

# ORIGINAL

Decision No. 73243

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of the Nicholls Warm Springs, A Corporation, dba Mesa Verde Water Co. for authority to increase rates for water service in the vicinity of Blythe, Riverside County.

Application No. 48981  
(Filed November 25, 1966)  
(Amended December 27, 1966)

Edward J. Soehnel, Sr. and Edward J. Soehnel, Jr.,  
for applicant.  
Mrs. James M. Burdett, Betty Copeland, Mrs. Thomas J. Fisher, Mrs. Homer L. Hasler, Vada McBride, and Mr. and Mrs. W. B. Shumaker;  
protestants.  
Maurice B. Hawkins, for Riverside County Department of Public Health; Marshall D. Nelson, for the Nelson Family; Mrs. Jeanette P. Elam, Norman E. Elam, Mrs. Earl F. Laird, Mrs. Alice Little, and Harold C. Mason, interested parties.  
Jerry J. Levander and Raymond E. Heytens,  
for the Commission staff.

## O P I N I O N

Applicant, Nicholls Warm Springs, a California corporation, doing business under the fictitious name of Mesa Verde Water Company, seeks authority to increase its rates for general metered water service and to establish rates for public fire hydrant service in its tariff service area, situated about seven miles west of Blythe, where it presently serves approximately 100 customers.

Public Hearing

At the request of the Commission, applicant sent a notice to each customer regarding the requested rate increases, inviting customers to call the Commission's attention to any problems concerning water service, billing procedure or other factors pertaining to a reasonable charge for water service. The response from customers was such as to make ex parte treatment inappropriate, and a duly noticed public hearing was held in this matter before Examiner Main at Blythe on June 13 and 14, 1967. The matter was submitted on the latter date and is now ready for decision.

Background

For a number of years applicant has been engaged in developing and selling land and providing water service within the area which later became its tariff service area and which as such includes three subdivisions known as Nicholls Warm Springs Units Nos. 1, 2 and 3, containing 382 lots and about 260 acres of unsubdivided land. On or about May 21, 1964, Edward J. Soehnel, Sr. (Soehnel) took over applicant's management by acquiring a controlling interest in the corporation and shortly thereafter embarked upon a water system improvement program to control a sanding problem at the source of supply, to increase and make more reliable the water supply to the distribution system, and to rehabilitate the distribution system to a minor extent. The system still requires extensive replacements of water mains and the installation of valves for proper segmentation.

On or about February 1, 1965, applicant raised its rates for water service, an action which precipitated the formal complaint of the Residents of Mesa Verde vs. Nicholls Warm Springs dba Mesa Verde Water Co., Case No. 8132, filed February 17, 1965. By Decision No. 69188 dated June 8, 1965, applicant was found to be a public utility subject to the jurisdiction of this Commission and ordered to file a schedule for general metered service setting forth rates fixed approximately at the level it had been charging prior to the unauthorized increase. A petition for rehearing of the matter was granted and by Decision No. 69805 dated October 19, 1965 the original decision was affirmed.

In the original decision applicant was further ordered to adopt the straight-line remaining-life method of determining depreciation and to file with the Commission (1) a copy of a water supply permit issued by the appropriate Department of Public Health or a copy of an application for such permit if the permit had not yet been issued, and (2) a report setting forth in detail a determination of the original cost (historical cost appraisal) estimated, if not known, of the properties used and useful in providing water service and also the depreciation reserve requirements applicable to such properties. Applicant has failed to comply with these further orders. Since Soebnel's many years of experience in public utility matters include management and partial ownership of the former Fontana Ranchos Water Company, applicant should be knowledgeable of the seriousness and potential consequences of such failure.

Prior to the filing of the present application, the Commission staff reviewed a draft thereof and made a limited examination of the utility's books and records, consistent with procedures usually followed for small water companies. By letter dated November 2, 1966, the Commission informed applicant that, in the staff's view, the accounting records of applicant and the recorded data in the proposed application were reasonably complete and current for use in a rate proceeding. Applicant shortly thereafter filed the application.

Organization, Ownership and Associated Interests

The principal corporate officers of applicant are: Mabel G. Nicholls, President; Edward J. Soehnel, Sr., Vice President; Edward J. Soehnel, Jr., Secretary-Treasurer. Soehnel owns 51 percent of its outstanding stock and the estates of A. E. Nicholls and Donald G. Dunne own 34 percent and 15 percent, respectively.

Applicant conducts its business through two divisions, a land division known as Mesa Verde Development Company and a water or utility division known as Mesa Verde Water Company, and has its headquarters in San Bernardino together with other Soehnel interests which include five to six firms engaged in the business of land development, real estate appraising or insurance. The employees in the San Bernardino office perform work for applicant as well as the other Soehnel interests and are compensated for the work performed for applicant on an hourly basis.

Water System and Service

Applicant's source of supply is obtained from two wells located within its service area. Well No. 1 was drilled in 1946 to a depth of 365 feet with 12-inch steel casing installed and is presently equipped with a 40-horsepower electric motor directly connected to a deep well turbine capable of delivering 540 gallons per minute through a 5,000-gallon pressure tank into the distribution system at an average system pressure of 30 pounds per square inch. Well No. 2 was drilled in 1956 to a depth of 363 feet with 16-inch steel casing installed and is presently equipped with a 60-horsepower electric motor directly connected to a deep well turbine capable of pumping 740 gallons per minute into the 70,000-gallon steel storage tank adjacent to the well site. Two booster pumps with 15-horsepower electric motors are installed adjacent to the 70,000-gallon storage tank and are capable of delivering 600 gallons per minute through a 10,000-gallon pressure tank into the distribution system with an average system pressure of 30 pounds per square inch. The equipment at Well No. 2 is used for normal system operations. The pump at Well No. 1 is manually started as a supplemental supply to meet abnormal system operating conditions.

The water production and related facilities described above have ample capacity. To some extent such capacity is indicative of applicant's future construction and development plans for unbuilt-on lots and for the unsubdivided land in its tariff service area. The water produced, however, is of poor quality as indicated by its total dissolved solids content of 1440 milligrams per liter including 2.4 milligrams per liter of fluorides. The status of the health permit for this system is under review by the Riverside County Department of Public Health.

The distribution system includes about 12,700 feet of unwrapped steel mains and 8,700 feet of cement-asbestos mains ranging in size from 3 to 8 inches in diameter. The steel mains were installed in Unit No. 1 of the subdivision development beginning in 1947, and the asbestos-cement mains were installed in Units Nos. 2 and 3 beginning in 1961. Valves have not been provided in the distribution mains to segment the system. There are fire hydrants in Units Nos. 2 and 3. Service connections are of galvanized steel pipe, copper, and plastic tubing. All customers are served on a metered basis.

Service is impaired by the deteriorated condition of steel mains installed in Unit No. 1 and installed in all of Mesa Drive. Major breaks are frequent and at such times the entire system must be shut down because of inadequate valving. To replace the most deteriorated mains, those installed in Mesa Drive and Blythe Way plus a few feeder lines, and to install reasonably-spaced valves throughout the system, applicant indicates that it would cost between \$20,000 and \$30,000 based upon an estimate made about two years ago.

A part-time employee operates and maintains the system. When necessary, outside services are used for major repairs or other work. Customer billing is performed at the San Bernardino office.

#### Rates

Applicant's present tariffs, including its schedule for general metered service, were filed March 23, 1966 and became effective March 27, 1966. The following Table 1 sets forth a comparison of applicant's present rates, those requested by applicant, and those authorized herein, together with representative monthly charges at several consumption levels for each set of rates.

TABLE 1

A - Comparison of Rates

	<u>Present</u>	<u>Proposed</u>	<u>Authorized Herein</u>	
			<u>Without Plant Improvements</u>	<u>With Plant Improvements</u>
<u>General Metered Service</u>				
Quantity Rates per meter per month:				
First 2,600 cu.ft. or less	\$3.50	-		
Next 6,700 cu.ft., per 100 cu.ft.	.20	-		
Next 5,200 cu.ft., per 100 cu.ft.	.15	-		
Over 14,500 cu.ft., per 100 cu.ft.	.10	-		
First 1,000 cu.ft. or less		\$5.00	\$ 3.95	\$ 5.00
Next 2,000 cu.ft., per 100 cu.ft.		.25	.22	.25
Over 3,000 cu.ft., per 100 cu.ft.		.20	.16	.20
Minimum Charge:				
For 5/8 x 3/4 inch meter	\$3.50	\$5.00	\$ 3.95	\$ 5.00
For 3/4 inch meter	4.00	7.50	5.25	6.50
For 1 inch meter	6.00	9.00	7.50	9.00
<u>Public Fire Protection Service</u>				
Per Hydrant per month	\$ -	\$2.00	-	-

B - Comparison of Monthly Charges

<u>Monthly Consumption in Cubic Feet</u>	<u>Applicant</u>		<u>Rates Authorized Herein</u>	
	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Without Plant Improvements</u>	<u>With Plant Improvements</u>
1,000	\$3.50	\$5.00	\$ 3.95	\$ 5.00
2,500	3.50	8.75	7.25	8.75
4,000	6.30	12.00	9.95	12.00
10,000	17.95	24.00	19.55	24.00

To improve the rate design, a pronounced departure from the blocking used in the present rate structure is necessary.

For the monthly consumptions of 1,000, 2,500, 4,000 and 10,000 cubic feet shown, the proposed rates and rates authorized herein with plant improvements produce increases of 43, 150, 90 and 34 percent, respectively. For the rates authorized herein without plant improvements, the comparable increases are 13, 107, 58 and 9 percent.

The request to establish public fire protection water service and to charge a rate of \$2 per hydrant per month therefor is premature, since applicant has not made suitable arrangements with the public authority, probably the State Division of Forestry, providing fire protection within applicant's tariff service area. Accordingly, we will not authorize applicant to establish such service at this time, but applicant can, as is often done by utilities under our jurisdiction in establishing this type of service, negotiate contractual conditions of service and rates with the fire protection district or authority and then file with the Commission by advice letter, pursuant to General Order 96-A, the appropriate tariff schedule and related contract.

#### Results of Operation

By its failure to comply with the pertinent order in Decision No. 69188, as previously stated, applicant must bear the responsibility for the original cost of total utility plant and its related depreciation reserve not being available for consideration in this record. Further, it is contended by the staff, and denied by applicant, that the staff was not given full access to the corporate books and records of applicant.



An examination of such books and records might have enabled the staff to ascertain the cost of utility plant and determine a proper basis for computing depreciation accruals for both accounting and rate-making purposes. Irrespective of the opposing contentions, the staff examined the books of the water division only.

Subject to the foregoing limitation which affects determinations of rate base and depreciation expense, witnesses for applicant and the Commission staff have analyzed and estimated applicant's operational results. Summarized in Table 2 herein, from pages 3 and 4 of the application and from the staff's Exhibit 6, are the estimated results of operations applicable to test year 1967 under present water rates and those proposed by applicant. While it should be clarified that the operational results estimated by applicant and those estimated by the staff correspond to 12-month periods ending May 31, 1967 and December 31, 1967, respectively, this difference is not significant in view of the stable level of operations during the present depressed building activity in the area. For comparison, this table also shows the results of operation at the rates authorized herein.

TABLE 2

Estimated Results of Operation - Test Year 1967

<u>Item</u>	<u>Present Rates</u>		<u>Proposed Rates</u>	
	<u>Applicant</u>	<u>Staff</u>	<u>Applicant</u>	<u>Staff</u>
<u>Operating Revenues</u>				
Metered Sales	\$ 6,824	\$ 6,150	\$ 8,448	\$10,130
Fire Protection	-	-	-	290
Total	<u>6,824</u>	<u>6,150</u>	<u>8,448</u>	<u>10,420</u>
<u>Deductions</u>				
Operating Expenses	10,150	6,300	10,150	6,300
Depreciation	3,200	800	3,200	800
Taxes other than Income	-	470	-	470
Income Taxes	-	100	-	200
Total	<u>13,350</u>	<u>7,670</u>	<u>13,350</u>	<u>7,770</u>
Net Revenue	(6,526)	(1,520)	(4,902)	2,650
Rate Base	20,380*	-	20,380*	-
Rate of Return	-	-	-	-

	<u>Rates Authorized Herein</u>	
	<u>Without Plant Improvements</u>	<u>With Plant Improvements</u>
<u>Operating Revenues - Metered Sales only</u>	\$ 8,220	\$10,130
<u>Deductions</u>		
Operating Expenses	6,300	5,800
Depreciation	500	1,000
Taxes other than Income	470	470
Income Taxes	100	100
Total	<u>7,370</u>	<u>7,370</u>
Net Revenue	850	2,760
Rate Base	17,000	42,000
Rate of Return	5%	6.6%

(Red Figure)

\* Rate base revised for arithmetical error in computation.

From Table 2 it can be seen that applicant's requested rates would result in an increase of \$3,980 or 65 percent in metered sales revenue, whereas the rates-without plant improvements-authorized herein, will produce a 34 percent increase. If applicant is able to finance and install an estimated \$25,000 in basic distribution system improvements, the rates-with plant improvements-authorized herein could become effective and would yield the same level of revenues as the rates proposed by applicant.

The method of estimating revenues used by applicant is set forth in Exhibit 1. In essence, it relates at present rates the monthly minimum revenue, which would be derived if all customers were to receive minimum bills, to the monthly average revenues for summer and winter months, and assumes that the resulting ratios hold for the computation of revenues at proposed rates. Among other deficiencies, applicant's method fails to measure properly the effect of the changes in rate blocking proposed by applicant. The staff's estimates of metered sales revenue were based upon a water use table whose accuracy was found to be within two percent based on recorded revenues.

Applicant's estimate of \$10,150 in operating expenses exceeds the staff estimate by \$3,850. This difference is due mainly to an expensed management salary of \$3,600 which applicant has included in addition to operating and maintenance salaries. The staff has estimated expensed salaries totaling \$2,900 which it considers reasonable for a utility of this size and set of operating characteristics. In terms of customers served, the \$2,900 represents about \$2.25 per customer per month.

Applicant did not determine its estimated depreciation expense of \$3,200 by the straight-line remaining-life method as required by Decision No. 69188, supra. Applicant's estimate reflects its practice of using very short plant lives in computing depreciation for both income tax and book purposes. The staff estimate of \$800 reflects a composite accrual rate of 2.6 percent applied to \$30,583 of depreciable utility plant, a substantial portion of which was installed after June 1, 1964.

In estimating its rate base, applicant used a cost of total utility plant of \$85,905, a depreciation reserve of \$65,285 and a working capital allowance of \$240. The staff did not compute an estimated rate base because recorded utility plant costs as of June 1, 1964 were not verified. Without such verification the rate base estimated by applicant does not have probative value.

In Exhibit 6 the position of the staff is set forth as follows:

"The staff recommends that rate base and rate of return not be considered as factors for determining rates to be authorized in this proceeding. Applicant's rates should be increased to produce gross revenues of approximately \$7,670 for the estimated year 1967; such gross revenues would compensate applicant for costs of service other than return. After applicant has complied with all Commission orders relating to its operations, and at such time as its corporate records are made available to the Commission and its staff, applicant might seek further rate relief including consideration of return on rate base."

Fundamentally, the effect of this staff recommendation is to allow for the recovery of an investment in utility plant but not for earnings on such investment. Perhaps the failure of

applicant to comply with certain orders of the Commission would justify an inconsistency in the treatment of utility plant for depreciation expense and rate base purposes. It appears preferable, however, to separate to the extent practicable the elements of rate fixing and compliance contained in the staff recommendation. In this way, our adopted operational results, which reach the ultimate issue of determining just and reasonable rates, can include rate base and return and the compliance matters can be properly placed within the purview of those provisions of the Public Utilities Code which provide for adequate means to enforce compliance with the orders of the Commission. Applicant is placed on notice that continued noncompliance with decisions and other requirements of this Commission will not be tolerated.

Utility plant installed after June 1, 1964 appears to be properly includable in rate base, since, according to the record herein, its cost and year of installation are known and it represents investment by applicant. Such plant was installed mainly under the system improvement program mentioned previously and has a recorded cost of \$17,242.

In the adopted operational results, without-plant-improvements shown in Table 2, the rate base of \$17,000 reflects said recorded cost of utility plant, a depreciation reserve computed on the basis of a 3 percent composite accrual rate and a judgment allowance of \$1,000 for working capital. The rate of return of 5 percent recognizes the impaired quality of service presently rendered.

In the adopted operational results/with-plant-improvements, the rate base has been increased to \$42,000 by including \$25,000 of required plant improvements and appropriate adjustments have been made to operating expenses and depreciation. Income taxes remain unchanged at the \$100 level, which is the minimum state corporation franchise tax, primarily because of the high depreciation accruals used by applicant for income tax purposes. A 6.6 percent rate of return results at the rates proposed by applicant and also at the rates authorized herein subject to the conditions set forth in the order herein.

Discussion

Applicant's principal business of developing and selling property within its tariff service area influences the proper balance sought by the Commission of the interests of the utility and its customers.

To provide some perspective and background on this matter, we observe that it is usual Commission practice to place an applicant, for certificate authority to construct a water system in a new area, on notice that operating losses may be expected until the area develops and to require as a condition precedent to certification a commitment from stockholders to provide additional funds as required until such time as the utility's income is adequate to cover all out-of-pocket operating expenditures.

In the present situation, the combination of low customer density and a small number of total customers makes the economics of applicant's utility operation unfavorable, limits its ability to obtain suitable financing and points to the need for financial assistance from the land development side of applicant's business. Such assistance is needed now to make basic improvements to the water system in order to provide reliable service to existing customers and should not be deferred until prospective home or lot purchasers and banks or other lenders make the needed improvements essential from a developer's viewpoint as building activity resumes in the area. Such a delay would be incompatible with the high degree of responsibility and trust, which a public utility, its officers and management have to the public they serve.

Further, applicant drew a comparison of its rates for general metered service with the rates of Yermo Water Company and the rates of Daggett Water Company as part of its affirmative showing. While applicant failed to establish sufficient comparability of operating costs and plant investment among the three utilities for us to give the rate comparison weight herein, applicant can justify its proposed rates on a cost basis alone, if it makes the needed improvements to its water system, as shown by the appropriate adopted operating results for test year 1967. In this way not only the rates but also the service could be at comparable levels for the three utilities.

Findings and Conclusions

1a. Applicant is in need of a rate increase but the proposed rates set forth in the application are excessive unless certain plant improvements are made.

b. The cost of total utility plant and the related depreciation reserve set forth in the application do not have probative value; our adopted estimates of operational results for test year 1967 include rate base and depreciation to the extent these items are supported by the record herein.

c. The adopted estimates, previously summarized and discussed herein, of operating revenues, operating expenses, depreciation, taxes and rate base for test year 1967 reasonably represent the results of applicant's future operations.

d. A rate of return of 5 percent on applicant's rate base is reasonable unless applicant makes the plant improvements needed to eliminate frequent systemwide outages; a rate of return of 6.6 percent, which is the level the rates proposed by applicant yield in our adopted operational results/with-system-improvements for test year 1967, will be reasonable upon timely completion of the needed improvements. These improvements consist of replacing the deteriorated steel distribution mains installed in Mesa Drive and Blythe Way and all deteriorated steel feeder mains and of installing suitably-spaced valves throughout the system; they are estimated to cost between \$20,000 and \$30,000.

e. 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.



2. Applicant has failed to comply with paragraphs 4, 5 and 6 of the order in Decision No. 69188 dated June 8, 1965 in Case No. 8132.

3. Applicant does not maintain its books of account on an accrual basis for revenue accounting as required by the Uniform System of Accounts for Class D water utilities.

4. Applicant's annual report to the Commission for year 1966 did not contain its corporate Balance Sheet; the Balance Sheet as reported therein is comprised only of those items pertaining to the water division.

The Commission concludes that the application should be granted to the extent, and under the conditions, set forth in the order which follows and that applicant should be required to take the actions set forth therein.

O R D E R

IT IS ORDERED that:

1. After the effective date of this order, applicant, Nicholls Warm Springs doing business as Mesa Verde Water Company, is authorized to file the revised rate schedule attached to this order as Appendix A. Concurrently, applicant shall cancel the presently effective Schedule No. 1, General Metered Service. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedule shall be December 1, 1967 or four days after the date of filing, whichever is later. The revised schedule shall apply only to service rendered on and after the effective date thereof.

2. If applicant shall have completed the plant improvements set forth in finding 1d herein on or before June 1, 1968 to the satisfaction of the Commission, it shall be authorized by supplemental order in this proceeding to file the rate schedule set forth in Appendix B to the order herein. Within ten days after completion of said plant improvements, applicant should submit a report to the Commission setting forth the details and cost of the improvements.

3. Within ninety days after the effective date of this order, applicant shall comply with paragraphs Nos. 4, 5 and 6 of Decision No. 69188 dated June 8, 1965 in Case No. 8132.

4. Applicant shall maintain its books of account on an accrual basis for revenue accounting.

5. Applicant's annual reports to the Commission shall contain its corporate balance sheet and shall cover its operations on a calendar year basis.

6. Applicant shall not extend service to any new tract or subdivision unless and until the Commission, upon a satisfactory showing to the effect that the plant improvements set forth in

finding ld herein have been made, shall have modified this service restriction by subsequent order.

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

Dated at San Francisco, California, this 24<sup>th</sup> day of OCTOBER, 1967

[Signature]  
President

[Signature]

[Signature]

[Signature]

[Signature]  
Commissioners

## APPENDIX A

## Schedule No. 1

METERED SERVICE

(T)

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Mesa Verde and vicinity, approximately 7 miles west of Blythe, Riverside County.

RATES

	<u>Per Meter</u> <u>Per Month</u>	
Quantity Rates:		
First 1,000 cu.ft. or less .....	\$3.95	(I)
Next 2,000 cu.ft., per 100 cu.ft. ....	.22	
Over 3,000 cu.ft., per 100 cu.ft. ....	.16	(I)
Minimum Charge:		
For 5/8 x 3/4-inch meter .....	\$3.95	(I)
For 3/4-inch meter .....	5.25	
For 1-inch meter .....	7.50	(I)

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

## APPENDIX B

## Schedule No. 1

METERED SERVICEAPPLICABILITY

Applicable to all metered water service.

TERRITORY

Mesa Verde and vicinity, approximately 7 miles west of Blythe, Riverside County.

RATES

	<u>Per Meter</u>	
	<u>Per Month</u>	
Quantity Rates:		
First 1,000 cu.ft. or less .....	\$5.00	(I)
Next 2,000 cu.ft., per 100 cu.ft. ....	.25	
Over 3,000 cu.ft., per 100 cu.ft. ....	.20	(I)
Minimum Charge:		
For 5/8 x 3/4-inch meter .....	\$5.00	(I)
For 3/4-inch meter .....	6.50	
For 1-inch meter .....	9.00	(I)

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