

ORIGINALDecision No. 74783

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 authorizing it to increase)
 rates charged for water service)
 in the San Mateo district.)

Application No. 50041
 (Filed February 23, 1968;
 Amended July 24, 1968)

McCutchen, Doyle, Brown & Enersen, by A. Crawford
Greene, Jr., for applicant.
Warren A. McClure, for Belmont County Water
 District, interested party.
William C. Bricca, Counsel, and Wallace Epolt,
 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 San Mateo district.

Public hearing was held before Examiner Catey in San Mateo on June 27, 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 June 27, 1968, with the understanding that the effect of a recent income tax surcharge would be considered concurrently if an appropriate pleading were timely filed. The amendment filed July 24, 1968 covers this aspect of the proceeding.

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Testimony on behalf of applicant was presented^{1/} by its vice-president and his assistant, and its general manager. The Commission staff presentation^{1/} was made through an accountant and two engineers.

Service Area and Water System

Applicant owns and operates water systems in twenty-one districts in California. Its San Mateo district includes the City of San Mateo and a section of unincorporated area of San Mateo County adjacent to the city. The service area slopes from near sea level to approximately 630 feet above sea level. Total population served in the district is estimated at 73,000.

The entire supply for this district normally is purchased from the San Francisco Water Department (SFWD), through four separate connections to SFWD's pipeline. Applicant's nine wells produce water of poor quality and in limited quantities, so are retained for emergency use only. The distribution system, which is in two parts, not interconnected, includes about 220 miles of distribution mains, ranging in size up to 24 inches. There are about 22,000 metered services, 96 private fire protection services and 1,600 public fire hydrants. Eighteen reservoirs and storage tanks and 33 booster pumps maintain system pressure and provide storage in the various pressure zones. Each booster pump has an electric motor and provision for emergency connection to a portable, gasoline-powered pump normally stationed in the district.

A field investigation of applicant's operations, service and facilities in its San Mateo district was made by the Commission

^{1/} Testimony relating to overall company operations had been presented by witnesses for applicant and the staff in Applications Nos. 49443, 49837 and 50042, the Salinas, Bear Gulch and San Carlos districts rate proceedings. This testimony was incorporated by reference in Application No. 50041.

staff. The plant was found to be in good condition, and satisfactory service was being provided. Only seven 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 these related to temporary conditions of dirty water. This problem generally has been corrected by applicant's main-flushing program.

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 rates became effective in 1956.

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. Table 12-C of Exhibit No. 4 shows that, for a typical commercial customer with average monthly consumption of 1,683 cubic feet through a 5/8 x 3/4-inch meter, the average monthly charge will increase 13 percent from \$7.04 under present rates to \$7.94 under the rates proposed in the original application. The temporary 2.22 percent surcharge will add \$0.18 to this average monthly charge at proposed rates.

TABLE I

COMPARISON OF MONTHLY RATES

<u>General Metered Service</u>	<u>Present Rates</u>	<u>Proposed Rates</u>
Service Charge*	\$1.65	\$2.00#
Quantity Rates:		
First 30,000 cu.ft., per 100 cu.ft.	0.32	0.353#
Over 30,000 cu.ft., per 100 cu.ft.	0.29	0.318#

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

Until the 10 percent surcharge to Federal income tax is removed, bills computed under these rates will be increased by 2.22 percent.

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 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, before considering the additional expenses and offsetting revenue requirement resulting from the 10 percent surcharge to Federal income tax. For comparison, this table also shows the corresponding results of operation modified as discussed hereinafter.

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	\$2,037,300	\$2,037,300	\$2,037,300
<u>Deductions</u>			
Purchased Water	776,000	771,800	773,900
Purchased Power	39,100	38,000	38,000
Oper. & Maint. Payroll	166,100	160,600	160,600
Other Oper. Exp.	45,900	44,600	46,300
Other Maint. Exp.	47,200	39,900	39,900
Additional Mailing Costs	8,300	2,600	8,300
Direct Admin. & Gen'l Exp.	23,700	21,900	21,900
Allocated Expenses, Depr. & Taxes	124,200	120,100	120,100
Ad Valorem Taxes	182,700	182,100	182,700
Other Taxes, Excl. Income Taxes	29,700	29,700	29,700
Direct Depreciation	156,700	156,700	156,700
Subtotal	1,599,600	1,568,000	1,578,100
Income Taxes	111,200	127,500	122,300
Total	1,710,800	1,695,500	1,700,400
Net Revenue	326,500	341,800	336,900
Rate Base	6,468,600	6,454,700	6,454,700
Rate of Return	5.05%	5.30%	5.22%
<u>At Rates Proposed by Applicant</u>			
Operating Revenues	\$2,308,100	\$2,308,100	\$2,308,100
<u>Deductions</u>			
Excl. Income Taxes	1,599,600	1,568,000	1,578,100
Income Taxes	251,100	267,400	262,200
Total	1,850,700	1,835,400	1,840,300
Net Revenue	457,400	472,700	467,800
Rate Base	6,468,600	6,454,700	6,454,700
Rate of Return	7.07%	7.32%	7.25%

From Table II it can be determined that the rates requested by applicant, exclusive of the temporary 2.22 percent increase due to the income tax surcharge, will result in an increase of 13 percent in operating revenues.

Purchased Water and Power

Applicant estimated the cost of water purchased from SFWD by deriving the average unit cost of such water during the period 1963 through 1966 and applying that unit cost to the estimated purchases for 1968. Calculations based upon the testimony of applicant's witness regarding the basic data used in his estimates show that he inadvertently used a factor of 7.48 gallons per cubic foot in deriving the unit cost of water and a factor of 7.50 gallons per cubic foot when applying that unit cost to 1968 purchases. This overstated his estimate by \$2,100, which represents half of the difference between the estimates of applicant and staff for this item.

The staff estimate is based upon a more detailed computation of charges for water delivered to applicant through each of SFWD's meters, assuming monthly but not yearly fluctuations in demand per customer. Because there are, in fact, yearly fluctuations in demand, and this results in additional charges under SFWD's rates, the staff estimate is understated. Applicant's estimate, corrected for the inconsistency between derivation and application of unit costs is adopted in Table II.

Applicant's estimates of purchased power for 1967 and 1968 are based upon projecting incremental annual unit costs of \$0.10 per million gallons of water pumped. Thus, the 1966 actual cost was \$9.83 per million gallons, the 1967 estimated cost was \$9.93 and the 1968 estimated cost was \$10.03. The staff had available for its estimates the actual 1967 cost of about \$9.70 which seems to invalidate applicant's assumed trend. The staff used the average unit cost for the years 1963 through 1967. The staff estimate of power cost is adopted in Table II.

Operation and Maintenance Payroll

The record does not show the method used in developing applicant's estimates of operation and maintenance payroll. The staff's estimate was derived by adding \$2,000 to the 1967 recorded operation and maintenance payroll to compensate for system growth and factoring the total upwards to reflect present wage levels. Comparative data for the past three years presented by the staff shows a very close correlation between the ratio of first-quarter payroll and full-year payroll in each year. The first-quarter payroll for 1968, adjusted for conversion of a part-time employee to full-time, appears to confirm the staff estimate, which is adopted in Table II.

Applicant's estimate for expenses grouped under "Other Operating Expenses" is based upon a projection of recorded expenses and wage rates for the past thirteen years, without any consideration of the number of customers served each year. The staff used the same basic data but fitted to those data, in lieu of a straight line, a curve with a progressively decreasing slope, consistent with the trend in number of customers.

From a review of the types of expenses grouped under "Other Operating Expenses", it appears that some, but not all, of these expenses are directly or indirectly affected by the number of customers. The modified estimate adopted in Table II was determined by (1) transferring \$1,700 of applicant's estimated administrative and general expenses to "Other Operating Expenses" to place the cost of telephone answering service in the same grouping of expenses used in the staff's estimates, (2) adding \$400 to the staff's estimate to correct an error in transfer of

expenses, and (3) averaging the resulting corrected estimates of applicant and staff.

Applicant's estimate for expenses grouped under "Other Maintenance Expenses" is based upon a projection of recorded expenses and wage rates for the past thirteen years. The staff utilized those data for only the more recent years. Applicant's replacement and improvement program in this district apparently has reduced the annual expenditures for repairs to the system. The staff's estimate is adopted in Table II.

Applicant's estimates include allowances for the cost of additional postage and envelopes related to applicant's conversion from postcard to envelope billing and also for the increase in basic postal rates applicable to all of its mail. Of those allowances, the staff expense estimates include only the additional postage expense due to the conversion from postcard to envelope billing. The record discloses no valid reason for excluding the other increases in expenses. Applicant's estimate of additional mailing costs is adopted in Table II.

The only significant difference between the estimates of applicant and the staff for direct administrative and general expenses is the difference in accounting for telephone answering service cost, as hereinbefore discussed. Inasmuch as this item has been included under "Other Operating Expense", the staff estimate is adopted in Table II.

The reasons for adoption of the staff's estimates of allocated expenses, depreciation and taxes have been discussed in earlier decisions in the current group of applicant's rate proceedings and need not be repeated here.

The small difference between the direct ad valorem tax estimates of applicant and the staff results from applicant's projection of a slight upward trend in "effective tax rate" in the 1968-69 fiscal year as compared with the staff's assumption of neither an increase nor a decrease from the 1967-68 effective rate. Chart 7-A of Exhibit No. 4 shows a fairly consistent downward trend in effective tax rate for this district from 1960-61 through 1965-66, reaching a low point at the end of that five-year period. For the next succeeding two fiscal years, however, the effective rate was significantly higher. Although projection of the steep short-term upward trend from the low year would not have been warranted, the nominal upward projection of trend assumed by applicant does not appear unreasonable. Applicant's estimate is adopted in Table II.

The differences between the income tax estimates of applicant and the staff are due to the offsetting tax effects of the difference in expense estimates hereinbefore discussed. The income taxes adopted in Table II reflect the expenses adopted in that table. The effect of the temporary surcharge to Federal Income Taxes is treated separately, as discussed hereinafter.

Rate Base

The rate base estimates of applicant and the staff differ only in the estimates of working cash. The reasons for adoption of the staff's estimates of working cash have been discussed in detail in earlier decisions in the current group 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.

Surcharge to Federal Income Tax

Subsequent to the filing of the application, a 10 percent surcharge to Federal income taxes was imposed by the Revenue and Expenditure Control Act of 1968. The surcharge is retroactive for the full year 1968 and, unless extended, expires June 30, 1969. The amended application shows that a 2.22 percent surcharge on bills computed under the general metered service rates requested in the original application will be required to offset the effect of the income tax surcharge and produce the same net revenues indicated hereinbefore in Table II. Applicant's proposed surcharge on its bills will offset only the future effect of the tax surcharge and is not designed to recoup any of the increased taxes on net revenue produced prior to the effective date of the increased water rates authorized in this proceeding.

Rate of Return

In the three recent rate proceedings involving applicant's Bear Gulch, East Los Angeles and Broadmoor districts, 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 as reasonable a range of rates of return, the midpoint of which is 6.65 percent. Applicant asks that consideration be given to the rate of return likely to be realized over a five-year future period.

Applicant's estimates for the test years 1967 and 1968 indicate an annual decline of 0.28 percent in rate of return at proposed rates. The staff's estimates show an annual decline of 0.25 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, nonrecurring 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 caused by such factors as changes in (1) wholesale water rates it pays to SFWD, and (2) income tax rates and allowances.

Exhibit No. 5 shows that, eliminating the effects of changes in SFWD water rates and changes in income tax rates and allowances, the average annual decline in rate of return during the period from 1961 through 1966 would have been 0.06 percent at applicant's present water rates and somewhat greater at its proposed rates. This adjusted decline for the five-year period is less than the 0.24 percent per year at present water rates projected by applicant and the 0.21 percent projected by the staff primarily because the average annual increase in consumption per customer from 1961 to 1966 was abnormally high. If average climatic conditions had prevailed throughout the period and the

trend in customer use indicated by studies made by both applicant and the staff had resulted, this would have affected the trends in operating revenues, purchased water and purchased power. Adjusting these three items to the normal trend results in an average annual decline in rate of return of about 0.2 percent at present water rates. There is no reason to believe that the trend in rate of return at applicant's proposed water rates in the next few years will be less than the 0.25 percent per year indicated by the staff's estimates for the test years 1967 and 1968.

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. That same approach is adopted for this proceeding.

The rate increase authorized herein will not be in effect for about the first three-fourths of the year 1968. With the indicated future trend in rate of return, the 7.25 percent return under applicant's proposed rates for the test year 1968 should produce an average rate of return of 6.7 percent for the next four years, approximately 5.5 percent for the year 1968 (with about one-fourth of the year at the new rates), 7.0 percent for the year 1969, 6.8 percent for 1970, 6.5 percent for 1971, and 6.2 percent for 1972.

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 0.25 percent in rate of return, reasonably indicate the probable range of results of applicant's operations for the near future.

3. An average rate of return of 6.7 percent on applicant's rate base for the next four 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 San Mateo district the revised rate schedule 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 Los Angeles, California, this
8th day of OCTOBER, 1968.

William J. Synovis, Jr.
President
John E. Decker
William L. Bensen
Augustin
John P. Morrissey
Commissioners

APPENDIX A

Schedule No. SM-1

GENERAL METERED SERVICEAPPLICABILITY

Applicable to all metered water service.

TERRITORY

San Mateo and vicinity, San Mateo County.

(T)

RATESPer Meter
Per Month

Service Charge:

For 5/8 x 3/4-inch meter	\$ 2.00
For 3/4-inch meter	2.20
For 1-inch meter	3.00
For 1-1/2-inch meter	4.20
For 2-inch meter	5.40
For 3-inch meter	10.00
For 4-inch meter	14.00
For 6-inch meter	23.00
For 8-inch meter	34.00
For 10-inch meter	42.00

(I)

Quantity Rates:

For the first 30,000 cu.ft., per 100 cu.ft.	\$ 0.353
For all over 30,000 cu.ft., per 100 cu.ft.	.318

(I)

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

SPECIAL CONDITION

Until the 10 percent surcharge to Federal income tax is removed, bills computed under the above tariff will be increased by 2.22 percent.

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