

**ORIGINAL**Decision No. 63942

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of  
 the SOUTHERN CALIFORNIA WATER COMPANY  
 for authority to increase rates for  
 water service in its SOUTHWEST DISTRICT.

)  
 )  
 ) Application No. 43574  
 ) (Filed June 29, 1961)

Investigation into the reasonableness of  
 rates and adequacy of water service of  
 SOUTHERN CALIFORNIA WATER COMPANY in the  
 latter's SOUTHWEST DISTRICT.

)  
 )  
 ) Case No. 7210  
 ) (Filed October 23, 1961)

O'Melveny & Myers, by Donn B. Miller;  
C. T. Mess, for applicant and respondent.  
 City of Inglewood, by Mark C. Allen, Jr.,  
 and Charles E. Mattson, interested party.  
Hugh N. Orr, Robert W. Beardslee and  
Richard E. Entwistle, for the Commission  
 staff.

O P I N I O NPublic Hearings

Public hearings in the above-entitled matters were held before Commissioner Peter E. Mitchell and/or Examiner F. Everett Emerson on November 29, December 6 and December 7, 1961 at Inglewood and on January 8 and 9, 1962 at Los Angeles. By filing made on December 7, 1961 applicant petitioned for the issuance of a presiding officer's proposed report. The matters were submitted subject to the filing of briefs on March 5, 1962.

Proposed Report

The issues in these matters are clearly developed. Applicant had every opportunity to make such showing as it desired during the five days of hearing devoted to the proceedings. In addition, applicant, as well as the Commission staff, availed itself of a lengthy period in which to prepare and file its brief. In view of

the comprehensive record made, the Commission finds that no useful purpose would be served by the issuance of a proposed report. Applicant's petition for the same is hereby denied.

Applicant's Southwest District

Applicant's Southwest District serves an area of about 21 square miles in the southwestern portion of Los Angeles County and includes all of the Cities of Gardena and Lawndale and portions of the Cities of Hawthorne, Inglewood and Compton. The greater portion of the area is residential in character. A small amount of industrial and commercial service is rendered in Gardena and Lawndale. The water supply for the district is obtained from 27 company-owned wells and from the Metropolitan Water District of Southern California through the facilities of the West Basin Municipal Water District. As of December 31, 1960, applicant was providing metered water service to approximately 38,700 customers and flat rate private fire protection service to 113 customers. In addition, applicant had 1,973 fire hydrants connected to its system. During the year 1960 applicant sold over 863 million cubic feet of metered water within the district.

Applicant's Request

Applicant seeks increased revenues, amounting to approximately \$412,760 on an annual basis, in order to yield what it considers to be a just, sufficient and reasonable return on its properties used and useful in rendering public utility water service in its Southwest District. According to applicant's showing, such an increase would provide a normal-year rate of return of approximately 7 percent on its claimed depreciated rate base of \$10,338,000.

Rate Increase Proposal

Applicant proposes to increase charges for general metered service and its optional special metered service, the latter type of service being restricted to deliveries of water between 10 p.m. and 5 a.m. The present rate schedules for these two services became effective on July 1, 1959. A comparison of monthly charges under present and proposed general meter rates is as follows:

<u>Consumption (Cubic Feet)</u>	<u>Present Charge</u>	<u>Proposed Charge</u>
700	\$ 2.35	\$ 2.80
800	2.60	3.09
900	2.85	3.38
1,000	3.10	3.67
2,500	6.85	8.02
5,000	11.60	13.52

Summary of Earnings

In support of its rate request, applicant presented 16 exhibits and the testimony of 8 witnesses. The record also contains 8 exhibits and the testimony of three Commission staff witnesses pertaining to the independent analysis of applicant's operations undertaken by the staff. Insofar as applicant's Southwest District is concerned, the presentations respecting earnings are summarized and compared in the following tabulations:

Summary of Earnings  
Year 1961 Estimated

Under Existing Water Rates

<u>Item</u>	<u>Applicant</u>	<u>CPUC Staff</u>
Operating Revenues	\$ 2,419,600	\$ 2,433,260
Operating Expenses	1,880,040	1,847,261
Net Revenues	539,560	585,999
Rate Base (Depreciated)	10,338,000	10,078,000
Rate of Return	5.22%	5.81%

Under Water Rates Proposed by Applicant

<u>Item</u>	<u>Applicant</u>	<u>CPUC Staff</u>
Operating Revenues	\$ 2,832,360	\$ 2,848,640
Operating Expenses	2,107,880	2,073,491
Net Revenues	724,480	775,149
Rate Base (Depreciated)	10,338,000	10,078,000
Rate of Return	7.01%	7.69%

Rate Base

As shown in the above tabulation, the rate base derived by the staff is \$260,000 less than that claimed by applicant. The major items contributing to this difference involve (1) contributions in aid of construction, and (2) the weighting to be accorded plant additions.

The problem respecting contributions in aid of construction arises because of applicant's method of accounting for the costs of relocating physical plant facilities at the request or demand of governmental agencies. Briefly stated, applicant from time to time must retire physical facilities in one location and install new facilities in a different location for the benefit of governmental projects. In some instances applicant is reimbursed for the full costs involved. The cost of the new facilities invariably is greater than the cost of the facilities replaced. Applicant has long looked at these transactions as being in effect a sale of property and has recorded the excess of the cost of the new facilities over the cost of the replaced facilities (with appropriate transfer to the depreciation reserve) in its capital surplus account. As early as 1954 applicant sought authorization for such treatment and by letter of March 25, 1954 this Commission outlined the specific procedure to be followed and authorized a crediting of the remaining balance to applicant's surplus account. Since such time, applicant has consistently followed such procedure and authorization and its reports to the Commission have included such amounts as separate items in the surplus accounts. In the instant proceeding the staff has taken the position that applicant should not credit such amounts to surplus but that the amounts should be treated as contributions in aid of construction. The staff has thus deducted an average weighted amount of \$82,502 from utility plant in determining its 1961 rate base for applicant's Southwest District.

While the method of accounting for relocation project reimbursements now followed by the Commission is that to which the staff has adhered in this proceeding, the record is clear that applicant has not heretofore been informed that it should revise its method to conform thereto. Applicant has meticulously followed the accounting procedure authorized in 1954 and its certified financial statements to its stockholders and to financial institutions have reflected such accounting since that time. In view of such evidence, the Commission finds that a reversal of entries at this late date would be unfair to applicant and not in the public interest. As to the future, however, applicant is hereby placed on notice that beginning with the year 1963 applicant will be expected to revise its accounting procedure so as to reflect any future relocation project reimbursements as an element of contributions in aid of construction. The deduction of \$82,502 from applicant's fixed capital accounts, as made by the staff in this proceeding, will not be made herein.

With respect to the weighting to be accorded plant additions for the test year 1961, we shall adopt the staff-derived figure of \$68,746 rather than applicant's claimed \$225,698 amount. In this regard, the evidence demonstrates that applicant has considered its 1961 budgeted amounts for all plant additions, except those attributed to new business, as being in place and operative as of the first of such year. In effect, applicant has thus derived an end-of-year rather than an average rate base for such plant items. The staff, on the other hand, essentially used actual 1961 gross additions in the total amount of \$175,383. Such amount as weighted by the staff is proper for the test year 1961 and will be used herein.

One other element of rate base deserves comment. An allowance of \$220,600 for working cash is claimed by applicant. The figure developed by the staff is \$196,900. These amounts are derived from "lead-lag" studies. In view of the evidence, we find the staff-calculated amount to be more accurate and it will be adopted for the test year 1961.

To summarize, the average depreciated rate base which this Commission finds to be fair and reasonable for the test year is \$10,160,018 derived as follows:

Weighted Average Utility Plant	\$12,561,745
Contributions in Aid of Construction	(613,686)
Advances for Construction	(609,700)
Full Year Weighting of Additions	68,746
Non-operative Property	(4,498)
Materials and Supplies	76,740
Working Cash	196,900
Depreciation Reserve	<u>(1,516,229)</u>
Rate Base	\$10,160,018

(Subtractive Amount)

Revenues and Expenses

In this proceeding both applicant and Commission staff basic presentations of revenues and expenses are on a so-called 'normalized' basis. Differences in these two presentations result not from differences in method but rather from the periods considered in the normalizing process. In this respect, applicant in general made its estimates at an earlier date and had some four or five months less actual data at hand than did the staff. In the light of the evidence the Commission finds the staff-estimated revenues and expenses to be reasonably representative of operations during the 1961 test year on the normalized basis. With appropriate adjustments to reflect the depreciation and tax expense effects of the hereinabove adopted plant items, such normalized revenues and expenses become the following:

Operating Revenues and Expenses,  
Normalized Basis  
Test Year 1961

<u>Item</u>	<u>Existing Rates</u>
Operating Revenues	\$2,433,260
Operating Expenses:	
Operating and Maintenance	836,940
Admin. and General	132,350
Depreciation	266,320
Taxes	614,200
Total Operating Expenses	<u>\$1,849,820</u>
Net Revenue	583,440

Also in evidence is a summary of earnings statement based upon recorded results of operations for each of the years 1956 through 1960 and for the year 1961 using ten months recorded and two months estimated data. Under existing water rates, the years 1959 through 1961 are particularly pertinent to this proceeding, since existing rates were established in 1959. These recorded or actual results may be summarized as follows:

Revenues and Expenses, Recorded Basis  
Years 1959 - 1961<sup>a</sup>

<u>Item</u>	<u>1959</u>	<u>1960</u>	<u>1961*</u>
Operating Revenues	\$2,239,325	\$2,501,849	\$2,614,715
Operating Expenses	1,631,730	1,809,394	1,883,260
Net Revenue	607,595	692,455	731,455

a - from Exhibit No. 18.

\* - 10 months actual, 2 months estimated

Rate of Return

Relating the above-indicated net revenues to the corresponding rate bases indicates rates of return as follows:

Rates of Return,  
Under Existing Water Rates

<u>Item</u>	<u>1959<sup>a</sup></u>	<u>1960<sup>a</sup></u>	<u>1961<sup>b</sup></u>	<u>1961<sup>a</sup></u>
Net Revenue	\$ 607,595	692,455	583,440	\$ 731,455
Rate Base	9,243,900	\$9,731,300	\$10,160,018	10,160,018
Rate of Return	5.57%	7.12%	5.74%	7.20%

a - recorded basis, as above

b - normalized basis

The record contains extensive evidence respecting the level of rate of return which applicant feels it should be accorded. The bulk of such evidence consists of statistical financial comparisons with other utilities in various parts of the United States. A study of such comparisons reveals that applicant, in general, is in a favorable position. The evidence is clear that over the past ten years applicant has generally shown good earnings, overall, and has been successful in financing its growth.

In arriving at a conclusion as to what constitutes a reasonable rate of return, it is not possible to rely on the use of a formula alone. The finding of the Commission in this respect must represent the exercise of judgment after giving consideration to all of the circumstances surrounding each case. This Commission has so often and so variously stated those elements which collectively determine its judgment as to what may constitute a fair and reasonable rate of return that it should be unnecessary to restate them here. Suffice it to say, however, that this Commission does not fix the return to be allowed a utility on the basis of outstanding shares of common stock and the annual dividends paid on such shares. The number of shares and the dividends paid reflect the exercise by applicant of its managerial judgment. This judgment is not to be substituted for the Commission's judgment when the Commission is called upon to fix rates for service. The Commission does, however, weigh the evidence and such facts as may pertain to security issues and earnings thereon. The Commission considers a utility's past



financing success and its future prospects in any rate proceeding. It considers many other elements as well.

The evidence in this proceeding, as illustrated by the foregoing summary tabulations, shows that during the period that applicant's present water rates have been effective, applicant's Southwest District operations have produced rates of return in the range of 6.57 to 7.12 percent on a recorded basis. On a normalized basis, a 1961 rate of return of 5.74 percent has been realized, while the estimated recorded rate of return was 7.20 percent.

The wide range between the normalized and recorded results of operations leads the Commission to question the advisability of applying normalization methods to the Southwest District operation, particularly in view of the fact that in applicant's Bloomington, Calipatria-Niland and Ojai operations (where the same normalization methods were employed), the recorded and normalized results practically coincided. There are factors present in the Southwest District which are not related to climatological influences and which are not present in the other three districts. The Commission concludes that water usage characteristics in this district differ from those in applicant's other systems.

The Commission finds that the normalization methods presented herein, when applied to the Southwest District operations, produce estimated operating results which should not be solely relied upon for rate-fixing purposes and that under the circumstances disclosed by the record in this proceeding, the recorded results provide a more reasonable basis for measuring the need for rate relief.

Based upon such recorded results, the Commission finds that they reasonably represent applicant's future operations in the

Southwest District; that such results are and will be just and reasonable and that they do not clearly and convincingly establish that applicant is in need of or entitled to increased revenues at this time. It follows, therefore, that applicant's request for increased water rates should be denied.

Service Matters

During the course of this proceeding one of applicant's customers complained of a periodic accumulation of sand in his water lines and appliances. The evidence indicates that such complaint was an isolated occurrence which, however, applicant is alleviating by more frequent flushing of mains in the area.

A representative of one other customer complained about an alleged inadequacy of water mains to provide private fire protection service. This matter is one of tariff provisions governing a specialized service commonly called fire sprinkler service. From the evidence respecting this problem, the Commission concludes that applicant is properly administering its tariff for such service and that complainant's recourse is to comply with the provisions of the tariff.

The evidence respecting an investigation of service conditions, as made by the staff engineers of the Commission, shows that applicant's facilities are well-maintained and operated and that the utility is rendering good water service to its customers. Further, applicant promptly responds to such complaints as are brought to its attention.

O R D E R

Based upon the evidence and the findings and conclusions set forth in the foregoing opinion,

IT IS ORDERED that the application of Southern California Water Company to increase rates for water service rendered in its Southwest District be and it is hereby denied.

IT IS FURTHER ORDERED that Case No. 7210 be and it is hereby discontinued.

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

Dated at San Francisco, California, this 17th day of JULY, 1962.

George T. Grover  
President  
W. J. Mitchell  
E. J. ...  
Walter ...  
Fredrick B. Holbrook  
Commissioners