

Decision No. 42584**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 it to
 increase rates charged for water
 service in South San Francisco
 and vicinity.

Application No. 29615

McCutchen, Thomas, Matthew, Griffiths &
 Greene, by Robert M. Brown, for applicant.

O P I N I O N

California Water Service Company, in this proceeding, seeks authority to increase the rates charged for water service in South San Francisco and vicinity in San Mateo County.

A public hearing on this application was held in South San Francisco on December 9, 1948, before Examiner O'Brien, after due notice to the political subdivisions affected, as well as individual notice to each customer in the South San Francisco District. No one present at the hearing registered any objection to an increase of rates nor to the proposed spread of the increase among various classes of customers.

The original South San Francisco water system was established by South San Francisco Land and Water Company prior to 1893, primarily to furnish water for a meat packing plant. In 1893 domestic service was undertaken. South San Francisco Water Company acquired the system in 1907 and Pacific Water Company purchased the properties in 1927. The properties of that company were acquired by California Water Service Company in 1931. South San Francisco is a community of about 16,000 people. In the area, applicant serves

approximately 3,800 active service connections with water from a pumping station supplied from nine wells and with water purchased from the water department of the City of San Francisco. During 1947, 1.4 billion gallons of water were purchased and produced. Above-ground storage is provided by two concrete reservoirs, two steel tanks and three redwood tanks having an aggregate capacity of 3.9 million gallons, and water is distributed throughout the territory through more than 240,000 feet of pipe, ranging in size from 3/4 inch to 18 inches. At the end of 1947, the number of service connections was 67% greater and the aggregate length of underground piping, 35% more than the respective quantities were at the end of 1942. Water procured in 1947 was 42% more than in 1942.

Applicant bases its justification for an increase in rates on the postwar rise in all expenses to which it is subjected. The record shows that since 1941, wage rates have risen 94%. Using specific examples of cost increases of comparable facilities, elevated storage tanks cost 165% more than in 1940, and costs of six-inch pipes laid underground are 96% higher than 1941. In general, construction costs have approximately doubled since the prewar years.

Another factor creating increased operating expense is the cost of procuring water. In 1925 the well field in South San Francisco furnished all of the water required for the needs of the community. Since that time, the growth of the community has been substantial and the demands for water can no longer be supplied from well sources. Accordingly, it has been necessary for the company to purchase ever increasing quantities of water from the San Francisco Water Department. Furthermore, the rates for water purchased by the company were increased about 18% on September 1, 1945. The minimum cost of water from this source of supply is now 11.8 cents per 100 cubic feet, as compared with a cost of about 3.2 cents per 100 cubic feet for water

produced locally from wells. Consequently, as all additional water delivered by the system must be obtained by purchase, the average cost of all water served gradually increases.

Financing of Properties

Besides South San Francisco, applicant serves 28 other cities and towns. In meeting its capital requirements through the issue of securities, it seeks to provide funds for all its plants and not for one particular system or district. It has been its practice to meet such requirements, in part, with temporary loans which later are re-funded through permanent financing. Generally speaking, it has financed its investment in plant through the issue of bonds, notes, preferred and common stock, and by the use of depreciation reserve monies and earned surplus. Its financial structure, considering the company as a whole, as of June 30, 1948, adjusted to reflect subsequent security issues and excluding its depreciation and amortization reserves which are stated at \$4,508,426, is shown as follows:

Long-term debt -			
First mortgage 3% bonds, due 1975			
1945 issue	\$11,282,000		
1947 issue	1,500,000		
1948 issue	<u>1,500,000</u>	\$14,282,000	53%
Serial notes		480,000	2
Total long-term debt		<u>14,762,000</u>	55
Preferred stock -			
1945 issue, 4.4% cumulative		3,475,000	
1948 issue, 5.3% cumulative, convertible		<u>2,000,000</u>	
Total preferred stock		<u>5,475,000</u>	20
Equity capital -			
Common stock		5,250,000	
Surplus		<u>1,440,813</u>	
Total equity capital		<u>6,690,813</u>	25
	Total	<u>26,927,813</u>	100%

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A representative of the company estimated the average effective interest rate on moneys obtained through the issue of bonds, serial notes, and preferred stock and the investment of those reserves which are being accumulated on the sinking fund basis at approximately 4%, while a member of the Commission's staff estimated such average effective rate as ranging from approximately 3.7% to approximately 4%, depending on whether or not charges pertaining to refunded issues are considered in the calculation. The record in this connection shows that from time to time applicant has availed itself of changes in prevailing interest rates to refund bonds and preferred stock with issues bearing lower interest and dividend rates.

As to outstanding common stock, the record shows that applicant has paid annual dividends of \$2 a share since 1942, being at the rate of 8% per annum on the par value. During the last five years, the average earnings per share from operations, excluding surplus adjustments, have amounted to 10.64% of the par value of the common stock. Stating it another way, the common stock earned, on the average for the five-year period, approximately \$2.66 a share and received, as dividends, \$2 a share, leaving an amount equivalent to approximately \$0.66 a share, as an addition to surplus. The record contains testimony showing the terms under which the outstanding shares of common stock were sold and the market value of such shares, and of the bonds and preferred stock as well, over a period of time. On this latter point, it is noted that the market prices of the outstanding securities have been declining. For example, in November, 1948, applicant sold \$1,500,000 of bonds on a 3.54% basis as compared with a 3.21% basis on the 1947 issue and a 2.86% basis on the 1945 issue. At or about the same time, it sold \$2,000,000 of cumulative convertible preferred stock on a 5.24% basis as compared with a 4.19% basis for the cumulative preferred issue in 1945.

The record in this and in other proceedings shows that applicant is faced with substantial construction expenditures which must be financed in part through the issue of additional bonds and/or stock. In passing on the present proceeding the Commission must consider, among other things, not only the historical costs of capital but also the maintenance of applicant's earnings so that it will be able to raise needed additional capital. Reference is hereafter made to the return that applicant may realize under the rates proposed by it.

Rate Base

The base upon which applicant may be permitted to earn a return should appropriately reflect the plant, properties, and equipment required to render proper service to its customers. For many years this Commission has used a base predicated upon the reasonable historical cost of the properties used and useful in rendering this service. Although considerable concern has been expressed over the effect of spiralling prices on future plant costs and the fact that present facilities could not be replaced for the historical book cost at present price levels, the use of an undepreciated historical cost base, which is the most readily obtainable and least speculative of any base which might be developed, will result in no injustice provided proper recognition is given to the utility's financial needs in the allowed return.

A summary of the estimated rate bases prepared by applicant and by the Commission's staff for the various periods involved is as follows:

<u>For Year Ending</u>	<u>Rate Base</u>	
	<u>Applicant</u>	<u>CPUC Staff</u>
12-31-47	\$	\$ 926,800
6-30-48	1,030,820	991,900
12-31-48	1,092,820	
6-30-49		1,113,200
12-31-49	1,230,820	

Only two of the above estimates cover the same annual period. For that period, the staff's estimate is \$38,920 less than applicant's. Applicant's working cash estimate is \$49,100 higher than that made by the staff. The staff's estimate of working cash is developed from an analysis of the current volume of monthly expenditures, the time lag between payment of expense items and collection of metered revenues, advance collection of flat rate revenues, and accrual of taxes in advance of payment. The same method has been used by the staff many times in the past. Applicant estimated its working cash requirement by determining two months' operating expenses including purchased water, less taxes and depreciation, to which was added an average of three months' construction expenditures. This latter allowance approximated \$30,000. The testimony reveals that frequently these construction funds are obtained by temporary bank loans at an interest rate of about 2%. The temporary loans are retired by funds secured from permanent financing at some later date. The utility is entitled to consideration for interest on reasonably necessary funds for construction purposes, but there is no justification for including construction funds in working capital. The difference in working cash estimates is partially offset by differences in the adjusted fixed capital portion of the rate base, the staff's figure being \$10,180 greater than applicant's. This portion of the rate base difference reflects a variance in the method of determining average fixed capital figures for the several periods. While the capital balances and net capital additions used by applicant and by the staff are identical in amount, the net additions have been accorded different weighting in the two studies. Applicant has apparently used an average of end-of-year balances. The staff, on the other hand, has used an average of monthly balances. Where expenditures predominate in the early part of

the year, the staff's method gives a somewhat higher result. Such a treatment, however, introduces no particular difficulty provided proper recognition is accorded in subsequent analysis.

Revenues

Applicant has submitted a revision of its rate schedules which will yield a gross annual income higher than will those presently in effect. The specific changes proposed will be discussed in somewhat greater detail later in this opinion.

Both the applicant and the Commission's staff have made estimates of the annual gross revenues which would be obtained by application of these alternative rates in a number of different annual periods. A comparative summary of these estimates is shown below:

<u>For Year Ending</u>	<u>Gross Operating Revenues</u>			
	<u>Present Rates</u>		<u>Proposed Rates</u>	
	<u>Applicant</u>	<u>CPUC Staff</u>	<u>Applicant</u>	<u>CPUC Staff</u>
12-31-47	\$258,930	\$	\$	\$
6-30-48	270,126	270,126*	302,105	302,117
12-31-48	277,735		310,906	
6-30-49		282,700		317,257
12-31-49	283,855		318,904	

* Actual

A study of this comparison indicates no marked difference in the estimates of revenue to be derived from a specific schedule of rates. Whether or not the rates proposed should be authorized depends upon the level of the net return which they will produce.

Expenses

Estimates of operating expenses for the several annual periods shown above have been made by applicant and by the Commission's staff. Such expenses include operating and maintenance costs, general administrative and miscellaneous charges, taxes, depreciation, and an amount to cover uncollectible bills. Comparisons of the total estimated expenses are shown on a summary similar to the tabulation of revenues.

<u>For Year Ending</u>	<u>Total Operating Expense</u>			
	<u>Present Rates</u>		<u>Proposed Rates</u>	
	<u>Applicant</u>	<u>CPUC Staff</u>	<u>Applicant</u>	<u>CPUC Staff</u>
12-31-47	\$	\$221,997*	\$	\$
6-30-48	220,193	219,838/	232,345	232,669
12-31-48	229,116		241,721	
6-30-49		236,741		250,600
12-31-49	237,523		250,842	

* Recorded
/ Adjusted

Here again a comparison of the estimates reveals only minor differences in estimated costs of operation. Applicant's estimated future expenses, being predicated upon trends of costs, reflect a probable increase in wage rates above those presently in effect. The Commission staff's estimate, for the year ending, June 30, 1949, on the other hand, is predicated upon the level of wages in effect in 1948. It is a matter of record that the wage rates paid by applicant are governed by agreements between a union representing the employees and applicant's management. Notice of a desire to negotiate new wage agreements for 1949 has been received by applicant and negotiation sessions have been scheduled.

Net Revenues and Rate of Return

A comparative summary of the estimated net revenues resulting from the foregoing revenue and expense estimates follows:

<u>For Year Ending</u>	<u>Net Revenues</u>			
	<u>Present Rates</u>		<u>Proposed Rates</u>	
	<u>Applicant</u>	<u>CPUC Staff</u>	<u>Applicant</u>	<u>CPUC Staff</u>
12-31-47	\$	\$ 36,933*	\$	\$
6-30-48	49,933	50,288/	69,760	69,448
12-31-48	48,619		69,185	
6-30-49		45,959		66,657
12-31-49	46,332		68,062	

* Recorded
/ Adjusted

A review of this summarization indicates rather close agreement between the estimates prepared by applicant and those made by the Commission's staff. When the above net revenues are related to the respective rate bases prepared by the applicant and the Commission's staff, a tabulation of the estimated rates of return shows the following comparative relationships:

<u>For Year Ending</u>	<u>Rate of Return</u>			
	<u>Present Rates</u>		<u>Proposed Rates</u>	
	<u>Applicant</u>	<u>CPUC Staff</u>	<u>Applicant</u>	<u>CPUC Staff</u>
12-31-47		3.99%		
6-30-48	4.8%	5.07	6.8%	7.00%
12-31-48	4.4		6.3	
6-30-49		4.13		5.99
12-31-49	3.8		5.5	

The above table reveals a number of significant factors. The rate of return developed from the staff's estimate is somewhat above that estimated by applicant for the period where directly comparable figures are available. This differential is traceable in large part to differences between the estimated rate bases heretofore discussed. The trend of the figures shows a declining rate of return over the period of time shown, and it appears that applicant will realize a rate of return somewhat less than 6% during 1949 on the rate base suggested by the staff of the Commission.

Rates, Present and Proposed

The present schedule of rates results in substantially all of the service being rendered at meter rates. Flat rates are available only for fire protection service. The present schedules of rates are predicated on schedules established in 1925. A reduction in certain rate blocks was made in 1932. In 1947 as a result of an application for increased revenues, rates for quantities of water exceeding 50,000 cubic feet per month were increased pursuant to authority granted by Decision No. 40194, dated April 22, 1947, in Application No. 27575.

The rates proposed by applicant were selected after a considerable study of present customer requirements and usage and an analysis of allocated costs of service. The monthly minimum charge for a 5/8-inch meter would be increased from \$1.25 to \$1.50 per month, with proportionate charges for larger meters. Commodity rates for consumptions below 50,000 cubic feet monthly would be adjusted, both as to level and blocking, to reflect more nearly an equitable spread of rates according to usage. Service to public agencies would be rendered at the same rates as paid by any other similar customers, and differentials heretofore in effect would be eliminated.

An estimate by the staff of the amount and percentage of increases which would result from applicant's proposed rates, by classes of service, based upon usage for the year ending June 30, 1949, follows:

	Estimated Total Revenue Present Rates	Revenue Increases					
		Flat Rate		Metered Rate		Total	
		Amount	%	Amount	%	Amount	%
Residential	\$110,000	\$23,144	21.0%	\$23,144	21.0%	\$23,144	21.0%
Business	14,070	3,598	25.7	3,598	25.6	3,598	25.6
Industrial	147,210	4,545	3.1	4,545	3.1	4,545	3.1
Municipal	5,720	1,870	81.3	1,870	32.7	1,870	32.7
Irrigation	5,000	1,314	26.3	1,314	26.3	1,314	26.3
Miscellaneous	300	86	28.8	86	28.8	86	28.8
Other	400						
Total	282,700	34,557	12.2	34,557	12.0	34,557	12.0

Another method of comparing the proposed rates with the present rates is to show examples of bills based upon estimated typical usage. Such a comparison is shown below:

<u>Metered Service</u>	<u>Monthly Bill</u>		
	<u>Present Rate</u>	<u>Proposed Rate</u>	<u>Per Cent Increase</u>
For monthly use of:			
500 cubic feet	\$ 1.25	\$ 1.50	20.0%
600 cubic feet	1.47	1.77	20.4
800 cubic feet	1.91	2.31	20.9
1,000 cubic feet	2.35	2.85	21.3
3,000 cubic feet	5.85	8.25	41.0
5,000 cubic feet	8.45	11.45	35.5
10,000 cubic feet	14.95	19.45	30.1
50,000 cubic feet	66.95	83.45	24.6
100,000 cubic feet	124.45	140.95	13.3
1,000,000 cubic feet	1,159.45	1,175.95	1.4
3,000,000 cubic feet	3,459.45	3,475.95	.5

One other analysis which is of interest was introduced by applicant to show the propriety of the changes made in the spread of rates. This analysis was based on an allocated cost of service study. This exhibit showed the following average relationship between the estimated cost of service and the estimated revenue yield of present rates:

<u>Per Average Customer</u>	<u>Revenue Present Rates</u>	<u>Estimated Allocated Cost</u>	<u>Revenue as Per Cent of Cost</u>
Residential	\$ 29.59	\$ 36.26	81.6%
Business	70.18	85.72	81.9
Industrial	3,051.50	3,025.54	100.9
Others	129.90	166.66	77.9
Total	72.43	79.71	90.9

Per 100 c.f. of Water

Residential	.22	.27	81.5
Business	.17	.21	81.0
Industrial	.12	.12	100.0
Others	.12	.16	75.0
Total	.15	.16	93.8

The inference which can be drawn from the study is that while total revenues should be increased, a proper revision would involve a substantial increase in rates for residential, commercial and other service, but no adjustment in rates for industrial service. Such revisions are incorporated in the proposed rates.

It is apparent from the evidence that the present rates will yield inadequate income from future service rendered in South San Francisco. The record likewise indicates that the net return which applicant will receive from its increased rates will not be unreasonable.

O R D E R

California Water Service Company having applied to this Commission for authority to increase the rates charged for water service in the City of South San Francisco and vicinity in San Mateo County, a public hearing having been held, evidence having been introduced, the Commission being fully advised in the premises, and the matter having been submitted for decision,

IT IS HEREBY FOUND AS A FACT that the increases in rates authorized herein are justified; therefore,

IT IS HEREBY ORDERED that applicant is authorized to file in quadruplicate with this Commission after the effective date of this order, in conformity with the Commission's General Order No. 96, the schedule of rates shown in Exhibit A attached hereto, and, upon not less than five (5) days' notice to the Commission and the public, to make said rates effective for service rendered on and after the 16th day of April, 1949, more particularly as follows:

1. Schedule No. 1, General Metered Service, shall be made effective for water service rendered from and after the regular meter reading next succeeding April 16, 1949.
2. Schedule No. 2, Fire Hydrant Service, shall be made effective for regular bills rendered after April 16, 1949, for such service.

IT IS HEREBY FURTHER ORDERED that California Water Service Company is authorized and directed:

3. To withdraw and cancel existing rate schedules superseded by Schedules Nos. 1, 2, and 3, concurrently with the filings hereinabove ordered.

4. To file with this Commission, within forty (40) days after the effective date of this order, four copies of a suitable map or sketch, drawn to an indicated scale upon a sheet 8½x11 inches in size, delineating thereupon in distinctive markings the boundaries of its present service area in and around South San Francisco and the location thereof with reference to the immediate surrounding territory; provided, however, that such filing shall not be construed as a final or conclusive determination or establishment of the dedicated area of service or any portion thereof.
5. To file with this Commission, within fifty (50) days after the effective date of this order, four copies of a comprehensive map, drawn to an indicated scale of not less than 600 feet to the inch, upon which shall be delineated by appropriate markings the territory presently served in and around South San Francisco. This map should be reasonably accurate, show the source and date thereof, and include sufficient data to determine clearly and definitely the location of the property comprising the entire utility area of service; provided, however, that such filing shall not be construed as a final or conclusive determination or establishment of the dedicated area of service or any portion thereof.

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

Dated at Los Angeles, California, this 8th day of March, 1949.

R. J. [Signature]
Justus J. [Signature]
[Signature]
[Signature]

Commissioners.

Schedule No. 1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all water service furnished on a metered basis.

TERRITORY

In the city of South San Francisco, San Mateo County, and in the vicinity thereof.

RATES

Quantity Rates:	Per Meter Per Month
For the first 500 cubic feet or less.	\$ 1.50
For the next 2,500 cubic feet, per 100 cu. ft.26
For the next 47,000 cubic feet, per 100 cu. ft.16
For all over 50,000 cubic feet, per 100 cu. ft.11½

Minimum Charge:

For 5/8-inch meter.	1.50
For 3/4-inch meter.	1.90
For 1-inch meter.	3.00
For 1½-inch meter.	5.00
For 2-inch meter.	7.50
For 3-inch meter.	13.00
For 4-inch meter.	20.00
For 6-inch meter.	40.00
For 8-inch meter.	65.00
For 10-inch meter.	95.00

The minimum charge will entitle the consumer to the quantity of water which that monthly minimum charge will purchase at the Quantity Rates.

Schedule No. 2

FIRE HYDRANT SERVICE

APPLICABILITY

Applicable to all water service rendered to fire hydrants of municipal, county or other political subdivisions of the state.

TERRITORY

In the city of South San Francisco, San Mateo County, and in the vicinity thereof.

RATES

Per Month

For each fire hydrant. \$1.00

SPECIAL CONDITIONS

For all other use by public agencies, including public buildings, irrigation of parks and grounds, playgrounds, library grounds, drinking fountains, swimming pools, and schools, charges are to be made at the General Metered Service rates.