

ORIGINAL

Decision No. 67645

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of MERCED WATER COMPANY)
for an order of the Public Utilities)
Commission of the State of California)
authorizing increased water rates in)
the City of Merced and adjacent)
territory.)

Application No. 46069
(Filed January 2, 1964)

Morrison, Foerster, Holloway, Clinton &
Clark, by Richard J. Archer, for
applicant.
William Bricca and John Gibbons, for
the Commission staff.

O P I N I O N

Applicant Merced Water Company seeks authority to increase its rates for water service.

A public hearing on this application was held before Examiner Catey in Merced on April 28, 1964, and the matter was submitted on that date. Copies of the application, the amendment filed April 3, 1964, and notice of hearing had been served in accordance with this Commission's rules of procedure.

At the hearing, testimony on behalf of applicant was presented by its superintendent, its treasurer and an accountant. The Commission staff presentation was made by an engineer and two accountants. One customer testified regarding the relationship between flat rates and metered service rates.

Service Area and Water System

Applicant's service area consists of the City of Merced and adjacent unincorporated territory in Merced County.

Applicant's water supply is obtained from ten wells equipped with pumps driven by electric motors. Water from these wells is pumped directly into the system or into three elevated storage tanks. Standby engines located at each tank site can utilize natural gas, gasoline or butane as fuel to drive the well pumps at those sites in the event of an electric power failure. The water is distributed through almost 100 miles of cast iron mains ranging up to 16 inches in diameter, to some 7,000 customers. About one-seventh of the customers, primarily commercial and industrial users, are on metered services; the rest receive flat rate service.

Rates and Rules

Applicant's present rates were established in 1954 in applicant's previous general rate increase application. They consist of schedules for general metered service, residence and church flat rate service, school and public park flat rate service, public fire hydrant service, private fire protection service, and flat rate service from fire hydrants.

Applicant proposes to increase the rates for general metered service, the rates for residence and church flat rate service, the rate per 1,000 square feet of premises under the schedule for school and public park flat rate service and the rate for street sweeper use under the schedule for flat rate service from fire hydrants. No other changes are requested in the schedules except the proposed deletion of temporary service to a circus or carnival under the schedule for flat rate service from fire hydrants.

Following is a comparison of applicant's present general metered service rates with those requested in the application, based upon service through a 5/8 x 3/4-inch service. Similar comparisons are included for the various flat rates which applicant proposes to increase:

TABLE I

Comparison of Rates

<u>Item</u>	<u>Per Customer Present</u>	<u>Per Month Requested</u>
<u>Metered Service</u>		
First 1,500 cu.ft. or less	\$2.50*	\$3.05*
Next 2,500 cu.ft., per 100 cu.ft. ....	.15	.17
Next 6,000 cu.ft., per 100 cu.ft. ....	.12	.14
Next 30,000 cu.ft., per 100 cu.ft. ....	.10	.12
Next 60,000 cu.ft., per 100 cu.ft. ....	.075	.08
Over 100,000 cu.ft., per 100 cu.ft. ....	.075	.075

Flat Rate Service

For each single-family residence or church, including a lot having an area of:

First 5,000 sq.ft. or less	\$2.70	\$3.30
Next 5,000 sq.ft., per 500 sq.ft. or fraction thereof .....	.10	.10
Over 10,000 sq.ft., per 1,000 sq.ft. or fraction thereof .....	.15	.15

* A graduated scale of increased minimum charges is provided for services larger than 5/8 x 3/4-inch.

The average monthly consumption by applicant's metered service customers is about 5,300 cubic feet. The charge for that quantity of water under present rates is \$7.81 and under applicant's proposed rates would be \$9.12, or an increase of 17 percent.

The average monthly revenue from applicant's flat rate residential and commercial customers during 1963 was \$3.70. At applicant's present flat rate, this charge would approximate a bill for flat rate service to a single-family residence on a lot

having an area of 10,000 square feet. The corresponding charge for that service under applicant's proposed rates would be \$4.30, or an increase of 16 percent.

Customer Complaints

A Commission staff engineer testified that applicant provides adequate service, both as to quantity and quality of water supply, and that applicant's system is capably managed and efficiently operated. He stated that there have been no informal complaints received by the Commission since the end of 1962 and that the 20 service complaints recorded by the utility during that period were satisfactorily resolved. Applicant's superintendent testified that the service complaints usually relate to sand in the system or to restricted flow in the customers' own plumbing.

One customer testified to alleged inequities between the present flat rates and the rates for metered service. In his opinion, the flat rate customers do not provide their fair share of the total revenue. Testimony by applicant's superintendent showed that, although this customer's bills for metered service were higher during the summer months than they would have been for flat rate service, his average annual bill was actually lower than the applicable flat rate charge.

Results of Operation

Witnesses for applicant and the Commission staff have analyzed and estimated applicant's operational results. Summarized in Table II, from the staff's Exhibit No. 3 and from applicant's amendment to Exhibits F and H attached to the amended application, are the estimated results of operation for the year 1964 under present water rates and those proposed by applicant. For comparison, this table also shows the results of operation adopted herein.

TABLE II
ESTIMATED RESULTS OF OPERATION, YEAR 1964

<u>Item</u>	<u>Staff</u>	<u>Applicant</u>	<u>Adopted</u>
PRESENT RATES			
Operating Revenues	\$ 398,000	\$ 400,105	\$ 398,000
Deductions			
Pump, Transm. & Distr. Exp.	78,700	77,500	78,700
Commercial Exp.	33,200	33,250	33,200
Management Fee	16,000	16,000	18,500
All Other Admin. & Genl. Exp.	27,070	29,799	27,070
Allowance in Lieu of Housing	10,100	-	10,100
Depreciation	45,780	47,605	45,780
Taxes, Other Than on Income	62,020	64,084	62,020
Income Taxes	43,670	48,077	42,400
Total	316,540	316,315	317,770
Net Revenue	81,460	83,790	80,230
Rate Base	1,612,600	1,679,021	1,636,100
Rate of Return	5.1%	4.99%	4.90%
PROPOSED RATES			
Operating Revenues	\$ 459,600	\$ 462,653	\$ 459,600
Deductions			
Pump, Transm. & Distr. Exp.	78,700	77,500	78,700
Commercial Exp.	33,200	33,250	33,200
Management Fee	16,000	18,500	18,500
All Other Admin. & Genl. Exp.	27,070	29,799	27,070
Allowance in Lieu of Housing	10,100	-	10,100
Depreciation	45,780	47,605	45,780
Taxes, Other Than on Income	62,020	64,084	62,020
Income Taxes	75,000	78,617	73,730
Total	347,870	349,355	349,100
Net Revenue	111,730	113,298	110,500
Rate Base	1,612,600	1,679,021	1,636,100
Rate of Return	6.9%	6.75%	6.75% ^{1/}

There are numerous differences between the estimates of applicant and staff but the overall results are very close. The discussion of issues herein has thus been limited to those items wherein the staff estimate has not been adopted or where differences in methods of estimating by applicant and staff warrant explanation.

^{1/} With the estimated annual decline in rate of return adopted herein, the adopted rate of return for 1965 is 6.4%.

Management Fee

Applicant is a wholly owned subsidiary of Crocker Land Company, which in turn is an affiliate of Crocker Estate Company. The latter provides applicant with overall management and supervision, maintains the general ledger and corporate records, and prepares the various tax returns and other governmental reports. Applicant's officers receive no salaries directly from the utility operation.

The fee paid by applicant for the management services provided by Crocker Estate Company has for several years been determined by taking four percent of applicant's annual gross revenue. That basis was used by applicant in preparing its estimates of operating expenses in the current proceeding. However, the witness for applicant who prepared its expense estimates also made a study of the cost to Crocker Estate Company of the management services rendered to applicant. That study indicated that a fair charge would be approximately \$19,500 per year, but Crocker Estate Company apparently will charge only \$18,500 per year until later studies indicate that a change should be made in the fee.

The staff's objections to applicant's estimates of the management fee relate to its arbitrary basis of determination, rather than to the end result. The staff engineering witness testified that the revised amount of \$18,500 which applicant will now pay per year appears reasonable. That amount has been adopted in Table II under both present and proposed rates.

Employee Housing

Five of applicant's employees live in houses on utility property owned by applicant and pay only a nominal rental. Applicant

includes the maintenance costs, taxes and depreciation related to the rental houses in its operating expenses and considers the houses as utility plant. Applicant's witnesses testified to certain advantages accruing to applicant and its customers due to this arrangement, such as having employees readily available in an emergency and avoiding need for hiring night watchmen.

The staff engineer tested the reasonableness of the employee housing arrangement by excluding from his estimated summaries of earnings the net plant investment and expenses related to the rental property and substituting therefor an "allowance in lieu of housing" based upon his estimate of costs which applicant would incur if it did not provide the employee housing. The engineer's testimony shows that the providing of low rent housing by applicant to its employees does not create an additional revenue requirement nor place any burden on applicant's customers.

Depreciation

Applicant determines its depreciation accruals by spreading the cost of individual items of plant over their estimated total lives. If an item of plant is fully depreciated on applicant's books prior to its actual physical retirement, no additional depreciation thereon is accrued. If an item of plant is retired without its having been fully depreciated, applicant includes in operating expenses for the year the item is retired an amount equal to the deficiency in the depreciation reserve related to the retired item.

The staff engineer recommends that applicant adopt the straight-line remaining life method in determining depreciation

accruals. This would eliminate the erratic depreciation charges which could result from applicant's present method.

Income Taxes

Subsequent to the filing of this application, federal income tax rates for 1964 and 1965 were reduced. Applicant then amended its application to request a lesser percentage increase in rates. The income tax estimates prepared by applicant and the staff, and those adopted herein, are all based upon the lower tax rates which become effective January 1, 1965.

Construction Work in Progress

The staff engineer, in developing his estimates of rate base, omitted applicant's construction work in progress at the end of 1963. Applicant does not charge interest during construction. The staff estimate of rate base for 1964 has been adopted with the addition of \$23,500 to offset the omission of construction work in progress.

Rate of Return

In Exhibit No. 6, a staff accountant recommended that applicant be allowed a return of 6 percent on its rate base. This recommendation was based upon the following considerations:

- (a) Applicant's rate of return on equity during any of the last seven years did not exceed 5.64 percent, and this did not hamper applicant's ability to finance additions primarily out of earnings.
- (b) Applicant enjoys the financial stability and backing of its affiliated companies.
- (c) Applicant has elected to finance itself wholly with common stock equity, rather than benefit from tax savings on interest on a reasonable amount of debt capital, and a possible lower cost of total capital.
- (d) The effects of continued inflation indicate the need for slightly increased rates of earnings.

Exhibit No. 6 also shows that applicant's capital structure consists of about 6 percent debt in the form of a 6 percent demand note, and about 94 percent equity. Under these circumstances, it is apparent that a 6 percent rate of return on applicant's rate base would produce only a 6 percent return on its equity, and a 6.4 percent return on rate base would produce less than 6.5 percent return on equity.

In addition to the 1964 estimates set forth herein, both applicant and the staff prepared corresponding estimates for 1963. By comparing the rates of return estimated for the two consecutive years, the trend in rate of return beyond 1964 is indicated. At applicant's proposed rates, an annual decrease of 0.4 percent results from the staff's estimates and 0.32 percent from applicant's. The rate of return of 6.75 percent shown in Table II for the test year 1964 under applicant's proposed rates would thus decline to about 6.4 percent in 1965, the first full year in which the increased water rates and the reduced income tax rates would be in effect.

Considering such factors as adequacy of service, past rate history, anticipated future growth, and quality of management, a rate of return of 6.4 percent for the year 1965 does not appear excessive and applicant's requested increase should be granted.

Findings and Conclusion

The Commission finds that:

1. Applicant is in need of increased revenues.
2. The adopted estimates, previously summarized and discussed herein, of operating revenues, operating expenses and rate base for the year 1964 and the trend of rate of return into

the year 1965 are reasonable and reasonably represent the results of applicant's operations, and a rate of return of 6.4 percent on applicant's rate base for the year 1965 is reasonable for the purposes of this proceeding.

3. The increases in rates and charges authorized herein are justified, the rates and charges authorized herein are reasonable, and the present rates and charges, insofar as they differ from those prescribed herein, are for the future unjust and unreasonable.

4. Applicant's present tariff map, rules and forms should be brought up to date.

5. Applicant should determine depreciation accruals by the straight-line remaining life method.

The Commission concludes that the application should be granted as set forth in the order to follow.

O R D E R

IT IS ORDERED that:

1. After the effective date of this order, applicant Merced Water Company is authorized to file the revised schedule of rates set forth in Appendix A to this order. Such filing shall comply with General Order No. 96-A. The revised rate schedules shall become effective for service rendered on and after September 1, 1964, or on and after the fourth day following the date of filing, whichever is later.

2. Within forty-five days after the effective date of this order, applicant shall file revised tariff service area maps clearly indicating the service area boundaries, appropriate revised general rules and revised copies of printed forms used in

dealing with customers. Such filing shall comply with General Order No. 96-A. The revised tariff sheets shall become effective on the fourth day after the date of filing.

3. Beginning with the year 1964, applicant shall determine depreciation accruals for each primary plant account by dividing the original cost of depreciable utility plant, less estimated future net salvage and less depreciation reserve, by the estimated remaining life of the plant. Applicant shall review the accruals whenever major changes in depreciable utility plant composition occur and for each plant account at intervals of not more than five years. Upon completion of each such review, applicant shall submit promptly to this Commission the results thereof.

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

Dated at San Francisco, California, this 17th day of AUGUST, 1964.

Frederick B. Volkeloff
President
George H. Crow

Commissioners

Commissioner Peter E. Mitchell, being necessarily absent, did not participate in the disposition of this proceeding.

Commissioner William M. Bennett, being necessarily absent, did not participate in the disposition of this proceeding.

APPENDIX A
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Schedule No. 1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Merced and vicinity, Merced County.

(T)

RATES

Quantity Rates:	<u>Per Meter</u> <u>Per Month</u>	
First 1,500 cu.ft. or less	\$ 3.05	(I)
Next 2,500 cu.ft., per 100 cu.ft. ....	.17	|
Next 6,000 cu.ft., per 100 cu.ft. ....	.14	|
Next 30,000 cu.ft., per 100 cu.ft. ....	.12	|
Next 60,000 cu.ft., per 100 cu.ft. ....	.08	(I)
Over 100,000 cu.ft., per 100 cu.ft. ....	.075	
 Minimum Charge:		
For 5/8 x 3/4-inch meter	\$ 3.05	(I)
For 3/4-inch meter	4.00	|
For 1-inch meter	5.00	|
For 1 1/2-inch meter	7.00	|
For 2-inch meter	12.00	|
For 3-inch meter	18.00	|
For 4-inch meter	25.00	|
For 6-inch meter	35.00	|
For 8-inch meter	60.00	(I)

The Minimum Charge will entitle the customer to the quantity of water which that minimum charge will purchase at the Quantity Rates.

(Continued)

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Schedule No. 1

GENERAL METERED SERVICE
(Continued)

SPECIAL CONDITIONS

1. If a customer who is eligible for flat rate service requests and is furnished metered service, a change to flat rate service may not be made until metered service has been taken for a period of 12 consecutive months.

2. Customers whose requirements may overburden the water system, may require unreasonable investment in additional facilities, or may interfere with the supply to the existing customers, will not be supplied water service under this schedule. In such cases a special contract will be required under such terms as the conditions warrant, subject to approval by the Public Utilities Commission of the State of California.

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Schedule No. 2

RESIDENCE AND CHURCH FLAT RATE SERVICE

APPLICABILITY

Applicable to water service furnished on a flat rate basis to residences and churches.

TERRITORY

Merced and vicinity, Merced County. (T)

RATES

	<u>Per Service Connection Per Month</u>	
For each single-family residence or church, including a lot having an area of:		
First 5,000 sq.ft. or less	\$3.30	(I)
Next 5,000 sq.ft., per 500 sq.ft., or fraction thereof .....	.10	
Over 10,000 sq.ft., per 1,000 sq.ft., or fraction thereof .....	.15	
In addition, for each residential unit served from the same service connection	1.50	
In addition, for each 100 cu.ft. of capacity of each swimming pool served from the same service connection	0.05	

SPECIAL CONDITIONS

1. All service not covered by the above classifications will be furnished only on a metered basis.

2. Meters may be installed at option of Company or customer for above classifications in which event service will thereafter be rendered only on the basis of Schedule No. 1, General Metered Service, and must be continued for not less than 12 months before it may again be changed to flat rate service.

(Continued)

Schedule No. 2

RESIDENCE AND CHURCH FLAT RATE SERVICE
(Continued)

SPECIAL CONDITIONS (Contd.)

3. If the customer requires the service connection to be moved or increased to a larger diameter, the customer shall pay the entire cost of removing the existing service and installing the new service. (D)

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Schedule No. 3

SCHOOL AND PUBLIC PARK FLAT RATE SERVICEAPPLICABILITY

Applicable to water service furnished on a flat rate basis to schools and public parks.

TERRITORY

Merced and vicinity, Merced County.

(T)

RATES

	<u>Per Month</u>	
For each service connection 3/4-inch or smaller	\$ 2.00	
For each 1-inch service connection	3.00	
For each 1½-inch service connection	5.00	
For each 2-inch service connection	7.50	
For each 3-inch service connection	15.00	
For each 4-inch service connection	25.00	
For each 6-inch service connection	50.00	
For each 8-inch service connection	100.00	(N)
In addition, for each 1,000 sq.ft. or fraction thereof, per 1,000 sq.ft.	0.05	(I)
In addition, for each building on premises served from the same service connection	3.00	
In addition, for each 100 cu.ft. of capacity of swimming pools on premises served from the same service connection	0.05	

SPECIAL CONDITION

Meters may be installed at option of Company or customer for above classifications, in which event service will thereafter be rendered only on the basis of Schedule No. 1, General Metered Service, and must be continued for not less than 12 months before it may again be changed to flat rate service.

Schedule No. 6

FLAT RATE SERVICE FROM FIRE HYDRANTS

APPLICABILITY

Applicable to water service furnished from fire hydrants on a flat rate basis for municipal, construction and temporary usages.

TERRITORY

Merced and vicinity, Merced County. (T)

RATES

	<u>Per Month</u>	
City of Merced:		
For flushing sewers	\$15.00	
For street sweeper	15.00	(I)
Construction:		
	<u>Per Linear Foot</u>	
For puddling trenches	\$ 0.01	
	<u>Per Estimated 1,000 Gallons</u>	
For sprinkling streets and other uses for street improvement work	\$ 0.15	

SPECIAL CONDITIONS

1. At the option of the Company a meter will be installed for service under this schedule.
2. Applicants for service under this schedule must obtain specific authorization from the Company before taking any delivery of water and shall use only the hydrants designated by the Company.
3. If a hydrant is damaged by a customer, the customer shall pay the cost of repairs thereto.