

Decision No. 42516

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
California Water Service Company,
a corporation, for an order
authorizing the establishment of a
new rule and regulation governing
water main extensions.

Application No. 29535

In the Matter of the Application of
San Jose Water Works, a corporation, for
an order authorizing the establishment of
a new rule and regulation governing water
main extensions.

Application No. 29536

McCutchen, Thomas, Matthew, Griffiths & Greene,
by Robert Minge Brown, for applicant; Edward C.
Watson, for San Mateo Airport.

MITTELSTAEDT, COMMISSIONER:

O P I N I O N

California Water Service Company and San Jose Water Works, each of which is a corporation, are engaged in rendering public utility water service, the former in 21 separate service areas^{1/} in the state, and the latter in the city of San Jose and environs. By separate application each of these water utilities has asked this Commission for authority to file a rule and regulation governing water main extensions different from and in certain respects more restrictive than that now filed by each.

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The 21 service areas or districts of California Water Service Company comprise the following localities in the state: Atherton, Bakersfield, Broadmoor (San Mateo County), Chico, Concord, Crockett, Danville, Dixon, East Los Angeles (Belvedere), Hanford, Hermosa Beach, Livermore, Lomita Park, Los Altos, Martinez (wholesale), Marysville, Menlo Park, Oroville, Petaluma, Port Chicago, Port Costa, Redondo Beach, San Carlos, San Mateo, South San Francisco, Stockton, Valona, Visalia, Walnut Creek (wholesale), Willows, and Woodside.

For purposes of hearing and decision, these matters were merged and a public hearing was held in San Francisco.

For a period of years prior to March 29, 1945, these two utilities were related to the extent that effective corporate control of each was vested in General Water, Gas & Electric Company; however, on that date the latter holding company divested itself of its entire interest in each of these utilities, and at the present time their stock is widely held throughout the United States.

California Water Service Company, in its 21 districts, at the end of 1947, owned 1,755 miles of mains and served a total of about 126,600 water consumers. In addition, this company delivers water at wholesale to the cities of Martinez and Walnut Creek. As of the close of 1947, San Jose Water Works served about 35,700 consumers in the city of San Jose and environs, and owned 507 miles of mains.

The main extension rules presently filed by the two utilities are identical in content and became effective on the same date, February 15, 1946. Prior to the filing of the existing uniform rule, California Water Service Company had several different extension rules, such rules in most instances having been carried over from predecessor companies.

Applicants' present uniform rules were filed as a result of the recommendations of this Commission in Case No. 4701, an investigation on the Commission's own motion into the rules and regulations of water utilities. The present rules provide basically that each bona fide individual consumer, to the extent necessary to serve, shall be allowed a main extension of 100 feet to be constructed entirely at the expense of the utility, the estimated cost of extensions beyond such so-called free allowance or free footage to be advanced by such individual consumer, based upon mains not

larger than four inches in diameter; and that such advances shall be subject to refund without interest over a ten-year period upon the basis of subsequent connections of bona fide consumers to the subject main extension at the equivalent cost of 100 feet of main per service connection. The existing rules also provide for the cost of main extensions to serve real estate subdivisions to be advanced in entirety by the subdivider, with refunds of such advances within a ten-year period based upon either the equivalent cost of 100 feet per bona fide consumer connection, sometimes referred to as the proportionate cost method, or 35% of the gross water revenues arising from the use of such extension, sometimes referred to as the revenue method, whichever refund method the subdivider may elect. The present rules contain other incidental provisions which need not be recited here.

The main extension rules are identical in content as proposed by both applicants but they differ from the existing rules in several respects. The proposed rules reduce the free footage from 100 to 75 feet for each bona fide new individual consumer and advances made for extensions in excess of such free footage are to be refunded without interest over a ten-year period upon the basis of subsequent connections to such main extension at the equivalent cost of 75 feet of main per service connection. The proposed rules with respect to real estate subdivisions provide that refunds to subdividers shall be based upon 75 feet instead of 100 feet per connection, or upon 30% instead of 35% of the gross water revenues arising from the use of the extension, the method of refund to be selected by the subdivider. The rules further predicate the amount of advance upon the estimated cost of a main not larger than four inches in diameter, in the case of extensions to serve individuals, and upon the estimated cost of the size and length of main decided on by the utility in real estate subdivisions. Provision

also is made for an additional deposit not in excess of \$100 per consumer which may be required at the option of the utility, where free footage has been allowed for two or more consumers to be served by a single extension regardless of whether an advance was made, such deposit to be refunded if a bona fide connection is made within 120 days; otherwise, it is to be applied to reimburse the utility for free footage laid, subject to refund.

Applicants requested, if this Commission should authorize the filing of their proposed main extension rules, that they be made effective not later than 30 days after the Commission's order, and further that the new rules be made to apply to all main extensions on which actual construction will have commenced on or after the effective date of the rule. Applicants indicated that on all subdivision extension agreements submitted for execution after September 1, 1948, they have added a paragraph calling the attention of subdividers to the pendency of this proceeding before the Commission. Upon questioning, witnesses for both applicants maintained that their respective construction schedules had not been modified or affected because of their applications before the Commission.

At the hearing applicants presented considerable testimony and a number of exhibits in support of their request. Excerpts from main extension rules of several municipal water utilities and water districts were introduced, permitting comparison with applicants' proposed uniform rules. Of the ten publicly-owned utilities listed, it was pointed out that three allow no free footage and charge the consumer or real estate subdivider for the entire main extension, as well as for service, without refund. One city water department requires a flat advance of \$100 per connection outside the city limits, without refund except in the event of annexation. Another city water department provides an unrefundable levy for a water connection, the amount dependent upon the front footage of the lot, and

further collects advances for extensions in excess of 200 feet, subject to a maximum of 50% refund. The remaining five examples cited reflect more liberal allowances than above, with the most liberal giving a free footage of 150 feet and providing for immediate refund of the full amount advanced for excess footage if, at any time within a 15-year period, the annual revenue exceeds 20% of the cost of the entire extension.

Applicants each presented a computation showing the amount of free footage that would result from the assumption that the proper dollar allowance should be based upon parity on the part of new consumers with existing consumers in terms of average ratio of investment in distribution mains to annual gross revenue. Using data as recorded for the years 1945, 1946, and 1947 on end-of-year investment in distribution mains and annual gross revenue, California Water Service Company obtained an average ratio of \$2.50 of investment for each \$1 of gross revenue. Multiplying the recorded average annual revenue of \$31.42 from metered residential consumers by the 2.5 ratio yielded an alleged justifiable company investment or free allowance of \$78.55, which is equivalent to the installed cost of slightly over 40 feet of four-inch main. This equivalent footage was computed on the basis of an average unit cost of \$1.95 per foot installed, which was determined from the actual amounts of various kinds of four-inch pipe laid in 1946, adjusted to 1948 cost levels. San Jose Water Works, in a similar manner, showed an average ratio of investment to revenue of 3.0, an average annual revenue per consumer of \$32, and a unit cost of four-inch pipe installed of about \$1.70 per foot, yielding an alleged justifiable free allowance of \$96, which is equivalent to the installed cost of slightly over 56 feet of four-inch main.

In support of applicants' proposal that the revenue basis of refund (applicable to real estate subdivisions only) be reduced

from 35% to 30% of gross revenue, there were submitted computations purporting to show the approximate return on the over-all investment per consumer, including the maximum investment in distribution mains that could be fully refunded in a ten-year period, under each of these percentages. These computations were predicated upon the current average annual revenue from metered residential consumers and upon total investment per consumer, excluding distribution mains and hydrants and intangibles, to which was added the maximum investment in distribution mains that could be fully refunded in ten years, determined as the average annual revenue divided by each of the revenue basis refund percentages. Reducing current operating and maintenance expenses, taxes, and depreciation to a unit cost per consumer, applicants showed incremental rates of return on the two revenue basis refund percentages. California Water Service Company showed a 3.5% incremental return on the 35% basis and a 3.8% return on the 30% basis, whereas the comparable results for San Jose Water Works were 4.4% and 4.7%. It was brought out that these incremental rates of return on the proposed 30%-of-revenue refund basis, although higher than on the 35% basis, were still lower than the respective system-wide rates of return. It would appear that these computations allow applicants a return on the full investment in distribution mains, whereas in reality this amount would be advanced by the subdivider and would then be refunded in equal annual amounts over the ten-year period. Accordingly, it is concluded that the investment base should include only half this amount for distribution mains, whereupon California Water Service Company would show rates of return of 4.8% and 5.1% for the 35% and 30% bases, respectively, and San Jose Water Works would show rates of return of 5.8% and 6.1%, respectively.

Applicants supplied certain experience data in support of their request for authority to collect a deposit of not to exceed

\$100 per consumer in cases where free footage is to be allowed two or more prospective consumers in computing the advance required on a single general extension, which deposit allegedly is desired to protect the utilities from failure of prospective consumers, for whom free footage is allowed, to make connection within a reasonable time after completion of the main extension. California Water Service Company submitted for each of its service areas the footages and corresponding costs of main laid at company expense due to such failure of prospective customers for which free footage had been allowed, which totaled about 7,000 feet and \$12,500 for the year ended June 30, 1948. San Jose Water Works during the same period showed corresponding figures of about 400 feet and about \$500.

As an indication of the magnitude of the capital outlay required of applicants under their present main extension rules, it was testified for California Water Service Company that 37% of the total capital added to the system in 1947 was for free extensions, which amount was equal to about 190% of the company's net income in that year. A witness for San Jose Water Works estimated that free extensions during 1948 would amount to about 120% of net revenue for that period.

Cross-examination brought out that very few real estate subdivision extensions would not be fully refunded as a result of the proportionate cost or free footage basis of refund as proposed, and applicants produced evidence showing that on the average, under the present rule, only fractional occupancy of a subdivision sufficed to refund the full amount of the advance upon the proportionate cost basis. It was pointed out that very few subdividers elect to have their advances refunded upon the revenue basis.

Asked why four-inch main was used in computing justifiable length of free footage rather than smaller-sized pipe, applicants answered that in their opinion the weighted average diameter of distribution mains now installed would in fact exceed four inches.

As a further criterion of parity between existing and prospective consumers with respect to main extensions, in addition to the investment-to-revenue ratio basis previously discussed, applicants submitted ratios of average length of distribution main per consumer as actually experienced. California Water Service Company at the close of 1940 showed 79.1 feet, this ratio diminishing to 68.7 feet at the end of 1947. Corresponding ratios of average length per consumer for San Jose Water Works were 73.4 feet and 74.1 feet.

The data of record in this proceeding permit yet another approach to the problem of ascertaining a proper free footage allowance. Assuming for this purpose that for a particular main extension no increases in capital other than distribution mains will be necessary, what may be termed the incremental cost basis yields results somewhat higher than the calculations of applicants. This method, in effect, gives the investment that could be supported by the net revenue currently realized by applicants, or the net revenue (expressed as the ratio of net revenue per dollar of gross revenue) capitalized. In ascertaining this net, taxes and depreciation are excluded from expenses, as these are a function of net revenue. From the record it is deemed proper to express taxes as $1\frac{1}{2}\%$ and depreciation as 3% of this net revenue before taxes and depreciation, and adding thereto 1% for maintenance and operation expenses and $5\frac{1}{2}\%$ as a tentative reasonable return on the investment, a total of 11% is obtained to use for the purpose of capitalizing the net revenue. For the year 1947, California Water Service Company realized gross revenues of \$4,808,620 and incurred expenses of \$2,576,610 excluding taxes and depreciation, yielding a net revenue of \$2,232,010 or a ratio of 46.4% net per dollar of gross revenue. Capitalized at 11% this yields a supportable investment of \$4.21 per dollar of gross revenue, or multiplied by the average revenue

per consumer of \$31.42 and divided by the average cost per foot of main of \$1.953, an equivalent free footage of 68 feet is obtained. San Jose Water Works in 1947 showed gross revenues of \$1,360,772, expenses excluding taxes and depreciation of \$506,090, giving a net of \$854,682 or a ratio of 30.628. Capitalizing this at 11% gives \$5.71, and multiplying by \$32, average revenue per consumer, and dividing by \$1.703, average cost per foot of main, yields 107 feet of free footage. It is apparent that under this criterion, wherein justifiable free footage is a direct function of net revenue, the question is implicit as to whether the desired end is to be reached by changing the free footage allowance or by changing rates.

Applicants' computations of justifiable free allowance on the investment-to-revenue basis, wherein California Water Service Company arrived at 40 feet and San Jose Water Works 56 feet, although mathematically accurate, would imply that, to qualify for free extension, new service areas would need to have consumer density much higher than the remainder of the system which has reached its present consumer density only after many years of development. Surely a new utility enterprise would not expect to attain such a high consumer density until well after the close of what might be considered the developmental phase of its operations, if ever. The question might well be raised in this connection as to possible discrimination between the utilities' original consumers and their prospective consumers.

Although still subject to the limitations just discussed, it would appear that a similar and perhaps somewhat more meaningful computation could be made by taking the average distribution main capital per consumer for the years 1945, 1946, and 1947 (same periods used by applicants) without bringing in revenue at all, and converting such unit capital to footage of free allowance by use

of the 1948 level of costs. This would yield 48 feet instead of 40 for California Water Service Company and 67 feet instead of 56 for San Jose Water Works.

The computations submitted by applicants in support of reducing the percentage under the revenue basis of refund to real estate subdivisions from 35% to 30%, adjusted to reflect in capital only one-half of the cost of extension as previously discussed, showed that the incremental rates of return on the 30% basis on such business were 5.1% for California Water Service Company and 6.1% for San Jose Water Works, both such percentages being 0.3% higher than yielded by the 35% refund basis. Although the end result of these computations would appear to yield not unreasonably high rates of return, their significance is questionable for the reason that the level of rates as reflected in the computations is so critical in the end result. It is impossible to conclude from the computations whether the present percentage under the revenue basis of refund should be changed or the rates changed.

It would appear that the most direct approach to the determination of footage allowance would be to take the system average footage of distribution mains per consumer as the criterion, 69 feet for California Water Service Company and 74 feet for San Jose Water Works as of the end of 1947. Ascertaining justifiable free footage by this means has the advantage of being in no way affected by the level of rates, which are properly not within the scope of this proceeding. These system average footages per consumer reflect for the most part fairly well built-up areas, the present consumer density of which was reached some time after the original main installation. It is acknowledged that the development of a real estate subdivision usually is concentrated into a relatively short period, and its ultimate consumer density for all practical purposes is reached within ten years, which would be

within the refund period. Extensions to serve individuals, however, can be expected to increase in consumer density quite materially over a considerable period of time, generally not reaching their ultimate density until after the ten-year refund period. From this difference in consumer connection characteristics, it appears that a different treatment of extensions to real estate subdivisions and of extensions to individuals is justified, in so far as footage allowance is concerned. Accordingly, it is concluded that the present system average footage per consumer would be appropriate to use for real estate subdivisions, where ultimate density is closely approached within the ten-year refund period, but, for extensions to individuals, where ultimate density is often not reached until after a ten-year period, that additional footage be allowed.

In view of the similarity of each of the applicants' figures on average footage per consumer, and the desirability of uniformity between utilities whenever practicable, a footage allowance for refund purposes of 75 feet per consumer in real estate subdivisions is deemed proper for each of the applicant utilities herein, and the order will so provide. Relative to extensions to serve individuals, in consideration of material increases in consumer density which reasonably may be anticipated after the ten-year refund period, a footage allowance of 100 feet per consumer will be ordered.

As to the request of applicants to reduce the refunds to real estate subdividers under the revenue basis from 35% to 30%, it is concluded that the results under the 35% basis are not unfair to the utilities, and, accordingly, no change in this percentage will be ordered.

The request for authorization to collect a deposit from each prospective consumer, at the option of applicant utilities, to

assure prompt connection of service as described heretofore where free footage has been allowed two or more prospective consumers in a single extension, is deemed to be reasonable and needed to protect the utilities. However, it is concluded that the deposit amount of not in excess of \$100 per consumer as requested by applicants would be excessive and would place an undue burden on the prospective consumer. It is accordingly concluded that \$50 will be adequate to secure the needed protection, and, to avoid any possibility of discrimination, that the collection of the \$50 deposit should be made mandatory upon the utilities with respect to all such prospective consumers. It is deemed appropriate that each prospective consumer having made a deposit hereunder be protected against retention of his deposit by the utilities for an unduly long period. This will be accomplished by adding a provision to the rule requiring the return of the deposit on demand in the event of an unreasonable delay in completing the extension from which service is to be secured. In case of disagreement between utility and consumer as to the unreasonableness of the delay, the matter may be presented, to this Commission by either party for settlement. The rule to be ordered will reflect these provisions.

The following form of order is recommended:

O R D E R

Good cause appearing, IT IS HEREBY ORDERED that California Water Service Company and San Jose Water Works be and they are authorized to file with this Commission, effective on the effective date of this order, the rule and regulation appended hereto as Exhibit A, applicable to all water main extensions applied for on or after the effective date of the rule.

RULE AND REGULATION

No. WATER MAIN EXTENSIONS

4. General Extensions:

(1) The Company will extend its water distribution mains to new consumers at its own expense when the required total length of main extension from the existing facilities is not in excess of 100 feet per service connection. If the total length of main extension is in excess of 100 feet per service, the applicant or applicants for such service shall be required to advance that portion of the reasonable estimated total installed cost of such extension over and above the estimated total installed cost of the said 100 feet of main per service; provided, however, that in no case will the above estimate be based upon a main in excess of four (4) inches in diameter. The money so advanced will be refunded, without interest, upon the basis of the total installed cost of 100 feet of main for each additional bona fide consumer directly connected within a period of ten (10) years from the date of completion of the extension for which advance has been made, but in no case shall the total refund exceed the original advance without interest. Adjustment of any difference between the estimated and the reasonable actual total installed cost will be made after completion of the installation.

(2) In the case of a single extension made pursuant to applications by two or more applicants under Section A (1) of this rule, in which the Company has made a per-service footage allowance in computing the advance required, the Company shall require the applicants to deposit with the Company cash security, in the amount of \$50 per service connection, to insure that each service for which footage allowance has been made will be in fact utilized by a bona fide consumer upon completion of installation of the extension. Upon establishment of service connection to an applicant hereunder, or upon receipt by the Company of written verification from the applicant to the effect that his facilities are ready for connection, within one hundred twenty (120) days after completion of the main installation, the full amount of the security deposit shall be subject to immediate refund without interest; however, failing such service connection within this period, the Company may reimburse itself from such security deposit for the cost of the footage allowance theretofore made in respect of such service. Any amount used by the Company in such reimbursement shall become an amount subject to refund in accordance with the provisions of Section A (1) hereof. In the event of an unreasonable delay in the completion of a main extension hereunder, the Company will, upon demand by any depositor, return the full amount of the cash security deposit to such depositor, and concurrently the Company will tender the return of security deposits to all other depositors involved in the prospective single main extension, together with all amounts advanced for construction, whereupon the extension agreement will be terminated. In case of disagreement between the Company and an applicant or applicants hereunder as to the unreasonableness of the delay, the matter may be presented to the Public Utilities Commission of the State of California by any of the parties for settlement.

No extension advance will be required from an applicant requesting service from a main already in place.

The footage allowance installed at Company expense will be installed only for the benefit of a bona fide consumer as defined by the terms of this rule.

RULE AND REGULATION

No. WATER MAIN EXTENSIONS (Continued)

B. Extensions to Serve Subdivisions, Tracts or Housing Projects:

Applicants for main extensions to serve subdivisions, tracts or housing projects shall be required to advance to the Company before construction is commenced the estimated reasonable total installed cost of the necessary facilities exclusive of service connections and meters. The size, type and quality of materials and location of the lines shall be specified by the Company and actual construction will be done by the Company or by a contractor acceptable to it. In case of disagreement over size, type and location of the pipe lines and the constructing medium, the matter may be referred to the Public Utilities Commission of the State of California for settlement. Adjustment of any difference between the estimated and reasonable actual total installed cost thereof shall be made after the completion of the installation subject to review by the Commission.

At the time of making said advance of the estimated reasonable total installed cost the applicant shall be entitled to elect either of the two refund methods next hereinafter set forth, provided that the election, once made, shall be binding upon the Company and the applicant and may not thereafter be changed:

(1) Revenue Method. For a period not exceeding ten (10) years from the date of completion of the main extension, the Company will refund to the party making the advance, or other party entitled thereto, annually, 35% of the gross revenues collected from consumers occupying the property to which the said extension has been made; provided, however, that the total payments thus made by the Company shall not exceed the amount of the original advance without interest.

(2) Proportionate Cost Method. For a period of not exceeding ten (10) years from the date of completion of the main extension, the Company will make refund to the party making the advance, or other party entitled thereto, for each bona fide consumer within the subdivision or tract in an amount equal to the average total installed cost of 75 feet of main within such subdivision or tract; provided, however, that the total payments thus made by the Company shall not exceed the amount of the original advance without interest. Each such refund will be made only at the date of original installation of service pipe and institution of service to a bona fide consumer and any subsequent change in the identity of the consumer receiving service through the same service pipe shall not give rise to any additional refund right.

RULE AND REGULATION

No. WATER MAIN EXTENSIONS (Continued)

C. Exceptional Cases:

In unusual circumstances, when the application of the provisions of this rule appear impracticable or unjust to either party, the Company or the applicant may refer the matter to the Public Utilities Commission of the State of California for special ruling, or for the approval of special conditions mutually agreed upon.

The total estimated installed cost of an extension to supply a housing project or premises containing more than one housing unit where the water distribution pipes are on private property shall be advanced by the applicant and repayment will only be made in accordance with the Revenue Method of refund.

A bona fide consumer entitling the applicant to refund, as referred to in both Sections A and B hereof, shall be a consumer, exclusive of a real estate developer or builder, who occupies premises which is improved and contains permanent structures with suitable facilities for the use of water and who has received water service from the main for which extension deposit was made for three consecutive months.

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

The effective date of this order shall be twenty (20) days from the date hereof.

Dated at San Francisco, California, this 15th day of February, 1949.

R. E. Anderson
Justus F. Gallen
Walter L. Rogers
Harold R. Kula
Samuel L. Potter
Commissioners.