

Decision No. 62923**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
 SOUTHWEST WATER COMPANY, a corporation,
 for authority to increase rates in its
 La Mirada, Etiwanda and La Sierra
 Districts.

Application No. 43589

C. H. Deitz; and Overton, Lyman and Prince, by Arthur D. Guy, Jr.; for applicant.
David M. Horwitz, for himself and neighbors (in La Mirada), interested party.
Chapman L. Bone, City Administrator, for City of La Mirada, interested party.
K. F. Ambs or Erby N. Davidson, for La Sierra Community Services District, protestant.
Ralph Winchester, for Loma Linda Food Company (La Sierra), protestant.
Vernon L. Von Pohle, for himself and neighbors (in La Sierra), protestant.
Burt Shelby, for Etiwanda Service Club, protestant and interested party.
Hugh N. Orr, A. L. Gielegem and John R. Gillanders, for the Commission staff.

OPINION ON REQUEST FOR INTERIM INCREASEApplicant's Request

Application as above-entitled was filed on July 7, 1961, followed by the filing on July 31, 1961 of a petition for an emergency interim increase in rates. The application requests an increase of 29 percent in La Mirada District, 48 percent in the Etiwanda District and 64 percent in La Sierra District, to result in a company-wide increase of 43 percent. The petition requests a total company interim increase of 25 percent, to be spread almost uniformly over all classes of general metered customers in all three districts. This 25 percent interim increase is over 86 percent of the 29 percent increase ultimately requested for La Mirada District but represents lesser percentages of the total increases requested for the other two districts.

Public Hearings

Six days of public hearing on this application, devoted primarily to the determination of the necessity for the requested interim increase, were held before Examiner E. Ronald Foster at Santa Fe Springs on September 27, at Corona on September 28, at Los Angeles on October 4, 5 and 6, and at San Francisco on October 10, 1961. Prior to the first two days of hearing, notices thereof were mailed to parties known to be interested and were published and posted in accordance with the Commission's procedural rules.

Only two La Mirada customers attended the first day of hearing; their pressure complaints were satisfactorily answered by applicant. The second day of hearing was attended by five customers from the Etiwanda District and over fifty from La Sierra District. A witness representing the Etiwanda Service Club presented two petitions. One, signed by 79 customers, requested the Commission to refuse to grant any increase and alleged that the present rates are sufficient to meet operating costs and that a rate increase would be disastrous to the residential and industrial growth and development of the area. The other, bearing signatures of 95 persons claiming to be both stockholders and customers of applicant, also requested that the Commission grant no increase in the Etiwanda District and alleged that the present rates are high enough to take care of all expenses and still pay satisfactory dividends. Representatives of customers in La Sierra District testified in protest to the extent of the increase proposed for this district and also in regard to excessive fluctuation of pressures in one area and insufficient pressure and volume of water under certain conditions in other areas.

On the last day of hearing, applicant's request for interim rate increases was taken under submission and further hearing on the application was continued to a date to be set. This decision will deal solely with applicant's request for interim rate relief.

Applicant's Position

Applicant's request for an immediate increase in rates is related to its claim for the need of additional funds with which to finance its current construction program. One potential source of such funds is from the sale of its Series "D" bonds. By Decision No. 61206 dated December 20, 1960 in Application No. 42907, the Commission authorized the issuance, on or before December 31, 1961, of applicant's First Mortgage Series "D" 5-3/4 percent Bonds in the total amount of \$750,000, of which \$500,000 have been sold, leaving an amount of \$250,000 unissued.

The trust indenture which sets forth the terms under which applicant may qualify for the issuance and sale of these bonds requires, among other things, that the company shall show net earnings, before Federal income taxes and before interest on bonds, of two times bond interest requirements for outstanding bonds. Applicant alleges that its current operating statements indicate that it will not be able to meet the interest requirements for the sale of bonds at the level of earnings resulting from its present rates for water service.

The net earnings required under applicant's trust indenture may be based on any twelve consecutive months' period out of the fifteen calendar months next preceding the date of the authentication and delivery of the additional bonds.

Utilizing the estimated results of operation for the calendar year 1961 as set forth in a report dated May, 1961, filed with the original application, the petition contains a tabulation which shows the additional earnings required to meet the terms of the trust indenture to be \$52,880. This additional net income would be produced in a period of about four months by applying the proposed 25 percent increase to the estimated metered sales of \$655,030 for the year 1961 shown in the said report.

Applicant's Exhibit No. 3, introduced in evidence at the hearing, is a pro forma income and expense statement for the year 1961, based on recorded amounts for the first eight months and estimates for the months of September to December, inclusive. In this exhibit, the estimated income and expenses were based on the average sales per customer for the previous five years. On this basis, the exhibit shows the additional earnings required to meet the terms of the trust indenture as \$11,389. From the detailed information shown in Exhibit No. 3, it may be observed that the metered sales as estimated for the last four months of 1961 total \$214,831. A 25 percent increase applied to that amount would be \$53,708, or slightly more than the \$52,880 deficiency shown in the petition. The deficiency of \$11,389 indicated in Exhibit No. 3 could have been produced by applying an increase of only 5.3 percent to the metered revenues for the same four months.

When applicant's secretary was asked on cross-examination as to what he attributed the rather substantial improvement shown by Exhibit No. 3 as compared with the deficiency indicated in the petition itself, he stated it was due to the unusual warm weather which has prevailed this year through August 31. He could not say whether a more recent computation, if made, might show an additional improvement.

Exhibit No. 11 is an interim report dated September 25, 1961, prepared by a Commission staff accountant, which includes comparative balance sheets as of July 31, 1960 and July 31, 1961 and comparative income statements for the twelve months ended July 31, 1960 and 1961, based on a limited investigation of applicant's books, records, reports and other data. This report shows the recorded net income for the 12-month period ended July 31, 1961, to be \$30,410 less than twice the interest requirements on bonds outstanding on September 30, 1961.

Following is a tabulation which provides a comparison of the three determinations of the deficiency in net income to meet the trust indenture requirement:

Net Earnings at Present Meter Rates
and Bond Interest Requirements

<u>Item</u>	:CPUC Staff : :Exh. No.11 : :12 Mos.End- :ing 7-31-61:	: Year 1961 : Application: : and : Petition :	: Estimated : Exh. No.3 : 8 Mos.Rec. : 4 Mos.Est.
<u>Income</u>			
Metered Sales		\$ 655,030	\$ 680,248
Other Sales		26,957	24,994
Total Operating Revenues	\$ 683,011	681,987	705,242
Other Income	1,809	320	82
Total Income	684,820	682,307	705,324
<u>Deductions</u>			
Operating Expenses	344,532	363,750	346,465
Depreciation	102,087	103,111	102,802
Amort. - Franchises	761	711	711
Taxes Other Than Fed.Inc.Tax	60,832	58,950	62,187
Interest on Debt	79,615	91,250	91,324
Amortization of Debt Expense	3,462	3,985	3,719
Other Interest Charges	7,881	10,280	6,429
Total Deductions	599,170	632,037	613,637
Net Income Before Fed.Inc.Taxes	85,650	50,270	91,687
Interest on Debt	79,615	91,250	91,324
Earnings Before Fed.Inc.Taxes and Interest on Debt	165,265	141,520	183,011
Twice Interest Requirements on Bonds Outstanding	195,675	194,400	194,400
Additional Earnings Required to Meet Terms of Trust Indenture	30,410	52,880	11,389

The petition alleges that reduced per-customer income since 1959, increased charges levied by the Central Basin Replenishment District and other factors have militated to reduce applicant's earning capacity over a relatively short period of time. Exhibits attached to the petition and other data are intended to demonstrate the necessity for immediate rate relief due to the dire cash position which applicant's present rates have created. Applicant claims that the continuation of such rates will adversely affect its ability to adequately serve its existing and future customers.

Applicant's Presentation

In its request for interim increases in rates in its three districts, applicant has not relied on any showing of the rate of return, or any decline therein, either on a company-wide basis or separately by districts. The comprehensive report, which accompanied the original application, was introduced for identification only as Exhibit No. 1.

At the hearing on its petition, applicant presented exhibits of its financial condition and its construction program which are more up-to-date than those filed with the petition.

Exhibit No. 2 includes a comparative balance sheet as of August 31, 1960 and August 31, 1961. It also includes comparative statements of income for the months of August, 1960 and 1961 and for the 8-month periods ending August 31, 1960 and 1961. It may be noted that total utility plant, including work in progress, increased from \$4,088,372 on August 31, 1960, to \$4,923,363 on August 31, 1961, an increase of nearly \$835,000. During the same period, the net total of advances for construction increased only about \$4,900.

Exhibit No. 4 shows the applicant's pro forma cash position, forecast in detail, from September 1 through December 31, 1961. In addition to \$55,000 for the acquisition of land and wells, this exhibit shows plant additions of \$75,000 for each of the four months. It also shows that \$250,000 of bank loans would be liquidated by the issuance of the bonds herein concerned. Exhibit No. 6 is a similar pro forma cash tabulation for the first four months of 1962.

Capital expenditures in progress on August 31, 1961, to be completed by December 31, 1961, are itemized in Exhibit No. 5, by districts. Exhibit No. 7 is a similar itemization of capital improvements planned for 1962.

There follows a summary of the capital expenditures as listed on Exhibits 5 and 7.

Exh. No.	Period	District			Totals
		La Mirada	Etiwanda	La Sierra	
5	:Aug. 31 to Dec. 31, 1961	\$238,375	\$ 6,585	\$ 53,700	\$298,660
7	: 1962	: 337,808	: 4,974	: 302,868	: 645,650
	: Total	: 576,183	: 11,559	: 356,568	: 944,310

In the foregoing tabulation, the total amount shown for La Mirada District includes \$360,000 for the completion of a 7,250,000-gallon reservoir on land previously acquired, \$50,000 for a proposed connection to the Metropolitan Water District aqueduct, and some \$58,500 for a booster plant and 20-inch mains in connection therewith.

Not included in the tabulation is an amount of about \$130,000 already expended for a 28-acre parcel of land in the Etiwanda District for various facilities including a filtration plant and reservoir eventually planned to be supplied from another MWD aqueduct connection.

The amount shown for La Sierra District includes a million-gallon reservoir, a new well, the replacement of various sections of small pipe and the installation of larger mains, and some valves, in accordance with a master plan for the improvement of service in this district.

Commission Staff Participation

Among other things, the Commission staff's Exhibit No. 11, previously referred to, contains the following tabulation which shows certain comparative statistics on a per-customer basis, for the 12-month periods ended July 31, 1960 and 1961.

Item	: Year Ended July 31:		Per Cent : Increase
	: 1960	: 1961	
Investment per Customer	: \$342.49	: \$367.33	: 7.25%
Operating Revenue per Customer	: 56.57	: 58.58	: 3.55
Operating Expenses per Customer	: 20.20	: 29.58	: 46.44

One of the factors contributing to increased operating expenses involves the transfer of a portion of administrative expense to utility plant. The rate used by applicant for this purpose for the first seven months of 1960 was 10 percent of 90 percent of construction work in progress, while in 1961 the rates used were 5% of 95% in January, 6% of 95% from February through June, and 8% of 95% for the month of July. For the first seven months of 1960 the amount so transferred was about \$47,000 as compared with about \$23,000 for the first seven months of 1961, thus increasing the net operating expense for 1961 over that in 1960 by a substantial amount.

Applicant's net income on a cash basis, amounting to \$96,327 for the first seven months of 1961 as shown in Schedule III of Exhibit No. 11, indicates that applicant has been able to meet its operating expenses, including bond and other interest charges and also expenses that could be deferred. Based on his limited examination, the staff accountant testified that applicant does not appear to be in a dire cash position insofar as operations are concerned, nor that it will be unable to continue operations at present rates for water service. This witness further testified that any financial emergency which may exist, because of the alleged decline in applicant's earnings, is limited to a partial curtailment of applicant's construction program and that this condition might have been lessened, to some degree, if it had made more use of advances for construction under main extension contracts to finance expansion into subdivisions within its operating area.

The staff representatives also cross-examined applicant's witnesses at considerable length. Inquiry was made concerning applicant's operating practices and managerial policies and procedures. While some of the information elicited from applicant's officials may have a more important bearing on the general rate increase application, several facts were developed which are related to the petition now under consideration.

It was clearly shown that in La Mirada District, in particular, applicant has not taken full advantage of its filed main extension rule to finance the construction of distribution mains and services in subdivisions by means of construction advances from the subdividers. Under the rule, it is possible that the cost of some of the "back-up" facilities also could have been obtained from the subdividers, had applicant sought and obtained the necessary authorization from the Commission. Instead, the record shows that many entire subdivision installations were financed by the issuance of applicant's stock, some of which was its Class A 5½% Preferred stock.

In the Etiwanda District, applicant has used large amounts of its available resources to acquire property and to install large water mains in anticipation of industrial developments which have not materialized. A 28-acre site for future use for a reservoir and other facilities was acquired at a total cost of about \$130,000 as a result of an option taken some years ago. Some considerable lengths of 18-inch and 12-inch mains have been installed which are presently only useful in supplying one customer through a single two-inch meter. Such investments in plant are speculative in nature.

In La Sierra District, applicant has engaged in an extensive improvement and development program. Applicant has repeatedly stated that this is largely in compliance with the Commission's orders to improve and enlarge the facilities in this district in

order to render adequate service and to bring the facilities up to the minimum requirements of the Commission's General Order No. 103. It may be pointed out that in Decision No. 58138 dated March 17, 1959, in Application No. 40273, which established the rates now in effect for this district, an amount of \$142,610 for future additions to plant and construction work in progress was included in the rate base upon which such rates were authorized. Some of the items included in those additions are just now being completed. Prior to their completion, applicant has installed many other capital improvements as part of its master planning.

The staff also developed the fact that an engineering department consisting of 14 persons was transferred from applicant's affiliate, Suburban Water Systems, to applicant's payroll on January 1, 1961. Whereas Suburban formerly charged applicant for engineering work done for Southwest Water Company, now applicant charges Suburban for work done in the engineering department, the residual expense being paid by applicant. It appears that this is another important factor contributing to the increase in expenses represented by applicant's records.

The staff questioned applicant's witnesses, in considerable detail, as to the immediate necessity of installing the numerous items shown on Exhibits No. 5 and No. 7. Applicant's management has already decided on the postponement or elimination of certain items.

Findings and Conclusions

From a careful review of the evidence, we find that applicant has not sustained its burden of proof that an emergency exists which justifies an interim increase in rates for water service to its customers. The utility is not entitled to rely upon an emergency of its own creation or resulting from speculation for the purpose of securing such increase.

We find that applicant has not shown the extent to which increases are necessary, if at all, in order to render a reasonable return on its investment in plant in any of its districts, or on a company-wide basis.

The evidence indicates neither a precarious financial condition nor other serious financial position which must be relieved now pending the orderly processes of establishing definitive rates in this proceeding. Any interim increase could be effective for only a few months before such rates may reasonably be expected to be established after a further showing by applicant, the Commission staff and other interested parties, followed by full cross-examination of all witnesses.

We find and conclude that the present record does not justify the granting of the interim relief sought pending a final decision in this proceeding. Accordingly, applicant's petition will be denied.

O R D E R

Based upon the evidence of record and the findings and conclusions set forth in the preceding opinion,


IT IS ORDERED that applicant's petition for emergency interim increases in rates be, and it is, hereby denied.

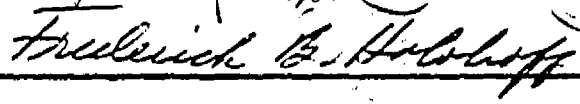
The effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 12th day of DECEMBER, 1961.



President





Commissioners

-11- Commissioner C. Lyn Fox, being necessarily absent, did not participate in the disposition of this proceeding.