

Decision No. 74308**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
CALIFORNIA WATER SERVICE COMPANY, a
corporation, for an order authoriz-
ing it to increase rates charged for
water service in the East Los Angeles
district.

Application No. 49838
Filed December 4, 1967

McCutchen, Doyle, Brown & Enersen, by
A. Crawford Greene, Jr., for applicant.
William C. Bricca, Counsel, and Richard D.
Gardner, for the Commission staff.

O P I N I O N

Applicant California Water Service Company seeks authority to increase rates for water service in its East Los Angeles district.

Public hearing was held before Examiner Catey in Montebello on April 2, 1968. Copies of the application had been served and notice of hearing had been published and posted, in accordance with this Commission's rules of procedure. The matter was submitted on April 2, 1968.

Testimony on behalf of applicant was presented¹ by its president, its vice president and his assistant, and its general manager. The Commission staff presentation¹ was made through two accountants and two engineers. No customers attended the hearing.

Service Area and Water System

Applicant owns and operates water systems in 21 districts in California. Its East Los Angeles district includes a section of

¹ Testimony relating to overall company operations had been presented by witnesses for applicant and the staff in Applications Nos. 49443 and 49837, the Salinas and Bear Gulch Districts rate proceedings. This testimony was incorporated by reference in Application No. 49838.

unincorporated area of Los Angeles County between the cities of Los Angeles and Montebello, and portions within the city limits of Commerce, Montebello and Vernon. The service area slopes from 145 feet to 632 feet above sea level. Total population served in the district is estimated at 84,400.

The water supply for this district is obtained from two sources. About 60 percent is produced by applicant's 39 wells. The rest is obtained from West Basin Municipal Water District (WBMWD) through three separate connections to pipelines of Metropolitan Water District of Southern California (MWD). The transmission and distribution system includes about 268 miles of distribution mains, ranging in size up to 24-inch. There are about 25,500 metered services, 420 private fire protection services and 1,640 public fire hydrants. Two reservoirs, 20 storage tanks and 28 booster pumps maintain system pressure and provide storage in 10 separate pressure zones. Each booster pump has an electric motor and provision for emergency connection to portable, gasoline-powered pumps normally stationed in the district.

A field investigation of applicant's operations, service and facilities in its East Los Angeles district was made by the Commission staff. The plant was found to be in good operating condition and satisfactory service was being provided. Only three informal complaints have been registered with the Commission during the past three years. A staff review of customer complaints in applicant's files showed that most of them were related to temporary conditions of dirty water, which has generally been corrected by flushing mains. Applicant has a regular main flushing program in areas particularly susceptible to this problem.

Rates

Applicant's present tariffs include schedules for general metered service, private fire protection service, public fire hydrant service and service to company employees. The present general metered service rates became effective January 1, 1965.

Applicant proposes to increase its rates for general metered service. There are no proposed changes in the other schedules. The following Table I presents a comparison of applicant's present general metered service rates and those requested by applicant. For the average of 1,800 cubic feet per month used by commercial customers, through a 5/8 by 3/4-inch meter, the monthly charge will increase 23 percent, from \$5.69 under present rates to \$7.01 under proposed rates.

TABLE I
Comparison of Monthly Rates

<u>General Metered Service</u>	<u>Present Rate</u>	<u>Proposed Rate</u>
Service Charge*	\$2.45	\$3.00
Quantity Rate:		
First 30,000 cu.ft., per 100 cu.ft.	0.18	0.223
Over 30,000 cu.ft., per 100 cu.ft.	0.17	0.210

* Service charge for a 5/8 x 3/4-inch meter. A graduated scale of increased charges is provided for larger meters.

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. 8 (modified to reflect the testimony of a staff engineer as to the effect of a recently negotiated wage adjustment) and applicant's Exhibit No. 4 are the

estimated results of operation for the test year 1968, under present rates and under those proposed by applicant.

TABLE II

Estimated Results of Operation
(Test Year 1968)

<u>Item</u>	<u>Applicant</u>	<u>Staff</u>	<u>Modified</u>
<u>At Present Rates</u>			
Operating Revenues	\$2,371,900	\$2,371,900	\$2,371,900
<u>Deductions</u>			
Purchased Water and Power Expense ...	556,100	543,600	550,100
Customer Accounting Expense	158,500	152,300	158,500
District Maintenance Expense	202,500	180,800	191,600
Allocated Oper. & Maintenance Expense	36,600	32,400	32,400
Wage Adjustment	*	10,800	10,800
Ad Valorem Taxes	172,100	160,800	160,800
Depreciation Expense	257,100	255,200	255,200
All other Expense, Excluding Franchise and Income Taxes	436,500	437,100	436,800
Subtotal	1,819,400	1,773,000	1,796,200
Local Franchise Taxes	33,700	33,700	33,700
Income Taxes	104,700	123,400	117,900
Total	1,957,800	1,930,100	1,947,300
Net Revenue	414,100	441,800	424,100
Rate Base	9,250,700	9,160,900	9,160,900
Rate of Return	4.48%	4.82%	4.63%
<u>At Rates Proposed by Applicant</u>			
Operating Revenues	\$2,911,600	\$2,911,600	\$2,911,600
<u>Deductions</u>			
Excluding Franchise and Income Taxes	1,819,400	1,773,000	1,796,200
Local Franchise Taxes	41,300	41,300	41,300
Income Taxes	379,500	398,200	392,800
Total	2,240,200	2,212,500	2,230,300
Net Revenue	671,400	699,100	681,300
Rate Base	9,250,700	9,160,900	9,160,900
Rate of Return	7.26%	7.63%	7.44%

* Applicant presented no revised estimate.

From Table II it can be determined that the rates requested by applicant will result in an increase of 23 percent in operating revenues.

The principal differences between the estimated results of operation for the test year 1968 presented by applicant and those presented by the Commission staff are in the estimates of (1) purchased water and power expense, (2) customer accounting expense, (3) district maintenance expense, (4) allocated operating and maintenance expense, (5) ad valorem taxes, (6) depreciation expense, and (7) rate base. The staff checked, verified and adopted applicant's estimates of revenues, certain operating expenses and most rate base components.

Operating Expenses

The difference between applicant's and the staff's estimates of purchased water and power results from a difference in the amount of "unaccounted-for" water used for such purposes as fire protection and flushing of mains and lost because of such causes as leakage and evaporation. Applicant estimated that unaccounted-for water would be 9.6 percent of total production, based upon the average experienced during the 5-year period ended with 1966. The staff's corresponding estimate was 8.5 percent, apparently based upon the average experienced during the 6-year period obtained by excluding the high-percentage years 1962 and 1963 from the 8-year period ended with 1967. By its very nature, the amount of unaccounted-for water can be expected to fluctuate from year to year and, in the absence of evidence of nonrecurring abnormalities in the years 1962 and 1963, the higher percentages experienced in those years should not be excluded in determining an estimated average for the future. The averages for the past six years, seven

years and eight years are all 9.1 percent, which is reflected in the expense for purchased water and power adopted in Table II.

The difference between applicant's and the staff's estimates of customer accounting expense results primarily from the staff's assumption that there is a possibility of savings in expenses due to conversion of billing functions to electronic data processing. No evidence was presented as to the nature, magnitude or timing of the assumed savings, and they appear to be too nebulous for consideration at this time. Applicant's estimate of customer accounting expense is adopted in Table II.

The difference between applicant's and the staff's estimates of district maintenance expense results primarily from differences in estimated level of average expense of maintaining transmission and distribution mains. The staff contends that applicant's estimates do not give sufficient recognition to the reduced level of repairs of mains reasonably expected to have resulted from applicant's long-standing main replacement program. Applicant contends that the staff estimate does not give sufficient recognition to work required as the result of freeway alterations which have taken place in the past and are scheduled in the near future. Both contentions appear to have merit, but there is not sufficient data in the record to determine the relative magnitude of appropriate modifications to the estimates of applicant and the staff. A figure about midway between the two estimates of district maintenance expense is adopted in Table II.

The adoption of the staff's estimates of allocated operation and maintenance expense was discussed in detail in the

decisions² on the first two districts of the current series of applicant's rate proceedings and need not be repeated here.

Ad valorem tax bills for the fiscal year 1967-1968 had not yet been received by applicant when the application was filed but were available to the staff in preparing its estimates. The "effective tax rate" related to utility plant in the East Los Angeles district over the past 14 years, when plotted graphically as in Exhibit No. 4-B, forms an upward sloping line for most of the period but begins to level off in 1964-1965. The rate advanced again in 1965-1966 but declined for the next two fiscal years. With the apparent leveling off of the previous trend, the staff's use of the 1967-1968 effective rate in estimating the first half of the 1968-1969 taxes for this particular district appears more reasonable than applicant's assumed reversal to the prior upward trend. The staff's estimate of ad valorem taxes, which also reflects a lower estimated level of plant, is adopted in Table II, consistent with the adoption of the staff's estimate of rate base discussed hereinafter.

The staff's estimate of depreciation expense is lower than applicant's due to the lower plant amounts included by the staff. The staff estimate is adopted in Table II, consistent with the adoption of the staff's estimate of rate base.

In the estimates of operating expenses other than those hereinbefore discussed, there is a very minor difference between the estimates of applicant and the staff, well within the range of accuracy possible in such estimates, so a level about midway between

² Decisions Nos. 73454 and 73456, dated December 12, 1967, in Applications Nos. 49444 and 49443, Visalia and Salinas districts.

them is adopted in Table II. The income taxes adopted in Table II reflect the revenues and expenses adopted in the table.

Rate Base

The difference between applicant's and the staff's estimates of rate base results primarily from applicant's inclusion, and the staff's exclusion, of certain mains and pumping facilities tentatively scheduled for construction in 1970 or 1971. These facilities are expected to further enhance the usefulness of applicant's new 3,000,000-gallon reservoir. It does not appear that the additional facilities will be in use for a significant portion of the 3-year period that the rates authorized herein will probably be in effect. The staff's estimate of rate base is adopted in Table II.

The adoption of the staff's basis for estimating the working cash component of rate base has been discussed in detail in a previous decision³ on another district of the current series of applicant's rate proceedings and need not be repeated here. It is assumed that there would be no significant change in the working cash requirement as a result of the adoption of somewhat higher operating expenses than estimated by the staff.

Rate of Return

In applicant's two most recent rate proceedings,⁴ the Commission found that an average rate of return of 6.7 percent over the next three years is reasonable for applicant's operations. In Exhibit No. 7, the staff recommends that the return be set in the

³ Decision No. 73686, dated February 6, 1968, in Application No. 49445, Hermosa-Redondo district.

⁴ Decisions Nos. 73984 and 73987, dated April 16, 1968, in Applications Nos. 49839 and 49837, Broadmoor and Bear Gulch districts.

upper part of a 6.55 to 6.75 percent range. Applicant asks that consideration be given to the rate of return likely to be realized over a 5-year future period.

Applicant's estimates for the test years 1967 and 1968 indicate an annual decline of 0.44 percent in rate of return at proposed rates. The staff's estimates, including the effect of a 1968 wage increase, also show an annual decline of 0.44 percent at proposed rates.

The comparative rates of return for two successive test years, or for a series of recorded years, are indicative of the future trend in rate of return only if the rates of change of major individual components of revenues, expenses and rate base in the test years, or recorded years, are reasonably indicative of the future trend of those items. Distortions caused by abnormal, non-recurring or sporadically recurring changes in revenues, expenses, or rate base items must be avoided to provide a valid basis for projection of the anticipated future trend in rate of return.

As an indication of the reasonableness of the trend in rate of return derived from the test years 1967 and 1968, applicant prepared Exhibit No. 5, a comprehensive analysis of the many changes in recorded items of revenues, expenses and rate base during the years 1961 through 1966. Applicant analyzed and evaluated distortions during those years, such as those caused by changes in its own water rates and in income tax rates and allowances.

Exhibit No. 5 shows that, eliminating only the effects of changes in applicant's own rates, the average annual decline in rate of return during the period from 1961 through 1966 would have been 0.42 percent at applicant's present water rates and even greater at its proposed rates.

There is no reason to believe that the trend in rate of return will level off in the next few years to less than the 0.44 percent per year indicated by applicant's and the staff's estimates for the test years 1967 and 1968. In fact, with the increase of \$4 per acre-foot for purchased water scheduled by MWD for July 1, 1970, the decline will be steeper than under the current \$3 annual increase.

In most of the recent decisions in rate proceedings involving other districts of applicant, the apparent future trend in rate of return has been offset by the authorization of a level of rates to remain in effect for several years and designed to produce, on the average over that period, the rate of return found reasonable. In one decision, a somewhat different method of offsetting the trend was the authorization of rate increases in several annual steps designed to produce, in each year rather than on the average, the rate of return found reasonable. Either approach should achieve the desired result.

In the current proceeding, the staff recommends that, should the Commission authorize step-type increases, steps subsequent to the initial one be authorized after further showing by applicant. Applicant contends that the delay inherent in the accumulation, presentation and review of additional data could result in a lower actual rate of return than is found reasonable. The single-step increase utilized for most of applicant's other districts is adopted for this proceeding.

The rate increase authorized herein will not be in effect for about the first half of the year 1968. With the indicated future trend in rate of return, the 7.44 percent return which would have resulted under applicant's proposed rates if in effect for the

test year 1968, should produce actual rates of return of approximately 6.0 percent for 1968 (with the new rates in effect for only half of the year), 7.0 percent for 1969 and 6.5 percent for 1970. With the extra dollar per acre-foot increase in cost of MWD water effective July 1, 1970, the rate of return for 1971 should be about 6.0 percent. Prospectively, then, applicant's proposed rates should produce an average rate of return of 6.7 percent for a period of about three years after they become effective.

Findings and Conclusion

The Commission finds that:

1. Applicant is in need of additional revenues.
2. The adopted estimates, previously discussed herein, of operating revenues, operating expenses and rate base for the test year 1968, and an annual decline of 0.44 percent in rate of return, reasonably indicate the results of applicant's operations for the near future.
3. An average future rate of return of 6.7 percent on applicant's rate base for the next three years is reasonable.
4. 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.

The Commission concludes that the application should be granted.

O R D E R

IT IS ORDERED that, after the effective date of this order, applicant California Water Service Company is authorized to file for its East Los Angeles district the revised rate schedule

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attached to this order as Appendix A. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedule shall be four days after the date of filing. The revised schedule shall apply only to service rendered on and after the effective date thereof.

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

Dated at San Francisco, California, this 25th
day of JUNE, 1968.

[Signature]
President
[Signature]
[Signature]
[Signature]
Commissioners

APPENDIX A

Schedule No. EL-1

GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

East Los Angeles, Commerce and vicinity, Los Angeles County.

RATES

	<u>Per Meter</u> <u>Per Month</u>	
Service Charge:		
For 5/8 x 3/4-inch meter	\$ 3.00	(I)
For 3/4-inch meter	3.30	
For 1-inch meter	4.50	
For 1-1/2-inch meter	6.30	
For 2-inch meter	8.10	
For 3-inch meter	15.00	
For 4-inch meter	20.00	
For 6-inch meter	34.00	
For 8-inch meter	50.00	
For 10-inch meter	62.00	
Quantity Rates:		
For the first 30,000 cu.ft., per 100 cu.ft.	\$ 0.223	(I)
For all over 30,000 cu.ft., per 100 cu.ft.	0.210	

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rates.