

ORIGINAL

Decision No. 79669

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of California Cities
Water Company, a California
corporation, under Section 454
of the Public Utilities Code for
authority to increase its public
utility water rates. (Cowan
Heights Division)

Application No. 52176
(Filed September 1, 1970)

Knapp, Gill, Hibbert & Stevens, by Karl K. Roos,
Attorney at Law, for applicant.
William Figg-Hoblyn, Attorney at Law, and
Chester Newman, for the Commission staff.

O P I N I O N

Applicant, California Cities Water Company, seeks authority to increase rates for water service in its Cowan Heights Division.

Public hearing was held before Examiner Catey in Santa Ana on August 26, 1971. Copies of the application had been served, notice of filing of the application had been published and notice of hearing had been mailed to customers and published, in accordance with this Commission's rules of procedure. The matter was submitted on August 26, 1971 subject to the receipt of late-filed Exhibits Nos. 8 and 9 on or before November 15, 1971. Those exhibits have been received.

Testimony on behalf of applicant was presented by its vice president/general manager and by a consulting engineer. The Commission staff presentation was made through two engineers. By mutual agreement between applicant and the staff, certain testimony which witnesses for applicant and the staff had recently presented in Application No. 52110, applicant's San Dimas Division rate proceeding, was not repeated at the Cowan Heights Division hearing. This testimony, relating primarily to overall company operations

rather than specific division operations, was instead incorporated by reference in Application No. 52176. Further, upon stipulation by applicant, some of the potential staff witnesses who prepared portions of the staff's exhibits were not called upon to present oral testimony relating to the exhibits.

Five customers testified, primarily regarding relatively high cost of water service, even under present water rates, and declining quality of the water.

Service Area and Water System

Applicant owns and operates water systems in the Counties of Los Angeles, Orange and San Bernardino and has a wholly owned subsidiary, Santiago Water Company, in Orange County. Applicant's Cowan Heights Division serves a 1200-acre portion of Orange County adjacent to the City of Tustin. The service area ranges in elevation from 280 to 900 feet above sea level.

All of the water for the Cowan Heights Division is purchased from two sources. The primary source is Red Hills Water Company, a nearby mutual water company in which applicant owns stock entitling it to a portion of the water produced from the mutual's two wells. The supplemental source is from connections to an agency of Metropolitan Water District of Southern California identified variously in the record as "Orange County Water District", "Orange County Municipal Water District" and "East Orange County Water District".

The distribution system is divided into three pressure zones. Water flows by gravity to the two lower zones but a booster pump supplies the top zone. Within the three zones there are approximately twenty miles of distribution mains, ranging in size from 1-inch to 14-inch. There are about 970 general metered service customers and 160 public fire hydrants.

Service

Staff Exhibit No. 1 states that only one informal complaint involving the service provided by applicant in its Cowan Heights Division was filed with this Commission last year. This complaint involved low pressure to 31 customers, all residing in the same general area within the system. Partial correction of the condition was effected by applicant by opening an interconnection valve which provided the area in question with two connections to the main grid system. Addition of another section of 8-inch transmission line by applicant is expected to completely overcome the previous problem. The order herein requires applicant to report and correct any remaining low pressure problems.

Exhibit No. 1 shows that the two complaints regarding water quality filed by customers with health authorities during 1968 and 1970 have been satisfied. The staff's review of the 75 complaints and inquiries presented by customers directly to applicant during 1970 indicates that these matters also have been resolved.

One of the most common complaints expressed by customers in interviews conducted by the staff during field investigations and by customers who testified at the hearing relates to chlorine taste in the water. It is possible that consultations between applicant, Red Hill Mutual, and local health authorities would result in a reduction in chlorine residuals now maintained. The order herein requires applicant to confer with the other parties and report back to the Commission.

One customer complained of hot water from applicant's mains. Applicant agreed to investigate this problem, report to the customer and advise the Commission of the results of the investigation by late-filed exhibit. That investigation shows that the warm water is caused by warm soil temperatures beyond the utility's control. Depths of mains are within the requirements of General Order No. 103.

Rates

Applicant's present tariff's for the Cowan Heights Division include rates for general metered service, public fire hydrant service and construction flat rate service. The general metered service rates were authorized in February, 1968, but the other schedules have remained unchanged since 1959.

Applicant proposes to increase its rates by about 28 percent for general metered service and 66 percent for construction flat rate service. No increase is requested for public fire hydrant service. Applicant bases the request for a higher percentage in construction flat rate service upon the generally higher costs involved in connecting, disconnecting and billing for this type of service for short periods of time, as compared with the costs involved in providing permanent service. No increase was requested for public fire hydrant service because there is no local public fire protection agency responsible for paying these charges.

In the application as filed, a request was made to establish a rate for intermittent, interruptible service of non-potable irrigation water. This rate was proposed to enable a sole remaining customer, other than applicant, of Seven Hills Mutual Water Company to obtain water from applicant rather than the mutual. From questions raised by customers at the hearing, however, it appeared that applicant might be placed in the position either of discriminating against other customers not within reach of the irrigation water source or of extending irrigation water mains which would parallel existing general use water mains. The application was modified at the hearing to delete the request for an irrigation service schedule but to add an additional rate block to the general metered service rates to cover large monthly use.

The following Table I presents a comparison of applicant's present rates, those requested by applicant and those authorized herein:

TABLE I
COMPARISON OF RATES

<u>Item</u>	<u>Per Service Per Month</u>		
	<u>Present</u>	<u>Proposed</u>	<u>Authorized</u>
General Metered Service:			
First 700* c.f. or less	\$4.35	\$5.50	\$5.00
Next 19,300 c.f., per 100 c.f.	.26	.34	.29
Next 30,000 c.f., per 100 c.f.	.20	.25	.23
Over 50,000 c.f., per 100 c.f.	.20	.22	.20
Construction Flat Rate Service	3.00	5.00	5.00

*Included in minimum charge for
5/8 X 3/4-inch meter. A graduated
scale of minimum charges is pro-
vided for larger meters.

Results of Operation

Witnesses for applicant and the Commission staff have analyzed and estimated applicant's operational results. Applicant's 1971 estimates included in the exhibits attached to the application were of necessity prepared prior to the September 1, 1970 file date. The staff's estimates are included in Exhibit No. 1, dated March 8, 1971. At the hearing, applicant stipulated that it would accept the staff's more up-to-date estimates for the purpose of this proceeding except for two significant changes in expense levels which took place after the staff's estimates were prepared. Those changes resulted from increases in electric rates and increases in effective ad valorem tax rates.

Summarized in Table II, from the exhibits attached to the application, from Exhibit No. 1 presented by the staff and from Exhibit No. 4 presented by applicant, are the estimated results of operation for the test year 1971, under present water rates and under those proposed by applicant. For comparison, this table also shows the corresponding results of operation adopted in this decision as discussed hereinafter and the corresponding adopted results under the water rates authorized herein.

TABLE II

ESTIMATED RESULTS OF OPERATIONS - TEST YEAR 1971

<u>Item</u>	<u>Applicant</u>			
	<u>Original</u>	<u>Stipulated</u>	<u>Staff</u>	<u>Adopted</u>
<u>At Present Rates</u>				
Operating Revenues	\$147,370	\$149,180	\$149,180	\$149,180
Operating Expenses:				
Purchased Power	8,800	11,190	9,730	11,190
Ad Valorem Taxes	19,820	21,840	18,200	20,200
Other Exp., Excl. Inc. Taxes	102,093	95,320	95,320	95,320
Subtotal	130,713	128,350	123,250	126,710
Income Taxes	-	(810)	(810)	(4,530)
Total	\$130,713	\$127,540	\$122,440	\$122,180
Net Revenue	\$ 16,657	\$ 21,640	\$ 26,740	\$ 27,000
Rate Base	576,700	484,700	484,700	484,700
Rate of Return	2.9%	4.5%	5.5%	5.6%
<u>At Rates Proposed by Applicant</u>				
Operating Revenues	\$189,090	\$191,050	\$191,050	\$191,050
Operating Expenses:				
Excl. Income Taxes	130,713	128,350	123,250	126,710
Income Taxes	8,486	18,190	20,820	17,230
Total	\$139,199	\$146,540	\$144,070	\$143,940
Net Revenue	\$ 49,891	\$ 44,510	\$ 46,980	\$ 47,110
Rate Base	567,700	484,700	484,700	484,700
Rate of Return	8.6%	9.2%	9.7%	9.7%
<u>At Rates Authorized Herein:</u>				
Operating Revenues	-	-	-	\$169,600
Operating Expenses:				
Excl. Income Taxes	-	-	-	126,710
Income Taxes	-	-	-	6,080
Total				\$132,790
Net Revenue	-	-	-	\$ 36,810
Rate Base	-	-	-	484,700
Rate of Return	-	-	-	7.6%

(Red Figure)

From Table II it can be determined that applicant's requested rates would result in an increase of 28 percent in operating revenues, whereas the rates authorized herein will produce a 14-percent increase. The percentage increase for individual bills will vary somewhat, depending on type of service and level of use.

The principal difference between the revenue estimates of applicant and the staff results from the higher staff estimate of average water use for general metered service. The staff estimate is based upon a study of the trend of customer usage in this district over the past eight years, adjusted for climatic differences, whereas applicant adopted 1969 as a normal water use year. The staff estimates of revenues, which applicant has stipulated are reasonable for the purposes of this proceeding, are adopted in Table II.

Applicant's original estimate of cost of purchased power is based upon applicant's estimated water usage per customer and the electric rates in effect when the estimates were being prepared in early 1970. The staff's estimate reflected the higher water usage used in the staff's revenue estimates and the electric rates in effect in late 1970. Applicant stipulated that the staff estimate is reasonable if adjusted to the electric rates now in effect. The staff stipulated that such adjustment is appropriate. The adjusted staff estimate is adopted in Table II.

Applicant originally estimated ad valorem taxes by using the 1969-70 average tax rate and the 1969-70 and 1970-71 assessed valuations increased by four percent to reflect prior years' trend in effective tax rates, plus estimated additional taxes for a proposed reservoir and booster pump. The staff's estimate of ad valorem taxes is based upon the effective tax rate for the fiscal year 1970-71, without any upward or downward trend, and excluding any allowance for an additional reservoir and booster plant.

At the hearing, applicant conceded that the new reservoir and booster plant will not be constructed as soon as originally planned. Applicant did not agree, however, with the staff's estimated leveling off of effective tax rates but, based upon newspaper articles, estimated the 1971-72 rate would be 20 percent higher than projected by the staff. The staff did not stipulate to the estimated 20 percent increase and late-filed Exhibit No. 9 was reserved for actual tax rate data to be presented when available. That exhibit shows that there was an 11-percent increase in effective tax rates for 1971-72. In the absence of some well-defined trend in the tax rate, it is appropriate to use the full-year effect of the latest known rate. Recognition is given to the actual 1971-72 effective tax rates in the expenses adopted in Table II, with no allowance for possible future installation of a reservoir and booster.

The staff's estimates of other expenses excluding income taxes and of rate base, which applicant stipulates are reasonable for the purpose of this proceeding, are adopted in Table II. The income taxes adopted in Table II are consistent with the revenues and expenses adopted in that table and include the effect of Investment Tax Credit and increased State Corporation Franchise Tax rate, as discussed hereinafter.

Rate of Return

In Exhibit No. 4, applicant derived for the Cowan Heights Division an 8.65-percent average cost of capital which includes a 12-percent return on common equity. No testimony was presented by applicant to justify that high a return on common equity.

In Exhibit No. 2, the Commission staff recommends a rate of return on rate base in the range of 7.40 to 7.75 percent for applicant's Cowan Heights Division based in part upon a study of capital structures and rates of return of other water utilities. Table No. 6 of Exhibit No. 2 shows that this range of return on rate base is equivalent to a return of from 8.5 to 9.3 percent on

applicant's common equity. The exhibit states that the recommendation as to allowable earnings on common equity involved consideration of such factors as (1) recently authorized rates of return for other California water utilities, (2) capital structure and imbedded cost of debt and preferred stock, (3) parent-subsidiary relationships, (4) need for construction funds, (5) nature of the investment in utility properties and (6) maintenance of financial integrity.

In setting rates prospectively but basing those rates upon a test year wholly or partly in the past, consideration should be given to any significant upward or downward trend that occurs from year to year under any particular level of water rates. In Exhibit No. 2, the staff concludes that there is no significant trend in rate of return inherent in the operation of the Cowan Heights Division. Applicant did not dispute this conclusion. The rates set forth in Appendix A to this decision are designed to produce a 7.6-percent return on rate base for the 1971 test year adopted herein. This is about midway in the range recommended by the staff in Exhibit No. 2, and is equivalent to about 9 percent return on equity.

Investment Tax Credit and State Corporation Franchise Tax Rate

The term "Investment Tax Credit" (ITC), as used herein, refers to a reduction in current tax liability allowed by Federal income tax authorities, pursuant to tax laws, based upon a stated percentage applied to the dollar amount of specified qualifying plant additions.

An ITC was introduced by the Revenue Act of 1962, suspended by the Suspension Act of 1966, restored by the Restoration Act of 1967 and repealed by the Tax Reform Act of 1969. A revised ITC was recently reinstated by the Revenue Act of 1971, with a credit of 4 percent for utilities. We hereby take official notice of the aforementioned previous and recent tax laws, and the recent increase to 7.6 percent for State Corporation Franchise Taxes.

Governmental wage and price regulations became effective after submission of this proceeding. The 1971 wage levels used in the staff estimates, however, were in effect prior to the effective date of wage controls. It is noted that applicant's present water rates will not have been increased for four years. The 14 percent increase granted herein, including the effect of ITC, represents less than a four percent annual increase.

We are of the opinion that the rate increases authorized herein are consistent with the standards and goals of the Price Commission. Data for the Price Commission are shown in Appendix B. Findings and Conclusions

The Commission finds that:

1.a. Applicant is in need of additional revenues but the rates proposed by applicant are excessive.

b. The adopted estimates, previously discussed herein, of operating revenues, operating expenses and rate base for the test year 1971 reasonably indicate the results of applicant's operations for the near future.

c. A rate of return of 7.6 percent on applicant's rate base for 1971 is reasonable.

d. 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.

e. Appendix B to the order herein accurately reflects data regarding the increases authorized herein and we so certify to the Price Commission.

2. The Commission staff recommendations on page 33 of Exhibit No. 1 are reasonable and should enable applicant to provide a more consistent quality of service.

The Commission concludes that the application should be granted to the extent set forth in the order which follows and that applicant should be required to place in effect the staff's service recommendations.

O R D E R

IT IS ORDERED that:

1. After the effective date of this order, applicant California Cities Water Company is authorized to file for its Cowan Heights Division the revised rate schedules attached to this order as Appendix A. Such filing shall comply with General Order No. 96-A. The effective date of the revised schedules shall be four days after the date of filing. The revised schedules shall apply only to service rendered on and after the effective date thereof.

2.a. Applicant shall continue its program of making pressure recordings at representative locations throughout the Cowan Heights system.

b. Within twenty days after any pressure recordings made in 1972 show lower pressure or greater variations in pressure than permitted by General Order No. 103, applicant shall file a written report in this proceeding, showing the nature of the deficiency, the proposed correction, and a time schedule for corrective action.

c. Within ten days after the effective date of this order, applicant shall file in this proceeding pressure charts taken at representative locations in the Clearview area (Zone 5) and the Greenbriar-Broadview area (Zone 4).

d. Within thirty days after the effective date of this order, applicant shall confer with representatives of Red Hill Mutual Water Company and local health authorities in an effort to keep

the chlorine residual of water from Red Hill's wells as low as is consistent with public safety, and shall file in this proceeding a written report of the outcome of those discussions.

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

Dated at San Francisco, California, this 1st
day of FEBRUARY, 1972.

L. P. Harrison
Chairman
1696 Hill Street, San Francisco, CA
Arthur
Vernon L. Stinson
Commissioners

APPENDIX A
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Schedule No. CO-1

(T)

Cowan Heights Tariff Area

(T)

GENERAL METERED SERVICEAPPLICABILITY

Applicable to all metered water service.

TERRITORY

Cowan Ranch, Peacock Hills and vicinity, located 2 miles northeast of Tustin, Orange County. (T)

RATES

Quantity Rates:		Per Meter Per Month	
First 700 cu. ft. or less		\$5.00	(I)
Next 19,300 cu. ft., per 100 cu. ft.....		.29	—
Next 30,000 cu. ft., per 100 cu. ft.....		.23	—
Over 50,000 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.....		9.50	—
For 1½-inch meter.....		15.50	—
For 2-inch meter.....		22.50	—
For 3-inch meter.....		45.00	—
For 4-inch meter.....		75.00	(I)

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

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Schedule No. CO-5

(T)

Cowan Heights Tariff Area

(T)

PUBLIC FIRE HYDRANT SERVICE

APPLICABILITY

Applicable to all fire hydrant service furnished to municipalities, (T)
organized fire districts and other political subdivisions of the State. (T)

TERRITORY

Cowan Ranch, Peacock Hills, and vicinity, located 2 miles northeast (T)
of Tustin, Orange County. (T)

RATE

Per Month

For each hydrant.....\$4.00

SPECIAL CONDITIONS

1. Water delivered for purposes other than fire protection shall (T)
be charged for at the quantity rates in Schedule No. CO-1, General
Metered Service.

2. The cost of relocation of any hydrant shall be paid by the party
requesting relocation.

3. Hydrants shall be connected to the utility's system upon receipt
of written request from a public authority. The written request shall
designate the specific location of each hydrant and, where appropriate,
the ownership, type and size.

4. The utility undertakes to supply only such water at such pressure
as may be available at any time through the normal operation of its
system. (T)

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Schedule No. CO-9FC (T)

Cowan Heights Tariff Area (T)

CONSTRUCTION FLAT RATE SERVICE

APPLICABILITY

Applicable to all water service furnished at flat rates for construction purposes.

TERRITORY

Cowan Ranch, Peacock Hills, and vicinity located 2 miles northeast of Tustin, Orange County. (T)
(T)

RATE

Per Month

For each service connection \$5.00 (I)

SPECIAL CONDITIONS

1. The above rate applies to service connections not larger than one-inch in diameter.

2. Service under this schedule will be furnished only during the initial construction period of a residence or other building, and in no event for longer than one year.

APPENDIX B

DATA REGARDING RATE INCREASE
AUTHORIZED FOR
CALIFORNIA CITIES WATER COMPANY
COWAN HEIGHTS DIVISION

- | (1) | <u>Item</u> | <u>Per Service</u> | <u>Per Month</u> |
|-----|--------------------------------|--------------------|---------------------------|
| | | <u>Former</u> | <u>Now</u> <u>% Incr.</u> |
| | General Metered Service: | | |
| | First 700 c.f. or less | \$4.35 | \$5.00 15% |
| | Next 19,300 c.f., per Ccf | .26 | .29 12 |
| | Next 30,000 c.f., per Ccf | .20 | .23 15 |
| | Over 50,000 c.f., per Ccf | .20 | .20 0 |
| | Construction Flat Rate Service | 3.00 | 5.00 67 |
- (2) The rate increase is expected to provide \$20,420 of additional annual gross revenue based upon a 1971 test year.
- (3) Net revenue as a percent of gross revenue is expected to be 22% as compared with 18% under present rates, a difference of 4%.
- (4) Rate of return on total capitalization assignable to this District is expected to be 7.6% as compared with 5.6% under present rates, a difference of 2.0%.
- (5) Sufficient evidence was taken in the course of the proceeding to determine whether or not the criteria set forth in paragraph (d), (1) through (4) of Title 6, Chapter III, Part 300, Sect. 300.16 of the Code of Federal Regulations, as amended effective January 17, 1972, are or are not met by the rate increase.
- (6) The increase is cost-based, and does not reflect future inflationary expectations; the increase is the minimum required to assure continued, adequate and safe service and to provide for necessary expansion to meet future requirements; the increase will achieve the minimum rate of return needed to attract capital at reasonable costs and not to impair the credit of the public utility. This Appendix to the rate decision constitutes the certification required by the Code of Federal Regulations.