

Decision No. 45884

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of)
Duarte Domestic Water Company for a)
certificate of public convenience)
and necessity; for establishment of)
rates; and for permission to issue)
shares of capital stock.)

Application No. 31393

Anderson and Anderson, by Trent G. Anderson,
for applicant; Philip F. Walsh, for Southern
California Water Company, and Mort Brandler,
for City of Hope Medical Center, interested
parties; C. G. Ferguson, for the Commission
staff.

O P I N I O N

Duarte Domestic Water Company, a corporation, by the above-entitled application filed May 11, 1950, seeks a certificate of public convenience and necessity to operate a public utility water system in unincorporated territory in and about the town of Duarte, Los Angeles County, California, and asks the Commission to establish a schedule of rates for domestic water service. Permission is also requested to issue shares of capital stock to acquire the domestic water system properties and 3,750 shares of capital stock of Duarte Mutual Water Company.

Public hearings in this matter were held before Examiner Warner on April 4, 1951, and June 6 and 7, 1951, in Los Angeles, California.

At the hearings, applicant amended its application by the introduction, as a part of Exhibit No. 4, of an amended schedule of proposed rates, and, as Exhibits Nos. 1-A and 2-A, of a map of the proposed service area together with a description of the boundaries thereof.

Duarte Domestic Water Company, a California corporation, was organized December 19, 1949. As set forth in its Articles of Incorporation, a copy of which was attached to the application as Exhibit A, its directors are: J. S. Blain, Max A. Bengel, C. B. Hopper, F. W. Livermont, and James A. Blain, all of Duarte, California. Applicant's board of directors and the officers elected thereby are identical in personnel with those of Duarte Mutual Water Company.

As alleged in its application, applicant is a new corporation and has not engaged in any business. It is authorized by its Articles of Incorporation to issue 10,000 shares of common stock only, having a par value of \$60 per share; the aggregate par value of all shares so authorized being \$600,000.

Applicant requests permission to issue and sell \$560,000 par value of its stock to Duarte Mutual Water Company.

Of this total amount, \$335,000 would be in payment of the physical properties of the domestic water system of the mutual water company, excluding all domestic water production facilities; but including domestic service water transmission lines, pipe lines, reservoirs, office building and lots, trucks, furniture, fixtures, tools, meters, materials, supplies, and miscellaneous equipment. Also included in this payment would be certain accounts receivable of the mutual company.

The balance of the total amount of stock requested to be issued, amounting to \$225,000, would be in payment of 3,750 shares of the capital stock of Duarte Mutual Water Company at a value of \$60 per share. Ownership of such mutual stock would entitle applicant to purchase, from the mutual company, a limit of 2,500 cubic feet of water per share per month and would constitute applicant's source of water supply. Water would be purchased by applicant from the mutual company at a rate of \$0.03 per 100 cubic feet.

Duarte Mutual Water Company was organized April 26, 1947, for the purpose of effecting the consolidation of Beardslee Water Ditch Company, incorporated in 1881, and Duarte Mutual Irrigation and Canal Company, incorporated in 1882, for the purpose of supplying irrigation, and some incidental domestic, water to farm lands and their owners in the vicinity of Duarte, California. The predecessor companies developed over the years substantial water supplies in the so-called Pasadena Basin, the Upper and Lower Canyon Basins, and the San Gabriel River Basin and through prescription, court adjudication and other means, established rights to some of these water supplies.

Since 1945 the character of the area has changed from agricultural and rural to domestic and suburban. Domestic water sales have increased from 15,445,000 cu. ft. to an average of 225 domestic consumers in 1945, to 76,379,000 cu. ft. to an average of 2,723 domestic consumers in 1950. It is because of this changing character of the area that, a witness for applicant alleged, applicant company was formed to take over the domestic water service operations of the mutual company and that the application herein being considered was filed.

The area proposed to be served by applicant, and now being served by the mutual company, is generally flat in terrain except that the most northerly portion is mountainous, and extends due east and southeast of the city of Monrovia to the San Gabriel River. It comprises about 5,000 acres. As of April 4, 1951, domestic water service was being furnished to 3,262 consumers, and 92 fire hydrants of the single outlet type were connected to the distribution system.

In support of its application applicant's president, Mr. J. S. Blain, also president and a director of Duarte Mutual Water Company, alleged that the operation of the domestic water services by applicant as a public utility would be very desirable and would be for the best interests of the mutual company and its shareholders, and also of its domestic consumers, in that it would (1) reduce operating expenses, (2) improve and simplify bookkeeping by machine bookkeeping, (3) eliminate the extensive and expensive details of issuing and reissuing mutual stock to lot purchasers in subdivided tracts, thus greatly simplifying applications for domestic water service, (4) provide for metered domestic service, and (5) minimize controversies with consumers because of regulation by this Commission, all of which would result in lower water charges and better water service for consumers of all classes.

The following tabulation shows a comparative summary of the present domestic water service rates being charged by the mutual company and the proposed rates to be charged by applicant:

DUARTE DOMESTIC WATER COMPANY
COMPARISON OF PRESENT (MUTUAL) AND PROPOSED RATES

Quantity Charge:	<u>Per Meter per Month</u>	
	<u>Present</u>	<u>Proposed</u>
First 800 cu. ft. or less	\$1.50	\$1.75
Next 2,000 cu. ft., per 100 cu. ft.07	-
Over 2,800 cu. ft., per 100 cu. ft.05	-
Next 1,200 cu. ft., per 100 cu. ft.	-	.18
Next 3,000 cu. ft., per 100 cu. ft.	-	.14
Over 5,000 cu. ft., per 100 cu. ft.	-	.08
 Minimum Charge:		
For 5/8 x 3/4-inch meter	\$ -	\$ 1.75
For 3/4-inch meter	-	2.00
For 1-inch meter	-	2.50
For 1 1/2-inch meter	-	5.00
For 2-inch meter	-	7.50
For 3-inch meter	-	10.00
For 4-inch meter	-	15.00
For 6-inch meter	-	25.00

Under present mutual company regulations, as shown in Exhibit No. 5, a \$50 installation charge is made for each service connection of two inches or less in size, plus the current list price of the service meter. Each user of water is required to own not less than two (2) shares of stock in the mutual company.

The record shows that approximately 51% of the consumers used, during 1950, 1,400 cubic feet of water, or less, per month and that whereas under the present mutual rates their bill was \$1.92 or less for such usage in 1950, it would increase to \$2.83 per month, an increase of \$0.91, or 47%, under the proposed rates. There would, however, be no assessments levied against stock ownership. As shown in Exhibit No. 6, such assessments amounted to \$0.50 per share twice in 1948 and 1949 and once in 1950. No assessments have been levied in 1951 to date.

The record shows that the number of shares of capital stock of Duarte Mutual Water Company which may be issued is 25,000 shares; that the par value of each share is \$50; and that the aggregate par value is \$1,250,000. As of December 31, 1949, the mutual company had 20,433 shares outstanding with a net book value, including \$825,000 of water rights, of \$65 per share, and 4,567 shares unissued. Of the total outstanding shares, a minimum of 6,524 shares was held by domestic water consumers. In its application, applicant alleged that the book value of the unissued shares was approximately \$60 per share and that the value of the needed 3,750 shares of mutual stock proposed to be acquired by applicant was \$225,000 at \$60 per share.

Concerning the value requested by applicant to be placed on shares of mutual stock proposed to be acquired by applicant, _____ a consulting engineer called as a witness for applicant, in _____

testifying regarding Exhibit No. 4 submitted by him, placed an appraised value on the mutual shares of \$43, as shown in said Exhibit No. 4, made up of the following items:

(1) The remaining book or physical value per share of \$22.20, computed as follows:

Total assets of Duarte Mutual Water Company	\$1,529,453.59
Less: Liabilities	200,115.98
Net Worth	<u>1,329,337.61</u>
Less: Water rights	875,000.00
Remaining book value	<u>454,337.61</u>
per share, of 20,433 shares	22.24

(2) The value of rights which applicant would acquire upon ownership of mutual stock, known as "participating value", of \$20.80 per share, computed as follows:

Estimated reproduction cost new as of 1945	
of water production facilities	\$ 78,000.00
Per share, of 3,750 shares	20.80

Applicant did not amend its application to reflect the various values appearing in the record and placed on stock of the mutual company. The record shows that some mutual stock has been exchanged recently from time to time for \$10 per share. A witness for the Commission staff testified that he had been unable to determine a value for rate making purposes of stock of the mutual company, and that he had not included any value therefor in the proposed estimated average rate bases for the years 1950 and 1951 as shown in Exhibit No. 9.

The domestic water supply of Duarte Mutual Water Company as shown in Exhibits Nos. 4 and 9 is developed from four sources, viz., (1) Fish Canyon, including gravity supply, and a well, 16 inches in diameter, 172 feet in depth, with an installed pumping plant capacity of 1,251 gallons per minute; (2) Los Lomas well, 26 inches in diameter, 172 feet in depth, with an installed pumping plant capacity of 980 gallons per minute; (3) Santa Fe well, 26 inches in diameter, 680 feet in depth, with an installed pumping

plant capacity of 1,286 gallons per minute; and (4) Mountain-Avenue (Beardslee) well, 20 inches in diameter, 352 feet in depth, with an installed pumping plant capacity of 1,581 gallons per minute. The Mountain Avenue and Santa Fe wells draw on the San Gabriel Basin, the Los Lomas well draws on the Lower Canyon Basin, and the Fish Canyon well draws on the Upper Canyon Basin. None of the domestic wells draws on the Pasadena (Raymond) Basin. The sources of domestic water supply are separate and distinct from those of the irrigation water supply and they are not physically connected. The record shows that the mutual company plans to build a filtration plant on Fish Creek at an estimated cost of \$100,000 for the purpose of treating waters diverted from the San Gabriel River for domestic uses.

The mutual company now owns, operates for its domestic water system purposes, and proposes to sell to applicant three distribution reservoirs as follows: (1) Fish Canyon reservoir, into which water from Fish Canyon sources is delivered, is a reinforced concrete reservoir, 80 feet in diameter, 15 feet in depth, with a capacity of 500,000 gallons; (2) Scott reservoir, into which water from the Santa Fe well is delivered, is a welded steel tank on concrete foundation, 60 feet in diameter, 30 feet in height, with a capacity of 625,000 gallons; and (3) Fair Oaks tanks, into which water from Fish Canyon reservoir is boosted, are: (a), a corrugated iron tank, 15 feet in diameter, 12 feet in height, with a capacity of 15,800 gallons, and (b), a bolted steel tank, 20 feet in diameter, 8 feet in height, with a capacity of 18,800 gallons. The record shows that contracts have been let by the mutual company and construction is now under way for a new reservoir of 1,500,000-gallon capacity which will augment the distribution system in the

southwest portion of the service area and will decrease the present area served by the Scott reservoir. Cost of this reservoir was estimated to be \$65,107, and it was estimated to be in service in June, 1951.

The domestic distribution system of the mutual company, proposed to be acquired by applicant, consists of approximately 244,100 feet of Transite and steel mains varying in diameter from 2 inches to 16 inches.

Exhibit No. 4, hereinbefore referred to, is a report on the rate base, operating expenses, rate schedule, and earnings of applicant. Exhibit No. 9, also referred to herein, is a report on a study of the operations of applicant for the year 1950 adjusted to reflect accounting practices with which applicant would have been required to conform if it had been operating as a public utility during 1950, and for the year 1951 estimated. Exhibit No. 9 was testified to by an engineer on the Commission's staff and the rate base is predicated on the appraisal shown by Exhibit No. 10 and prepared by another engineer

of the Commission's staff. The earnings information contained therein is summarized and compared in the following tabulation:

DUARTE DOMESTIC WATER COMPANY

SUMMARY OF EARNINGS
YEAR 1950 ADJUSTED, AND YEAR 1951 ESTIMATED
AT PRESENT AND PROPOSED RATES

Item	:Per P.U.C.: Per Co. :		:Exh. No. 9:Exh. No. 4:		
	: Year 1950:	: Year 1951:	Per P.U.C. Exh. No. 9		
	: Adjusted :	: Estimated:	Year 1951 Estimated		
	: Present :	: Proposed :	: Present :	Proposed Rates	
	: Rates :	: Rates :	: Rates :	(1)	(2)
Operating Revenues	\$ 84,020	\$155,377	\$100,380	\$155,930	\$155,930
Operating Expenses, Including Taxes and Depreciation	76,751	117,384	92,340	116,540	114,950*
Net Operating Revenues	7,269	37,993	8,040	39,390	40,980
Estimated Depreciated Historical Cost of Production Facilities (Per Exh. No. 10)	-	-	-	-	40,000
Average Rate Base, Depreciated	412,604#	654,077φ	486,520#	486,520#	526,520#
Rate of Return	1.8%	5.8%	1.7%	8.1%	7.8%

(1) Assuming mutual-owned production facilities.

(2) Assuming utility-owned production facilities.

* Includes estimated net saving of \$1,590 due to water not purchased.

Excludes value for water rights.

φ Includes value for water rights of \$161,250 (3,750 shares of mutual company stock at \$43 per share).

It is evident from the above tabulation that the inclusion in the rate base by the Commission staff witness of a value for water rights proposed by applicant to be acquired through ownership of mutual company stock would have had the effect of considerably reducing the estimated rate of return under the proposed rates.

Also, it is evident that the estimates of operating revenues and operating expenses, including taxes and depreciation, for the year 1951 under the proposed rates as submitted by applicant's witness and by the Commission staff engineer, are not far apart, except for net savings due to water not purchased, assuming

utility-owned production facilities, as estimated by the staff witness. Such savings, the record shows, would result primarily from the elimination by the staff witness of interest payments calculated by applicant's witness as a component of the cost of water of \$0.03 per 100 cubic feet. The development of this cost was set forth in applicant's Exhibit No. 7.

In explaining Exhibit No. 7, applicant's witness testified that he had considered "interest paid" as an operating expense for the purpose of his computation of cost of water purchased. The record does not show the basis of the determination of the items of total system administrative expenses of which, as shown in said exhibit, 73.6% was allocated to pumping costs.

This witness further testified that it was his understanding that the \$0.03 rate (cost of water purchased) would be subject to revision by the mutual company, either upward or downward, depending on the "cost" to produce such water. When determination of such "costs", whether on a monthly, annual or some other periodic basis, would be made by the mutual, is not shown in the record. The Commission, therefore, is unable to arrive at a conclusion as to the reasonableness of the estimated rate of return of applicant, based on applicant's showing with respect thereto.

According to testimony of applicant's president, certain stockholders of the mutual company are reluctant to turn over the water supply production facilities to applicant, and, in fact, the testimony indicates that they would not consent to a plan of applicant's operation which would incorporate that proposition. The underlying reasons for such reluctance are obscure in the record, but it appears from the testimony of applicant's president that certain irrigation stockholders would "like to make some money" from the sale to applicant of excess shares of mutual stock which they

own. This witness stated that those stockholders anticipated that the 3,750 shares of stock to be acquired by the applicant would soon prove to be an inadequate number and that more shares would soon have to be acquired in order to assure to applicant its source of water supply, and that the demand for the stock would increase, thereby increasing the price.

The record shows that earnings of applicant might be used by the mutual company, at the discretion of the board of directors, either of applicant or the mutual company, to (1) reduce irrigation rates, (2) reduce indebtedness of the mutual company, (3) effect improvements to the mutual irrigation system, (4) effect improvements to the domestic water production facilities, or (5) reduce the whole-sale, or cost of, water rate to applicant. Some of these actions might be beneficial to applicant and to its consumers and some might not, and the record does not disclose which actions might be beneficial, in what degree, to what extent or when or over what period they might be beneficial, if they were. The Commission, therefore, concludes that it would not be in the public interest to authorize the stock issuance as applied for. Counsel for applicant cited the matter of the Commission's Decision No. 42172, dated October 26, 1948, in Application No. 29398, of San Dimas-Charter Oak Domestic Water Company for an increase in water rates, as being in point both as to mutual company complete ownership of utility stock, and as to inclusion by the Commission in the rate base of a value for mutual stock owned by the utility. Upon reviewing this matter, it is evident that this case is not in point, ~~in either regard.~~ R 2.2,

After a careful review of the application as submitted and the record of the proceeding in this matter, it is our considered opinion that it would not be in the public interest to grant the application as requested. Our considerations have included, of

course, applicant's allegations as set forth in the application and in the record, as outlined hereinabove, that it would be in the public interest for the domestic water system properties of Duarte Mutual Water Company to be acquired and operated by applicant.

However, we conclude to the contrary, in view of the following facts:

1. That the rates requested to be established would result in a substantial increase in monthly water bills to present domestic consumers.
2. That the record does not disclose a sound basis for determining a reasonable rate of return.
 - (a) The record does not disclose a sound basis for determining a reasonable cost of water to be purchased.
 - (b) The record does not disclose a sound basis for the placing of a value on the capital stock of the mutual company proposed to be acquired by applicant for inclusion in the rate base.
3. That the proposed acquisition by applicant of 3,750 shares of mutual company stock of an undeterminable value would not necessarily assure to applicant, over the years, as dependable or economical a source of water supply as would be assured if applicant were to acquire these or other physical water production facilities.
4. That the record shows that the absolute control and ownership of all of applicant's capital stock by the mutual company might or might not prove to be beneficial to applicant and its domestic consumers, that the corporate relationship established thereby would be obscure; that actions of either board of directors, at their discretion solely, might or might not be equitable, or inequitable, as between the mutual

company and applicant as the case might be or as the circumstances direct, and that it would be ambiguous in its purposes and in practice.

Therefore, the order which follows will provide that the application be denied without prejudice.

O R D E R

Duarte Domestic Water Company having applied to the Commission for a certificate of public convenience and necessity, for the establishment of rates, and for permission to issue shares of capital stock, public hearings having been held, and the matter having been submitted for decision,

IT IS ORDERED that Application No. 31393 filed by Duarte Domestic Water Company be and it is hereby denied without prejudice.

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

Dated at San Francisco, California, this 16th day of June, 1951.

[Signature]
Justus F. Casper
Harold Hule
[Signature]
[Signature]
Commissioners.