

ORIGINAL

Decision No. 76723

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of Split Mountain Water Company, a California corporation, for a certificate of public convenience and necessity to construct a public utility water system near Wofford Heights in Kern County and to establish rates for service and to issue stock.

Application No. 51203
(Filed June 26, 1969)

Edwin W. Wilson, applicant.

William R. Seugling, for Arden Water Company, interested party.

Sergius Boikan, Counsel, and Jerry J. Levander, for the Commission staff.

O P I N I O N

This application was heard before Examiner Rogers at Bakersfield on November 17, 1969, on which date it was submitted. Copies of the application and notice of hearing were served in accordance with the Commission's Procedural Rules.

Applicant requests a certificate of public convenience and necessity to construct and operate a public utility water system in Tract No. 3141 comprising 42 acres divided into 101 lots near a community known as Wofford Heights in Kern County, authority to establish rates and authority to issue stock.

The applicant is a California corporation. Its articles of incorporation were filed with the Secretary of State of California on March 24, 1969. The primary purpose for which it was

formed was to engage in a domestic water company under the regulation of this Commission.

The directors named in the articles are Oscar Greene, Carolyn Greene and Edwin Wilson.

Pala Ranches, Inc. (Pala) is the land owner and developer of Tract No. 3141. Oscar Greene is also the secretary of the latter corporation.

The applicant's articles authorize it to issue 200,000 shares of stock at \$1.00 per share. It seeks authority to issue 40,000 shares to Pala for funds for construction of all facilities, including the supply, storage, services and meters for the original system.

The Utilities Division staff made a report (Exhibit No. 17) which was concurred in by the applicant. The results of such investigation by the staff are summarized as follows.

Pala, owner and developer of land in Wofford Heights, and Kern River Distributors (Kern), owned by Oscar Greene, distributor of petroleum and propane products, share an office in Wofford Heights which applicant plans to use. Applicant will be operated by personnel of Pala and Kern under the supervision of Greene. Applicant plans to construct the water system by contracting for materials and personnel on an hourly basis, and has hired William Seugling, president and operator of Arden Water Company, to supervise all construction work on the proposed water system.

Applicant will be given easements or title to the land used as sites for its operative plant by Kern and will obtain easements for its transmission and distribution lines from Pala.

Applicant has applied for a water supply permit and has been advised that this will be issued for both wells. No county franchise is required.

Arden Water Company and Mountain Shadows Water Company, public utilities under this Commission's jurisdiction, are located within one mile of applicant's requested service area.

Applicant's water supply will be from two wells (Well No. 1 and Well No. 2) and two storage tanks. Water from Well No. 1 will be pumped into the storage tanks and the system will be supplied from the storage tanks by gravity flow. Well No. 1 is 7 inches in diameter and 300 feet deep, and is equipped with a 15-horsepower submersible motor and pump. The static water level is 108 feet. A 72-hour sustained pumped test indicated a yield of 105 gallons per minute with a pumping water level at 198 feet. Applicant proposes to install an in-line meter to measure the quantity of water produced from Well No. 1. Well No. 2, located on property owned by Greene, is 6 inches in diameter and 200 feet deep, equipped with a 7½-horsepower submersible motor and pump and an 8 hydrocell Jacuzzi, which acts as a pressure balancing device. The static water level is about 75 feet and the yield is estimated at 35 gallons per minute (Exhibit No. 9). Water from Well No. 2 will be pumped through 1,000 feet of 2-inch steel line to reach the system. Greene has no objection to an agreement pursuant to which Well No. 2 could be used as a standby well.

Storage will be provided by one 21,000 and one 100,800 gallon steel storage tank.

The staff engineer stated that Well No. 1 and the proposed storage of 121,800 gallons are adequate to provide for its initial service area plus an additional 50 customers.

Distribution System

The distribution system consists of 4,905 feet of 4-inch and 2,222 feet of 6-inch class 150 asbestos cement pipe. The service connections consist of 1,250 feet of 1-inch and 340 feet of 3/4-inch plastic pipe, leading to double and single meter boxes, respectively. The pressures at customer service connections will range between 42 psi and 105 psi.

The system meets the requirements of General Order No. 103.

Rates

The rates requested by applicant are identical with those of Arden Water Company and Mountain Shadow Water Company, both public utility water companies in the immediate vicinity. The staff engineer stated that the proposed meter minimum charges for the larger meters are inconsistent with those for the 5/8 by 3/4-inch meters and suggested that they be increased. The applicant had no objection to the proposed change.

Financing

The applicant proposes to finance the entire initial system, including the in-tract system, by the sale of stock to Pala in the amount of \$40,000. This would allow the following amounts:^{1/}

<u>Account No.</u>	<u>Account</u>	<u>Amount</u>
301	Intangible Plant	\$ 1,150.00
306	Land	1,000.00
315	Wells	3,080.00
317	Other Source of Supply	300.00
324	Pumping Equipment	1,969.20
342	Reservoirs and Tanks	7,658.17
343	Water Mains	19,669.22
345	Services	4,349.20
346	Meters	500.00
	Total	<u>\$39,675.79</u>

The Utilities Division concurred in the request that the initial financing be by equity capital. A hydraulic engineer's stated reason was that if water mains and services are financed by the main extension rule the ratio of advances to total capital would be approximately 60.5 percent^{2/} which exceeds the limitations of paragraph A.2 a of the main extension rule.

The Finance and Accounts Division of the Commission objected to the financing of the initial in-tract facilities by equity capital and urged that they be financed by a main extension contract. A staff financial examiner stated that no reason was offered in support of the request for equity financing.

1/ Exhibit No. 16. These costs except for the customers' meters, are the actual original costs of the system as installed. The staff's figures (Exhibit No. 17) are estimated costs.

2/ Using the applicant's figures (Exhibit No. 16) plus \$500 for meters (Account No. 346).

The financial examiner further stated that granting of this request would result in a higher rate base than otherwise would exist, and would result in the entire cost of this water system being included in the rate base of some other utility if a merger with another water company in the area is subsequently effected.

The witness stated that the Commission has had considerable experience with small water utilities having large rate bases and few customers, which subdividers are willing to operate at a loss until the lots in their developments are sold. Subsequently, the water system may be transferred to new owners who are unwilling to continue to subsidize the operations and request increased rates. He said that, even if full saturation is assumed for rate-making purposes, high water rates often become unavoidable. For these reasons, the witness stated, if a certificate is granted to applicant, all its in-tract plant should be financed in accordance with the main extension rule, and the initial stock issue should be limited to the cost of plant included in Accounts Nos. 301 through 342 and Account No. 346, a total of \$15,658.

The witness further stated that, in his opinion, it also would be appropriate for the subdividers to transfer the main extension contract to the utility to hold as an investment, with refunds being credited to capital surplus as they are earned.

We agree with the Division of Finance and Accounts that this is a case where the in-tract facilities should be financed by a main extension contract. As we have stated before,

"Considering only the appropriate relative responsibilities of the utility and the subdivider, there is no reason that these relative responsibilities should be different for the initial unit than for subsequent units of a subdivision, or should be different for an extension made by a new utility than for one made by a utility which already is in operation, or should be different between affiliated subdividers and utilities than between nonaffiliated. Inasmuch as the applicability of the rule affects the utility's rate base and potentially the customers' water bills, it follows that there is no reason that water users of a new utility should be subjected to less favorable policies affecting water rates than the policies that affect customers of older utilities.

"In those instances where the Commission has exempted certain initial units from the applicability of the main extension rules, there have generally been potential financial problems such as the utility's inability to make future refunds of advances required by the rule. This does not appear to warrant revising the rule because each situation can be evaluated in the related certificate proceeding. In fact, rather than to change the rule, the discussion in Exhibit No. 69 on the effects of deviating and not deviating from the rule for initial units leads us to believe that there may be better solutions to the financial problems encountered by a new utility than to relieve the initial subdivider of his obligation to advance the cost of the required main extension. For example, when a new utility is formed by the subdivider who needs water service to his property, as is almost invariably the case with new water utilities, the developer may be willing to forego cash refunds and credit them to proprietary capital or capital surplus, accept refunds in common stock or, without terminating the initial main extension agreement, turn it over to his utility as part of its assets. As a result, the utility's equity in utility plant would increase as refunds become payable but there would be no cash drain on the utility. These and other potential solutions can be explored in the individual certificate proceedings, rather than to prescribe a blanket solution for all situations. No change relating to the initial unit served by a new utility is made in the rule."

(Investigation of water main extension rules, Decision No. 75205, dated January 21, 1969, in Case No. 5501.)

The applicant estimated the following numbers of customers, operating revenues and expenses (excluding depreciation) at the end of the first, fifth and tenth years of operation:

<u>End of Year</u>	<u>No. of Customers</u>	<u>Revenues</u>	<u>Expenses</u>	<u>Revenue Exceeds Expenses</u>
First	10	\$ 240	\$1,052	\$ (812)
Fifth	50	2,400	1,368	1,032
Tenth	100	4,800	1,848	2,952

(Red Figure)

The applicant alleges that the parent corporation is willing and financially able to absorb operating losses during the development period (Exhibit No. 2). It will execute a contract, acceptable to the Commission, with Pala Ranches, Inc. the developer, showing that no lot in Tract No. 3141 shall be sold, transferred or encumbered without the payment of \$10.00 by the developer for each of the 101 subdivision lots with appropriate escrow instructions for the deposit into an interest bearing Special Fund Account of the utility, separate from other cash accounts, with a non-affiliated financial institution, and that the funds so deposited, together with their earned interest, shall be used, insofar as operating revenues are deficient, only for out-of-pocket operations, repairs, maintenance and replacement of facilities exclusive of any management salaries paid to the stockholders or the developer of the tract.

The staff engineer's estimates of customers, revenues, out-of-pocket expenses (including taxes and excluding depreciation expense), and the operating cash drain during the ten years before revenues, which will be sufficient to cover operational costs for the proposed service area, are as follows:

<u>Year</u>	<u>No. of Customers</u>	<u>Revenues</u>	<u>Out-of-Pocket Expenses</u>	<u>Operating Cash Drain</u>
1970	10	\$ 500	\$ 2,180	\$1,680
1971	20	1,000	2,280	1,280
1972	30	1,500	2,440	940
1973	35	1,750	2,540	790
1974	40	2,000	2,620	620
1975	44	2,200	2,710	510
1976	48	2,400	2,790	390
1977	52	2,600	2,890	290
1978	56	2,800	2,980	180
1979	60	3,000	3,080	80
		<u>19,750</u>	<u>26,510</u>	<u>6,760</u>

Operating cash drain per each of 101 lots = \$70.

The staff engineer considered rent, taxes, power, accounting, meter reading, customer billing and collecting, water system maintenance, office supplies, insurance, and transportation costs for out-of-pocket expenses, and based the estimated number of customers in Tract No. 3141 on data on the development of mobile home tracts in the service area of Arden Water Company, which company is only about one mile east of the proposed service area of applicant. Considering the type of development, the staff engineer's forecast of development is reasonable.

The engineer recommended that a fund be established to cover the out-of-pocket losses during the first ten years. The fund, he said, should be in an amount sufficient to cover the out-of-pocket operating losses which the staff estimates will be incurred in

the operation of this system during the first ten years. The witness estimated this deficiency to be about \$6,760, or approximately \$70 for each of the 101 lots.

The applicant agreed to the impound proposal but objected to the size thereof.

The Finance and Accounts Division had proposed that Arden Water Company should provide service in the applicant's proposed service area. The president of Arden was called as a witness and he specifically stated that he would not undertake to provide service to the area until it became self sustaining.

Findings

The Commission finds from the evidence herein the following facts:

1. Split Mountain Water Company (hereinafter applicant) is a corporation duly organized and existing under and by virtue of the laws of the State of California, and is authorized by its articles of incorporation, subject to the jurisdiction of the California Public Utilities Commission, to construct and operate a public utility water system in the State of California and to issue 200,000 shares of \$1.00 per share par value stock.

2. Applicant requests authority to furnish domestic water to Tract No. 3141 located at approximately two miles west of Lake Isabella, in Kern County California. Tract No. 3141 comprises 41.81 acres of land divided into 101 lots. The smallest lot contains 10,000 square feet. The largest contains 14,000 square feet. The lowest point in the subdivision is 3,550 feet above sea level and the highest point is 3,775 feet above sea level. The subdivision

is designed for mobile homes and mountain cottages and the lots are to be sold without homes. The sewer system is to be septic tanks and leach lines. Electricity is available from the Southern California Edison Company; telephone service from the Continental Telephone Company, and gas service from various propane distributors.

3. There are two other public utility water companies in the area. Both were notified of the hearing herein and neither appeared as a protestant.

4. The water system has been installed and complies with the requirements of General Order No. 103.

5. The water supply is from two wells, Well No. 1 and Well No. 2. Well No. 1 is the primary well and produces 105 gallons of water per minute. Well No. 2 is the standby well and produces 35 gallons of water per minute. There are two storage tanks with a total capacity of 121,800 gallons of water. Applicant has applied for but has not received a water supply permit from the Kern County Health Department. The water supply from Well No. 1 is adequate for the tract and an additional 50 customers.

6. No franchise to use the county streets is required.

7. No private or public water supplier other than applicant presently is able, ready or willing to provide water facilities and service to Tract No. 3141. The property owner, Pala Ranches, Inc., is ready to improve the tract, is financially able to proceed with the improvement thereof, and desires that applicant provide water service thereto.

8. Public convenience and necessity require and will require the construction and operation by applicant of a water system for sale of water to the general public in Tract No. 3141.

9. Pala Ranches, Inc., has expended the sum of \$39,175.79 for installation of the water supply and distribution system in Tract No. 3141 and will be required to expend an additional sum of \$500.00 for meters. These sums represent a total capital requirement at this time, exclusive of working cash, of \$39,675.79. Applicant herein seeks authority to issue and sell 40,000 of its authorized shares of capital stock at a par value of \$1.00 per share to Pala Ranches, Inc. Included in this proposed stock issue is \$24,018.42 for the acquisition of water mains and services (Accounts Nos. 343 and 345) for Tract No. 3141.

10. The water mains and services in the tract should be paid for by the subdivider, Pala Ranches, Inc., and financed through the main extension rule. The issuance and sale of no more than \$16,000.00 aggregate par value of applicant's capital stock is required at this time for the purpose of financing the initial plant cost herein as above set forth, exclusive of mains and services and including working cash. The money, property or labor to be procured or paid for by the issuance of such amount of stock is reasonably required for the aforesaid purposes and such purposes are not, in whole or part, reasonably chargeable to operating expenses or to income.

11. During the first ten years of operation applicant will incur an estimated loss in the total sum of \$6,760.00. This amounts to the sum of approximately \$70.00 for each of the 101 lots in Tract No. 3141. Applicant should be required to secure an agreement with Pala Ranches, Inc., for the payment by Pala into a special trust fund, of \$70.00 for applicant's operating expenses at the time each lot is sold, as recommended by the staff engineer in Exhibit No. 17.

12. Applicant should be required to obtain a firm agreement with Oscar Greene for the use of water from Well No. 2 as a standby source of water.

13. Applicant's developed source of supply, Well No. 1, is adequate for Tract No. 3141. Before it extends beyond said tract it should secure an additional source of supply other than the standby Well No. 2.

14. The rates and charges set forth in Appendix A are reasonable and should be made applicable for the water service to Tract No. 3141.

Conclusion

The Commission concludes that the application herein should be granted in accordance with the provisions of the order which follows. The certificate issued herein is subject to the following provision of law:

The Commission shall have no power to authorize the capitalization of this certificate of public convenience and necessity or the right to own, operate, or enjoy such certificate of public convenience and necessity in excess of the amount (exclusive of any tax or annual charge) actually paid to the State as the consideration for the issuance of such certificate of public convenience and necessity or right.

In issuing our order herein, we place applicant and its shareholders on notice that we do not regard the number of shares outstanding, the total par value of the shares nor the dividends paid as measuring the return applicant should be allowed to earn on its investment in plant and that the authorization herein given is not to be construed as a finding of value of applicant's stock or properties nor as indicative of amounts to be included in proceedings for the determination of just and reasonable rates.

O R D E R

IT IS ORDERED that:

1. A certificate of public convenience and necessity be granted to Split Mountain Water Company, a California corporation, authorizing said company to construct and operate a public utility water system to serve Tract No. 3141 near Wofford Heights, Kern County, as delineated on the map, Exhibit No. 5 attached to the application.

2. Applicant is authorized to file, after the effective date of this order, the schedule of rates set forth in Appendix A to this order, a tariff service area map clearly indicating the boundaries of the certificated area, appropriate general rules, and copies of printed forms to be used in dealing with customers. Such filing shall comply with General Order No. 96-A and the tariff schedules shall become effective on the fourth day after the date of filing.

3. Compliance by applicant with paragraph 2 of this order shall constitute acceptance by it of the right and obligation to furnish public utility water service to Tract No. 3141 in Kern County. The authority granted herein shall expire unless the designated tariff sheets are filed within one year after the effective date of this order.

4. Within ten days after the date service is first rendered to the public under the authority granted herein, applicant shall submit written notice thereof to this Commission.

5. Applicant shall prepare and keep current the system map required by paragraph I.10.a. of General Order No. 103. Within thirty days after the water system is placed in operation under the authority granted herein, applicant shall file with the Commission two copies of the map.

6. Applicant shall obtain easements on or title to the land used as sites for its operative plant and easements for its transmission and distribution lines.

7. Applicant shall install a meter to measure the volume of water pumped from Well No. 1.

8. Applicant shall not extend its facilities or offer to provide service outside of Tract No. 3141 in Kern County without further order of the Commission.

9. For the year 1970, applicant shall apply a depreciation rate of 3.0 percent to the original cost of depreciable plant. Until review indicates otherwise, applicant shall continue to use this rate. Applicant shall review the depreciation rates at intervals of five years and whenever a major change in depreciable

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plant occurs. Any revised depreciation rate shall be determined by: (1) subtracting the estimated future net salvage and the depreciation reserve from the original cost of plant; (2) dividing the result by the estimated remaining life of the plant; and (3) dividing the quotient by the original cost of plant. The results of each review will be submitted promptly to the Commission.

10. The effective date of this order shall be established by supplemental order of the Commission after applicant has:

- a. Entered into an appropriate agreement, subject to the approval of the Commission, whereby water from Well No. 2 will be available to applicant as a standby source of supply.
- b. Filed a copy of the recorded easements and/or conveyance of title to applicant's operative plant sites and pipeline easements.
- c. Entered into a loss reimbursement agreement in a form acceptable to the Commission which shall provide that the developer of Tract No. 3141 will pay applicant the amount of \$70.00 per lot upon sale or transfer by developer of lots in Tract No. 3141. All funds paid to applicant by developer in accordance with provisions of this agreement shall be deposited in a separate interest-bearing account in a bank or savings and loan association. Such funds, together with interest earned thereon, shall be used only to pay out-of-pocket (cash) operating expenses and taxes in connection with the operations of the utility's system excluding any management fees or payments to stockholders or affiliated developers, to the extent that such operating expenses and taxes actually incurred exceed gross revenues. Expenditures from the fund for these purposes shall not exceed the staff's estimated cash drain for each year as tabulated in paragraph 20 of Exhibit No. 17 herein.

11. Upon the eleventh anniversary of the initial deposit, any amount remaining in the special fund not utilized for the purpose set out above shall be refunded to the subdivider or paid to his designee. Applicant shall provide subdivider with a statement not later than March 31 each year detailing the purpose, description and amount of all additions to and withdrawals from the fund during the prior calendar year, and the balance in the fund at the close of the year.

12. A copy of these statements shall concurrently be filed with the Commission, attention of the Finance and Accounts Division. Two copies of this agreement shall be filed with the Commission concurrently with the filing of the tariffs authorized in ordering paragraphs of this decision.

13. Within one year after the effective date of this order, applicant may issue not to exceed \$16,000.00 aggregate par value of its common stock to Pala Ranches, Inc., for the purposes specified in this proceeding.

14. Upon the issuance of the stock as authorized by ordering paragraph No. 13 herein, applicant shall pay to the Commission the fee required by Section No. 1904.1 of the Public Utilities Code, which fee is \$50.00.

15. Applicant shall file with the Commission a report, or reports, as required by General Order No. 24-B, which order insofar as applicable is hereby made part of this order.

Dated at San Francisco, California, this 27th day of JANUARY, 1970.

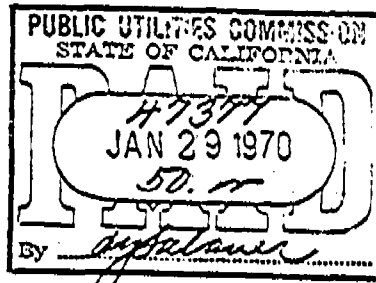
William S. ...
President

...

J.P. ...

...

Vernon L. ...
Commissioners



APPENDIX A

Schedule No. 1

METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Tract No. 3141, and vicinity, located near Wofford Heights, Kern County.

RATES

	<u>Per Meter</u> <u>Per Month</u>
Quantity Rates:	
First 900 cu.ft. or less	\$ 3.45
Next 3,100 cu.ft., per 100 cu.ft.30
Over 4,000 cu.ft., per 100 cu.ft.16
Minimum Charge:	
For 5/8 x 3/4-inch meter	\$ 3.45
For 3/4-inch meter	5.00
For 1-inch meter	8.00
For 1½-inch meter	15.00
For 2-inch meter	20.00

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