory service and reasonable rates, from whence shall issue, secondarily, to the corporation a reasonable return. We are unable and unwilling to place any amount upon the "going value" of this utility in the fixation of rates.

Cash Working Capital, Materials, and Supplies:

The company claims an allowance of \$36,000. for these items. The evidence of the Commission was that the actual working capital requirements were about \$10,000., and for the last seventeen months the materials and supplies on hand have averaged a little less than \$22,000. a month. The \$36,000. company claim embraces a relatively large investment in pipe purchased in contemplation of additions that remain uninstalled. A reasonable deduction from the company figure appears in order, so that we are justified in allowing for "Working Capital, Material and Supplies" in the sum of \$35,000.

Therefore, we conclude that a rate base developed as

follows would be reasonable:

Physical Property - non-landed	\$2,000,000.
Land and Rights of Way	150,000.
Water Rights	20,000.
Cash Working Capital and Material and Supplies	<u>35,000.</u>
<u>Total Rate Base</u>	<u><u>\$2,205,000.</u></u>

Revenues:

The company estimates annual revenues of \$260,000; Stava at \$270,000. The revenue is to a considerable degree dependent upon climatic conditions. Rainfall and temperature are responsible for a considerable variation in the irrigation sales of the company. However, it is true that the domestic business is growing relatively as a source of revenue for this company.

Stava's estimate of normal revenues was supported as follows:

<u>Year</u>	<u>Actual Revenue</u>
1929	\$285,375.72
1930	269,859.87
1931	269,042.56
1932	<u>258,884.10</u>
Total 4 years	<u><u>\$1,083,162.25</u></u>
Average	\$ 270,790.

The company estimate by Kenzel was supported by these same four years together with an estimate of revenue for 1933 of \$225,000, resulting in an average over a five year period of \$261,632. a year. The company reports currently filed with the Commission reveal that the actual revenue for the first nine months of 1933 is but \$10,000 less than for the same months of 1932. Hence it would appear that Kenzel's estimate of \$225,000 for 1933 is too low. 1929 is said by the company to be a freak year. On the other hand, the succeeding three years are years of depression.

Looking into the future for a reasonable time it would appear that Stava's estimate of annual revenue amounting to \$270,000 is reasonable and proper. The Commission feels justified in adopting a figure between that of Stava and Nenzel, to wit: \$265,000. as a safe conception of annual revenue.

Operating Expenses:

The allowance for annual operating expenses claimed by the company is largely based on the testimony of the witness Nenzel. The total contended for is \$109,625. For the Commission, Stava estimated \$75,000. During the course of the proceedings the local taxes (San Diego and the City of Chula Vista), were increased slightly in excess of \$5,000. Stava's estimate of taxes was also deficient with respect to Federal Income Tax. The following tabulation shows the detail of the company's estimate of expense:

Expense:

1.	Source of Supply - - - - -	\$2,200.
2.	Pumping - - - - -	1,600.
3.	Purification - - - - -	2,300.
4.	Transmission and Distribution - -	19,500.
5.	Commercial - - - - -	6,800.
6.	General and Miscellaneous - - - -	29,800.
7.	Taxes - General - - - - -	24,300.
	Federal - - - - -	5,300.
	Capital Stock - - - - -	650.
8.	Uncollectible - - - - -	1,600.
9.	Extraordinary Expense - - - - -	13,774.
		<u>107,824.</u>
10.	Additional Rate Case - - - - -	1,801.
		<u>\$109,625.</u>

For purposes of decision the first five items above, totaling \$32,400, will be accepted.

"General and Miscellaneous Expense" as estimated by the company includes about \$11,000 as fees and salaries, drained from the utility by the management corporation. The total for this.

group of accounts as estimated by the company is substantially the amount charged to these accounts in 1932 and include certain expenditures objected to by Mr. Stava, such as dues to the National City, San Diego and Chula Vista Chambers of Commerce, San Diego Country Club membership, Community Chest contributions, dues and lunch expense to Rotary and Kiwanis Clubs, etc., as well as the billed detailed charges from Loveland engineers and the Western Utilities Corporation charge of 1 per cent of gross revenue. Loveland engineers' charges purport to be based on certain rates per hour for time spent by various Loveland employees in connection with the operation of the Sweetwater System, such as a "general officer" at \$9.375 an hour, senior engineers at \$6.25 an hour, assistant engineers at \$4.375 an hour, junior engineers at \$3.125 and clerical help at \$1.25.

Again for purposes of decision, after a full consideration of the foregoing, we shall allow for "General and Miscellaneous" expenses the rounded sum of \$22,000.

Local Taxes:

In the hearing Stava allowed for local taxes \$15,000. The company claimed \$22,200 (Exhibit 27, Page 21). At a belated hour in the hearing it appeared that San Diego County and Chula Vista had raised the company assessments, which necessitated the stipulation that the company should file its affidavit following the reception of testimony at San Diego, setting forth accurately the increase in local taxes as occasioned by said increased assessment. Thereafter, the Commission received the affidavit of Clayton B. Neill (spokesman for the company) dated September 1, 1933, wherein the sum of \$27,366.97 was claimed for total taxes upon the assumption that the same tax rate would apply. It appeared manifest that the effect of the Riley-Stewart Tax Bill

of 1933 would result in a different and lower tax rate.

The company, being apprised of this situation, on November 17, 1933, asked to amend the Neill figure to conform with the actual amount that comprises the local company tax for 1933-34. This sum is \$23,161.50. This latter figure admittedly includes approximately \$3,000 of escaped taxes which should not be allowed in computing our estimate for future local taxes. The company's commitment of November 17, referred to above, includes the company's estimate of normal taxes for the future based on present assessed values and existing tax rates in the sum of \$20,739.37. This amount will be allowed subject to elimination from this figure of taxes upon those parcels of land heretofore excluded from the rate base, as well as the taxes applicable to 14 cabins located at Sweetwater Lake and admittedly non-operative property. These exclusions aggregate \$187.13.

From the foregoing the final answer of this local tax problem brings us to the figure of \$20,552 which will be allowed for the company local taxes. It thus appears that \$3,748 is annually saved in local taxes and becomes available for rate reductions.

It is also patent that, were it not for the vigilance of San Diego County and Chula Vista in boosting the company's assessments during the late hours of this protracted hearing, an additional annual sum approximating \$6,000 would have been available to the consumers in rate reductions. While said County and City share the benefits resulting from these greater assessments, the rate payers of the Sweetwater Valley will bear the burden.

Federal Taxes: :

In the light of our determination of the reasonable amount estimated for "Revenues" (\$265,000) and Expenses (\$82,602),

the Federal Income Tax is found to be \$7,000. This is based upon the company's estimate of depreciation and other deductions used in its computation of Federal Income Taxes. Federal Capital Stock Tax will be allowed in the amount claimed by the company in the sum of \$650.

Uncollectible, and Amortization or Extraordinary and Rate Case Expenses are fixed at \$7,000. In adopting this figure, we accept the conclusions of the witness Stava. The company's contention of the sum to be allowed to cover these items is without reason or conscience. Illustrating, they urge \$27,204.91 to be amortized on account of their expenses incurred in these proceedings. Analyzing these gross demands, it appears that \$16,919.04 is claimed for "engineering services and expenses". No rate proceeding of this magnitude should cost the consumers any such sum. If the company wishes to conduct such extravagant proceedings the cost of their conduct should be borne by the stockholders and not by the rate payers.

Summarizing and concluding our determination of Expense the following tabulation reveals our judgment:

Expense:

1. Source of Supply - - - - -	\$2,200.
2. Pumping - - - - -	1,600.
3. Purification - - - - -	2,300.
4. Transmission and Distribution - - - - -	19,500.
5. Commercial - - - - -	6,800.
6. General and Miscellaneous - - - - -	22,000.
7. Taxes - General Local - - - - -	20,552.
Federal Taxes - - - - -	7,650.
8. Uncollectibles and Amortization of Extraordinary and Rate Case Expense	<u>7,000.</u>
Total	<u>\$89,602.</u>

Depreciation Expense.

The company estimated depreciation expense on a 5 per cent sinking fund basis at \$18,000. a year. Mr. Travis, of the Commission's staff, estimated depreciation expense on the 6 per cent sinking fund basis at \$12,615. a year. Neither estimate may be viewed with entire satisfaction. There is some merit to the company's criticism of Mr. Travis' estimate, in that his estimated lives (using the sinking fund basis) were computed by accounts rather than on the varying lives of the groups of property entering into those accounts. Under existing circumstances and for purposes of this decision, being mindful of the large investment in the dam and transmission lines, we deem an allowance of \$17,000. to be reasonable for depreciation expense on a sinking fund basis. The company will be expected and required to conform its depreciation accounting to the 5 per cent sinking fund method, augmenting the reserve by adding to it interest at the rate of 5 per cent per annum on the balance in the reserve.

Rate of Return.

The company, on brief, made no claim for any specific rate of return, merely arguing that the amount now being earned by the company is less than the sum to which it is legally entitled.

For the company, the witness Faude presented an exhibit showing the cost of money to be 6.72 per cent, and Gilbert W. Smith, investment banker, also a witness for the company, testified with respect to the present day costs of obtaining money, if as a matter of fact money could be obtained at any price by this company, and the prices at which the company's bonds are now selling.

Mr. Stein, of the Commission's staff, in Exhibit No. 15, showed the effective rate on moneys which the company now has borrowed to be 5.86 per cent.

The Faude Exhibit on cost of money is faulty in several particulars. It includes all the issues of bonds of predecessor companies about which he was able to obtain information, despite the fact that all of the predecessor company bonds have been retired. It also assumes the existence of an issue of preferred stock at an estimated cost of 6.82 per cent, though this issue of stock has been retired. It includes the present bonded indebtedness of the company, but assumes a discount of 6.5 per cent in connection with its issuance. The books of the company reflect no such discount, as these bonds, together with the company's preferred and common stock, were issued on a par basis in exchange for property of the predecessor company, Sweetwater Water Corporation. It is worth noting in the Faude Exhibit (No. 35) the preferred stock issued with an assumed discount of 12 points and a net cost of 6.82 per cent was called within one year after its issue and a premium of 5 points paid with the proceeds of a note issued to the Western Utilities Corporation, bearing interest at 7 per cent. In other words, The Sweetwater Water Corporation paid a premium of 5 per cent and is now paying 7 per cent to the holding company for money which it had obtained through the issuance of 6 per cent preferred stock, a clear loss to the operating company and an unwarranted gain to the holding corporation.

Under the conditions here present, which are set out at some length in this opinion, the Commission is not justified in disregarding entirely the value of the service to those obliged to make use of it. Weight must be given to this factor, even though it reduces the rate of return to a point somewhat lower

than might be considered reasonable if the service were not so unsatisfactory. The rates to be prescribed herein are deemed to represent the full worth of the service. They will effect a reduction in revenue of approximately \$27,000., leaving an earning of slightly more than six per cent on the rate base.⁸ This return is somewhat in excess of the cost of money to the company and will enable the company to meet fixed charges on its bonds, interest on loans from the holding corporation, 5 per cent interest on the balance in the depreciation reserve, and more than 5 per cent on its common stock. This earning, moreover, may be augmented by reductions in expense under those set out and allowed in this opinion through practice of justified economies.

The following form of order is recommended:

O R D E R

The Cities of National City and Chula Vista having complained against the rates of The Sweetwater Water Corporation and having applied to the Railroad Commission for an order fixing lower rates, and an investigation having been made by this Commission into the rates, charges, services, rules, regulations, classifications, contracts, practices and operations of said corporation and its water works, public hearings having been held thereon, the matter having been argued orally and by briefs, and submitted, the Commission being now fully advised in the premises,

8. The use of an undepreciated rate base requires that the expense of depreciation be computed on the sinking fund basis. If a depreciated rate base were used depreciation expense must be allowed on the so-called straight line basis, which is substantially higher than the sinking fund allowance. On the other hand a depreciated rate base would be materially below the sum found reasonable herein for the testing of future rates. Tested on this alternative basis the return which the company will receive under rates here fixed will approach 6½ per cent on a reasonably depreciated rate base.

IT IS HEREBY FOUND AS A FACT that the rates now charged by The Sweetwater Water Corporation for water supplied to its consumers are unjust and unreasonable in so far as they differ from the rates herein established and that the rates herein established are just and reasonable rates to be charged for such service, and basing its order upon the foregoing findings of fact and upon the statements of fact contained in the opinion preceding this order,

IT IS HEREBY ORDERED that The Sweetwater Water Corporation be and it is hereby directed to file with this Commission, within thirty (30) days from the date of this order, the following schedule of rates to be charged for all water delivered to its consumers subsequent to the thirty-first day of December, 1933:

Monthly Minimum Charges:

For 5/8-inch meter	- - - - -	\$1.25
For 3/4-inch meter	- - - - -	1.50
For 1-inch meter	- - - - -	2.00
For 1 1/2-inch meter	- - - - -	3.00
For 2-inch meter	- - - - -	4.00
For 3-inch meter	- - - - -	7.00
For 4-inch meter	- - - - -	12.00

Each of the foregoing "Monthly Minimum Charges" will entitle the consumer to the quantity of water which that monthly minimum charge will purchase at the following "Monthly Quantity Rates."

Monthly Quantity Rates:

From 0 to 1,000 cubic feet, per 100 cubic feet	- -	\$.25
From 1,000 to 2,000 cubic feet, per 100 cubic feet	- -	.15
Over 2,000 cubic feet, per 100 cubic feet, for irrigation use	- - - - -	.05-3/4
For use above 2,000 cubic feet, per 100 cubic feet, for other than irrigation use	- - - - -	.15

Fire Hydrants:

Per month, each	- - - - -	\$2.00
For street and road sprinkling, per 100 cubic feet	- -	.15
Minimum charge for each sprinkling hydrant	- - - - -	2.00

For all other purposes, the effective date of this order shall be twenty (20) days from and after the date hereof.

The foregoing opinion and order are hereby approved and ordered filed as the opinion and order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 1st day of December, 1933.

C. C. Seamy
Leon O. Whitell
W. A. Cunn
W. B. Harris
W. H. Moore
Commissioners.