

ORIGINAL

Decision No. 80207

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.

Application No. 52110
 (Filed August 6, 1970)

Wyman C. Knapp and David P. Christianson, Attorneys
 at Law, for applicant.

Eugene U. Blalock, for Forest Lawn Company; Carlina
 Griffiths, for 200 residents of Fox Glen Tract;
J. Frank Haven, for City of Covina; Nancy Steiner,
 for 54 residents of Mangrove and Rimhurst Streets;
MaryTheunisson, for 11 residents of East Baseline
 Road; Jimmy V. Thompson, for himself; and Gerhardt
 Van Drie, Attorney at Law, for Vinnell-Pauley;
 protestants.

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 San Dimas Division.

Ten days of public hearing were held before Examiner Catey
 in Pomona, San Dimas and Los Angeles, from August 24, 1971 through
 November 12, 1971.

Copies of the application had been served and notice of
 hearing had been published, in accordance with this Commission's rules
 of procedure. Notice of filing of the application had not been
 published in accordance with Rule 24, but none of the parties objected
 to the waiver of this requirement. The matter was submitted on
 November 12, 1971, subject to the filing of briefs. Opening briefs
 were filed by applicant and the Commission staff on February 7, 1972,
 reply briefs were filed by the same parties on February 25, 1972, and
 applicant's final reply brief was filed April 10, 1972.

Testimony on behalf of applicant was presented by its vice president-director, its vice president-general manager, one of its former directors, one of its attorneys and three consulting engineers. The Commission staff presentation was made through two engineers and three accountants. Seven customers testified, primarily regarding problems they have had with low pressure and with sand or silt in the water, and expressed their opposition to a rate increase. The Mayor of Covina testified regarding the city's opposition to the increase. A witness for Forest Lawn and one for Vinnell-Pauley advocated a rate structure which would provide a lower level of rates for large users, such as cemeteries and golf courses.

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 San Dimas Division serves portions of the Cities of San Dimas, Covina and LaVerne and the unincorporated community of Charter Oak, in Los Angeles County. Because of the range of elevations, the service area is divided into five pressure zones.

Underground sources and some stream sources have been developed to supply the San Dimas Division service area. Water is extracted from 14 wells owned by applicant and from three leased wells, in four ground water subbasins. Additional water is imported to the area by the Metropolitan Water District of Southern California (MWD) and is available to applicant through two active service connections. One connection provides treated water and the other untreated water.

For irrigation service, applicant has distribution mains which are essentially separate from the rest of the system, although some production, storage and related facilities are used jointly for all service. The distribution systems include about 138 miles

of mains, ranging in size from 1-inch to 30-inch. There are about 7,200 general metered service customers, 32 irrigation customers, 21 private fire protection service customers and 720 public fire hydrants.

Service

Staff Exhibit No. 19 states that no informal complaints involving the service provided by applicant in the San Dimas Division have been filed with this Commission during the past three years. A staff review of applicant's service complaint records indicates there have been some problems with dirty water, low or high pressure, color, taste, odor, air in the water, noise and lack of water. The staff concludes that applicant generally provides adequate service and corrects poor service conditions as they arise. The staff recommends, however, that applicant institute a more effective routine flushing program to avoid some of the problems before, rather than after, they cause inconvenience to customers. The order herein so provides.

The various service complaints described by customers who testified at the hearings were similar to the complaints previously reviewed by the staff. Applicant investigated specific complaints presented at the hearings. Corrective action was taken where appropriate and the customers were advised when there were apparent deficiencies in their own plumbing.

Over the past several years, the water served to San Dimas Division customers has become progressively harder. This is typical of similar Southern California communities which have had to import MWD water. The imported water is harder than the local water so, inevitably, as more imported water is used to supplement the relatively fixed local supply, the end product becomes harder. The imported water is, however, of a better quality than the water from some of the local wells, which has an excessively high nitrate content.

Rates

Applicant's present tariffs for the San Dimas Division include rates for general metered service, fire hydrant service, private fire protection service and measured irrigation service. These rates were authorized in 1967.

Applicant's tariffs provide that the measured irrigation service rate applies only to water used for agricultural purposes, that the irrigation water is not guaranteed to be potable, and that the irrigation service is interruptible. Water for most lawn and garden irrigation is not provided from the separate irrigation mains and properly comes under the general metered service rate. Because of the block rate structure for general metered service, large users pay a lower unit price for water than do small users. Protestants Forest Lawn and Vinnell-Pauley, the two largest users in the San Dimas Division, request that the number of rate blocks be increased, with progressively lower rates for the large consumption blocks.

Applicant proposes to increase all of its rates, except those for public fire hydrants, by about 33 percent. 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>Author- ized</u>
<u>General Metered Service</u>			
First 500* cu.ft. or less	\$2.75	\$3.65	\$3.40
Next 4,500 cu.ft., per 100 cu.ft.	.27	.36	.33
Next 11,000 cu.ft., per 100 cu.ft.	.20	.27	.24
Next 34,000 cu.ft., per 100 cu.ft.	.15	.20	.18
Over 50,000 cu.ft., per 100 cu.ft.	.15	.20	.15
<u>Private Fire Protection Service</u>			
Per inch of diameter of service	1.40	1.85	1.70
<u>Measured Irrigation Service</u>			
Per miners inch-hour	.07	.093	.085

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

Applicant requests authority to eliminate special conditions in its tariffs relating to the former Investment Tax Credit. We note, however, that the proposed deletion was effected some time ago pursuant to Advice Letter 29, filed by applicant on July 28, 1967.

Applicant proposes to add a provision to its measured irrigation service schedule, limiting such service to existing irrigation customers who continue to utilize the service each year. No objections were raised to this proposal. With the continuing decline in number of irrigation customers, some portions of applicant's separate irrigation distribution system could become unnecessary, yet without the proposed limitation on customers would have to be maintained for the remote possibility that irrigation demand would come back. That would not be in the public interest. The requested limitation will be authorized.

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 August 6, 1970 filing date. The staff's original 1971 estimates were presented in Exhibit No. 19, dated March 2, 1971. At the hearing, applicant presented, in Exhibit No. 3, dated August 16, 1971, revised estimates which reflected more recent information than was available at the time its original estimates were being prepared. By the time of the hearing, later information was also available to the staff and prompted certain revisions incorporated in Exhibit No. 19-A, dated September 14, 1971.

Summarized in Table II, from applicant's Exhibit No. 3 and from staff Exhibit No. 19, as modified by Exhibit No. 19-A, 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 OPERATION - TEST YEAR 1971

<u>Item</u>	<u>Applicant</u>	<u>Staff</u>	<u>Adopted</u>
<u>At Present Rates</u>			
Operating Revenues	\$ 713,566	\$ 739,280	\$ 739,300
Operating Expenses:			
Source of Supply	58,870	27,630	58,900
Pumping	104,087	95,300	95,300
Treatment	7,650	6,630	7,600
Transm. & Distrib.	70,090	65,670	70,100
Cust. Accts. Excl. Uncollect.	55,540	45,350	55,500
Sales	900	500	500
Admin. & General:			
Salaries	48,940	33,460*	41,700
Office Suppl. & Exp.	33,358	20,210	30,000
Regulatory Commission	22,468	4,000	9,000
Outside Services	13,000	7,420	13,000
All Other A & G	25,650	27,040	26,300
Subtotal A & G	143,416	92,130*	120,000
Miscellaneous	(21,090)	(12,850)*	(16,700)
Depreciation	104,175	105,080	104,200
Ad Valorem Taxes	153,070	144,210	135,200
Payroll Taxes	6,900	5,480	6,500
Subtotal Excl. Uncoll.			
& Inc. Tax	683,608	575,130	637,100
Uncollectibles	1,750	1,850	1,800
Income Taxes	-	3,070	(33,100)
Total	\$ 685,358	\$ 580,050	\$ 605,800
Net Revenue	28,208	159,230	133,500
Rate Base	3,164,295	2,613,400	2,685,000
Rate of Return	0.9%	6.1%	5.0%

(Red Figure)

* \$ after reclassification of \$2,140 A & G salaries from "Miscellaneous", for comparison purposes.

TABLE II
(Continued)

ESTIMATED RESULTS OF OPERATION - TEST YEAR 1971

<u>Item</u>	<u>Applicant</u>	<u>Staff</u>	<u>Adopted</u>
<u>At Applicant's Proposed Rates</u>			
Operating Revenues	\$ 945,785	\$ 984,350	\$ 979,600
Operating Expenses:			
Excl. Uncollectibles			
& Inc. Taxes	683,608	575,130	637,100
Uncollectibles	1,750	2,450	2,400
Income Taxes	61,308	127,580	91,400
Total	\$ 746,666	\$ 705,160	\$ 730,900
Net Revenue	199,119	279,190	248,700
Rate Base	3,164,295	2,613,400	2,685,000
Rate of Return	6.3%	10.7%	9.3%
<u>At Rates Authorized Herein</u>			
Operating Revenues	-	-	892,000
Operating Expenses:			
Excl. Uncollectibles			
& Inc. Taxes	-	-	637,100
Uncollectibles	-	-	2,200
Income Taxes	-	-	46,000
Total	-	-	685,300
Net Revenue	-	-	206,700
Rate Base	-	-	2,685,000
Rate of Return	-	-	7.7%

From Table II it can be determined that applicant's requested rates would result in an increase of about 32 percent in operating revenues, whereas the rates authorized herein will produce a 21 percent increase. The percentage increase for individual bills will vary somewhat, depending upon type of service and level of use.

Operating Revenues

The principal difference between the revenue estimates presented by applicant and those presented by the Commission staff results from the staff's higher estimates of average general metered service customer usage, based upon a correlation of past usage and climatic variations. This difference is partly offset by the staff's assumption of lower revenues than estimated by applicant for measured irrigation service and some flat rate revenues. The staff's basis for estimating average customer usage appears to be more accurate than the straight arithmetical average used by applicant and takes into account an apparent gradual upward trend in normal customer usage. The staff's revenue estimates are adopted in Table II, rounded and modified to reflect the amendment made by applicant at the hearing, in which the previous request for increased public fire hydrant rates was withdrawn.

Operating Expenses

Applicant's estimate of Source of Supply Expenses is more than double that of the staff. A large portion of the \$31,240 difference is due to the staff's exclusion of \$16,000 annual rental of a leased well known as the Malone Well. Most of the rest of the difference in estimates of this group of expenses stems from the differences in estimated proportions of purchased MWD water and well production.

The staff's exclusion of the annual rent for the Malone Well is based upon the staff's conclusion that it would have been more prudent for applicant to have drilled a well of its own instead of leasing one. In view of the litigation over water rights in the San Gabriel River Basin, it appears likely that other producers in the basin could have prevented by injunctive restraint the drilling of a new well by applicant. Inasmuch as the unit cost of the Malone Well water supply, including the annual rent, is lower than imported MWD water, we cannot conclude that the Malone Well lease was imprudent.

In regard to the proportion of purchased water needed, there are several factors which prevent the maximum theoretical utilization of local sources. Some of the local supplies have a high nitrate content, requiring blending with imported water. Also, MWD regulations limit fluctuations in delivery flows, forcing applicant to use its own sources partly for covering peak demands rather than continuously pumping local water. The staff's estimate based upon purchasing only ten percent of the total water requirements for the San Dimas Division appears overly optimistic. Applicant's estimate based upon combined purchases of about 15 percent and pumping from leased wells of about 20 percent of total requirements is reasonably consistent with actual experience in the area and appears more realistic. Inasmuch as the staff's revenue estimates adopted in Table II reflect a higher consumption per customer than estimated by applicant, it is possible that applicant's estimate of purchased water costs also should be modified to reflect a higher consumption. On the other hand, the annual rent for the Malone Well does not increase with consumption. Looking at the combined effects of costs of purchased water and power adopted herein, however, we will assume no significant change from applicant's estimate of source of supply expense adopted in Table II.

Applicant's estimate of pumping expense, exclusive of the cost of purchased power, is almost 40 percent higher than the staff estimate. The staff's estimate of purchased power is somewhat higher than applicant's estimate, due to the staff's assumption of a greater proportion of pumped water and reclassification of power purchases at leased wells. Applicant's estimates are based largely upon a projection of 1970 expense levels. Table 6-C of Exhibit No. 3 shows that some of the pumping expenses in 1970 were far greater than in 1968 and 1969. No justification for such a large increase is apparent from the record, which leads to the conclusion that there must have been some abnormally high operation and maintenance expense

in 1970. It is possible that the staff's estimate of purchased power costs should be modified to reflect a somewhat lower proportion of pumped water but higher overall consumption. Looking at the combined effects of costs of purchased water and power adopted herein, however, we will assume no significant change from the staff's estimates of pumping expense adopted in Table II.

Applicant's efforts to improve water quality result in higher water treatment expense. The order herein requires continuation and perhaps even expansion of applicant's flushing program. Applicant's estimate for the 1971 test year appears reasonable and, after rounding, is adopted in Table II.

The reasons for the differences between applicant's and the staff's estimates of transmission and distribution expenses are not clear in the record. Looking at the end results, however, a review of Exhibits Nos. 3 and 19 shows that the staff estimated increases of 0.1 and 3.3 percent, respectively, from 1969 to 1970 and from 1970 to 1971, whereas the actual increase from 1969 to 1970 was 5.5 percent and applicant projected a 4.7 percent increase into 1971. Applicant's estimates appear more reasonable and are adopted, after rounding, in Table II.

Staff Exhibit No. 19 states that the difference between applicant's original estimate and the staff's estimate of customer records and collection expense was predominantly due to differences in allocation percentages for payroll. The staff developed four-factor allocation percentages, whereas applicant's general manager testified that applicant spreads these expenses in proportion to the number of customers. For the rendering of bills and maintaining of customers' accounts there appears to be no justification for considering (1) direct operating expenses, (2) number of division employees and (3) division gross plant, the three additional factors used by the staff. Applicant's allocation method more properly relates customer records and collection expense to the numbers of customer accounts and bills rendered.

In Exhibit No. 3, applicant increased its original estimates of customer records and collection expense by \$6,367, primarily to reflect its 1970 experience with the actual net cost of contracting with a centralized electronic data processing (EDP) service rather than expanding its previous mechanical billing and accounting procedures. Its previous system had reached the limits of its capacity so applicant's management had concluded that a switch to EDP in late 1969 was timely. Preliminary comparative studies had indicated that the EDP system would do a much better job and might even reduce expenses.

Applicant's revised estimates for the test year 1971 show that the net overall costs of the EDP system were higher than originally estimated. The staff questions whether the benefits derived are worth the extra costs. Applicant's general manager pointed out that the EDP system simplifies the billing and accounting functions, is more accurate and provides an automatic check for errors and omissions, gives an immediate and complete history of every account, conserves space, is more readily expandable, simplifies computations of refunds on main extension contracts, provides customer statistics and data on delinquent accounts and provides applicant with experience using EDP which will be of value in assessing possible future conversion of other accounting functions to EDP. Although it is not possible to assign specific dollar values to the various present and potential benefits of applicant's conversion to EDP, the end result appears worth the additional expense. Applicant's estimates of customer records and collection expense, after rounding, are adopted in Table II.

The record does not disclose the reason for the difference between the estimates of sales expense presented by applicant and the staff. This expense includes advertising, which is always subject to question as to benefits to a utility's customers. In the absence of details relating to applicant's estimate, we have adopted in Table II the staff estimate, which is the same amount adopted in Decision No. 72426, dated May 23, 1967, in Application No. 48812, applicant's previous San Dimas Division rate proceeding.

The difference between applicant's and the staff's estimates of administrative and general expenses are primarily in four accounts: (1) administrative and general salaries, (2) office supplies and expenses, (3) regulatory commission expenses and (4) outside services.

Neither applicant's nor the staff's estimates of administrative and general salaries and of office supplies and expenses reflect normal future operations. During 1970, applicant's parent corporation, Consolidated Water Company, moved its office. Prior to the move, other affiliates of the parent had temporarily been providing certain services and materials to the parent without charge, and the resulting abnormally low expenses were projected in the staff's estimates. Also, additional administrative and general personnel required for general administrative and accounting purposes at applicant's San Dimas office were not included in the staff's estimate. On the other hand, some nonrecurring expenses associated with the parent's moving its office are included in the 1970 expenses which applicant used as a base in projecting its 1971 estimates, thus overstating normal expenditures. The staff allocation percentages for administrative and general expenses common to more than one affiliate or division are derived from a different formula than applicant used, but the resulting percentages are not significantly different.

As might be expected from the foregoing paragraph, the actual 1971 expenses^{1/} for administrative and general salaries and for office supplies and expenses were lower than estimated by applicant and higher than estimated by the staff. The actual recorded 1971 expenses for those items are adopted, after rounding, in Table II.

^{1/} From applicant's 1971 Annual Report to the Commission covering San Dimas Division, incorporated by reference herein.

Applicant's estimate of regulatory commission expense does not reflect normal future average expenses in that the estimate includes both an annual three-year amortization of the estimated cost of the current proceeding and the annual five-year amortization of the cost of the previous proceeding. The latter amortization expired during 1971. The staff's estimate was based upon a five-year amortization of the cost of a fairly simple rate proceeding. The previous rate proceeding for this district required only two days of hearing, as compared with the ten days of hearing held on the current proceeding. We note, however, that most of the controversial issues, such as inclusion of water rights in rate base, were temporarily waived by applicant in that proceeding. This expedited the previous proceeding considerably, but it still cost applicant more than estimated by the staff for the current proceeding. Considering all of the facts, together with the assumption that the key issues resolved in the current proceeding will not have to be relitigated again, we have used \$9,000 per year for average normal regulatory commission expense adopted in Table II.

For the years 1968, 1969 and 1970, applicant's expenses for outside services, such as auditing, engineering and legal fees, have been in the range of about \$19,000 to \$24,000 allocable to the San Dimas Division. With the strengthening of applicant's internal organization in 1970, applicant hopes to reduce these expenses to about \$13,000. The staff based its estimates on the level of expenditures required in 1966 and 1967, which does not even cover applicant's current costs of auditing alone. Applicant's estimate is adopted in Table II.

Numerous small differences in estimates account for the remainder of administrative and general expense differences. Detailed evidence on the relative merits of all of those minor differences was not presented by applicant or the staff. We have adopted an amount about midway between the two estimates in Table II.

Both applicant and the staff estimated about the same proportion of administrative and general expense that normally would be transferred to clearing accounts or capital accounts and credited to miscellaneous expense. The same proportion has been applied to the adopted administrative and general expenses to arrive at the credit adopted for miscellaneous expense in Table II.

Although applicant and the staff utilized the same depreciation rates in their estimates of depreciation expense, there are numerous differences in the detailed development of the estimates. Some of the differences relate to the staff's substitution of a hypothetical utility-owned well for the leased Malone Well, as hereinbefore discussed. This increased depreciation accruals charged to expense in the staff's exhibit and reduced the accruals charged to contributed plant relating to the Malone Well. Despite the various differences, many of which are offsetting, there is less than one percent difference in the final estimates. At least part of this difference is due to the Malone Well issue. We have adopted applicant's lower estimate of depreciation expense, rounded, in Table II.

Most of the difference between the estimates of taxes other than on income presented by applicant and the staff are in ad valorem taxes. Applicant used its estimates of 1971-72 fiscal year taxes as though they were applicable to the calendar year 1971 and, in addition, included estimated taxes on 1971 additions, which actually will not be taxed until the 1972-73 fiscal year. The staff used half of 1970-71 fiscal year taxes plus half of 1971-72 estimated fiscal year taxes, adjusted to "roll back" nonrevenue-producing plant,^{1/} consistent with the rate base treatment of such plant. Both estimates include further adjustments for nonoperative plant. Applicant assumed a somewhat higher increase in tax rates for 1971-72 than did the staff. A further difference is due to an arithmetical error in applicant's exhibit.

^{1/} Such as plant additions which improve service but do not result in additional customers or consumption.

When applicant and staff were preparing their estimates, the 1971-72 tax bills had not been rendered. When those bills were received by applicant, a summary was prepared and presented as Exhibit No. 17. The ad valorem taxes adopted in Table II are based upon that exhibit and reflect half of 1970-71 taxes at the latest known tax rate plus half of 1971-72 taxes, with appropriate adjustment for nonoperative plant and nonrevenue-producing plant.

The difference between applicant's and the staff's estimates of payroll taxes results from differences in estimated expenses which include payroll. There is insufficient data in the record to correlate the payroll taxes directly with payroll. Inasmuch as some of the expenses consisting wholly or partly of payroll have been adopted at a level between applicant's and the staff's estimates and others have been adopted at either applicant's or the staff's estimated level, we have estimated a consistent amount for payroll taxes adopted in Table II.

The various differences between applicant's and the staff's estimates of operating revenues and expenses result in differences in estimates of income taxes. The income taxes adopted in Table II are consistent with the revenues and expenses adopted in that table. Further, we take official notice of those changes in income tax laws which result in a 7.6 percent rate for state corporation franchise tax and which reinstate an investment tax credit for federal income taxes at a 4 percent rate for utilities.

The income tax estimates under present water rates presented by applicant failed to show the negative income taxes which result from a negative taxable income. Those presented by the staff also fail to show the negative surtax which results from a negative taxable income for that portion of the federal taxes. A negative taxable income in one division of a multi-division operation offsets positive taxable income of other divisions, reducing the total company tax liability.

Rate Base

The difference between the rate base estimates of applicant and staff are the result of numerous differences in individual items which are components of rate base. Some significant differences between the estimates are:

Applicant included amount paid for water rights in excess of "original cost".....	\$ 479,565
Applicant used a lower level of advances and contributions.....	52,900
Applicant included expenditures subsequent to acquisition of water rights to "protect" those rights.....	34,928
The staff assumed a hypothetical utility-owned well in lieu of the leased Malone Well.....	(16,000)
Net effect of all other differences in rate base	<u>(498)</u>
Total	\$ 550,895

Cost of Water Rights

A major issue in this proceeding is the amount to be included in rate base for water rights. Applicant contends that the original-cost rate base should be increased by about \$480,000 in recognition of the amounts paid by applicant to two predecessor mutual water companies in excess of the original cost of those water rights to the mutuals. The staff recommends adherence to an original cost basis.

The concept of an original-cost rate base is well established in California. Under that concept, a utility constructing plant and utilizing it for serving the public normally is entitled to earn a reasonable return on only the actual investment in those facilities, even though at any particular time similar property not dedicated to serving the public might have a significantly higher resale value. Further, if a utility purchases assets from another

utility and continues to utilize those assets in serving the public, the purchaser normally is entitled to earn a reasonable return on only the predecessor's original cost less, of course, any retirements and accrued depreciation. The mere transfer of title thus does not affect the earning power of the utility plant.

A different situation is presented when a utility neither constructs the assets in question nor acquires them from an entity which has already utilized them in serving the public. For example, if a utility acquires a second-hand pump which had not been used by the former owner in any way related to public utility service, the utility normally is entitled to earn a reasonable return on the purchase price to the utility, rather than the original cost to the predecessor. Consideration must naturally be given to such things as arms-length dealing and prevailing prices for similar second-hand assets.

The situation is not so clear-cut when a utility obtains assets from a mutual water company. A bona fide mutual does not come under the jurisdiction of this Commission so its accounting records may not show original cost on the same basis as for a regulated utility. Further, there is the question as to whether or not service to a limited portion of the public (the mutual's members or stockholders or their assignees) warrants adherence to the original cost concept for determining the successor utility's rate base.

Decision No. 68242, dated November 24, 1964, states that applicant was formed in 1964 by the merger of Clinton County Water Company (an Ohio corporation), San Dimas Water Company (an alleged California mutual), San Dimas-Charter Oak Domestic Water Company (a California utility) and The Columbia Land and Water Company (an alleged California mutual). That decision indicates close affiliation of some of the entities involved: (1) San Dimas-Charter Oak Domestic Water Company (Domestic) was a wholly owned subsidiary of San Dimas

Water Company (San Dimas), (2) Domestic obtained virtually all of its supply from San Dimas which, in turn, obtained part of its water supply from the Columbia Land and Water Company (Columbia). It may further be presumed that, in order for water to have been provided from San Dimas to Domestic, the utility must also have been a stockholder of its parent, the alleged mutual.

The aforementioned merger was authorized by Decision No. 68242 but, at that time, there was insufficient evidence to permit verification of the accuracy or propriety of proposed journal entries, particularly with respect to plant accounts. Applicant, in compliance with a requirement of Decision No. 68242, submitted a petition on March 15, 1965 for an order approving its proposed journal entries and plant account. The Commission's staff in the Finance and Accounts Division took exception to some of the figures proposed in the petition. Thereafter, by Decision No. 70149, dated January 4, 1966, the Commission authorized entries pertaining, among other things, to Plant Accounts 311 through 378, covering all property except intangible plant and land. Those latter accounts were still in dispute between applicant and the staff. The proceeding was reopened to resolve the dispute. Following a prehearing conference and extensive negotiations, counsel for applicant and the staff submitted a stipulation and supporting exhibits concerning the disputed account balances, which stipulation was incorporated in the final order in Decision No. 77962, dated November 24, 1970.

Decision No. 77962 established the original cost of land and water rights to be entered in applicant's plant accounts. Paragraph 4 of the order therein, however, left open the disposition of \$350,106 representing the acquisition adjustment related to the difference between original cost and purchase price to applicant of the water rights. Applicant now asks that it be permitted to include in rate base not only the \$350,106 acquisition adjustment but also \$129,459 which it previously had stipulated would be written off to Capital Surplus.

When a utility acquires the assets of a mutual water company, there is a strong presumption that those assets had previously been utilized to serve a portion of the public. The original costs to the mutual are thus normally used in determining the portion of the utility's rate base represented by the assets acquired from the mutual. The staff cited several decisions indicative of this concept.

Applicant points out that, in at least one instance, the Commission found that the water rights acquired by a utility from a mutual had not been previously dedicated to public use and therefore the price paid by the utility was, in effect, the original cost. Decision No. 61954, dated May 9, 1961, in Application No. 42375, cited by applicant did adopt a rate base which included certain water rights at a utility's cost rather than its predecessor mutual's cost but specified that the treatment of such items for rate-making purposes must, in each case, be decided upon its merits.

In the current proceeding, where a utility, Domestic, had been wholly owned by an alleged mutual, San Dimas, and had obtained virtually all of its water supply from its parent, we cannot consider that the water supply and any related water rights had first been dedicated to public service at the time of the merger into the present applicant corporation. Evidence presented by applicant shows that, had the water rights not already been utilized to serve the public, they may well have had a fair market price at the time of merger which would have been in excess of the amount paid by applicant. This alone does not warrant deviation from the original cost concept in establishing rate base. Further, any of applicant's water rights which may be established or confirmed in the pending court litigation as a result of historical production from sources in the basin would presumably be directly related to production which was used to serve the public. The rate base adopted in Table II does not include the amounts paid by applicant for water rights in excess of the \$85,000 stipulated original cost to predecessors.

Advances and Contributions

The lower level of advances and contributions estimated by applicant was based upon later data on actual receipts and refunds than were available when the staff estimate was being prepared. The rate base adopted in Table II reflects applicant's estimates for those items.

Cost of Protecting Water Rights

Applicant included \$34,928 in rate base for expenditures made after acquisition of water rights in order to "protect" those rights. Some of those expenditures were not to protect the rights themselves but rather to establish the amount to be allowed in rate base for those rights. Until the pending court litigation over water rights is completed, it is difficult to determine how much of the \$34,928 produced information useful in actually protecting water rights and thus properly included in capital accounts. The remainder should not technically be included in rate base, but the effect on revenue requirement is similar, for this proceeding, to amortization of the abnormal expense over a period of years.

Two staff accountants were not in complete agreement as to the proper accounting for the \$34,928 expenditures. One of the witnesses testified (Tr. 515) that, in his understanding of the issue, this item is a proper amount to further increase the cost of water rights or, in the alternative, it would properly go into the expense of the present rate case. Another staff accountant testified (Tr. 734) that, in his opinion, the expenditures weren't to defend title but rather were to establish an accounting basis, and should not be capitalized. Inasmuch as the final segregation of the \$34,928 is not yet determinable and is somewhat academic for the purposes of this proceeding, we have included all of those expenditures in rate base, rather than partly in rate base and partly in expenses.

Other Rate Base Items

Consistent with our inclusion of the rental expense of the Malone Well, we have not included the staff's substitution of a hypothetical utility-owned well in rate base.

The staff estimates excluded more items of plant as not used or useful in utility operations than did applicant's estimates. For example, the staff excluded a creek diversion which subsequently has been repaired and placed in service. The staff excluded certain property traded to the City of San Dimas in exchange for improvements to a utility parking lot. The staff recommended reduction in certain office and storage space. It appears that many of the exclusions not made by applicant but which were recommended by the staff are not warranted. In any event, other differences between the two plant estimates more than offset the staff exclusions and result in an insignificant net difference between those portions of the plant estimates exclusive of the water rights and Malone Well issues.

Rate of Return

In Exhibit No. 4, applicant derived for the San Dimas Division a cost of capital ranging from 7.9 to 8.7 percent, using 10 to 12 percent return on equity capital. Applicant points out that a return of from 9.4 to 10.3 percent on an original cost rate base would be required to produce the 10 to 12 percent return on equity capital, due primarily to the large acquisition adjustment related to the mutuals hereinbefore discussed.

In Exhibit No. 18, the Commission staff recommends a rate of return on rate base in the range of 7.40 to 7.75 percent for applicant's San Dimas Division, based in part upon a study of capital structures and rates of return of other water utilities. Table No. 6 of Exhibit No. 18 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, after eliminating the acquisition adjustment from 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 is likely to continue from year to year under any particular level of water rates. In Exhibit No. 3, applicant showed a slightly lower rate of return for its test year 1971 than for a similar test year 1970. Applicant's witness conceded, however, that the results for his two consecutive test years were not intended to indicate the probable future trend. In Exhibit No. 19, the staff states that its results of operation estimates indicate a downward trend of about 0.3 to 0.4 percent annually, and that this attrition is primarily the result of wage increases. An analysis of the staff estimates, however, discloses that the major cause of the downward trend indicated between 1970 and 1971 is in the estimates of ad valorem taxes. Neither applicant nor the staff presented any detailed studies which would assist in determining probable future trend in rate of return.

In a system where the local supply of water is relatively fixed and where growth results, in the long run, on a greater percentage of more expensive imported water, there is a tendency for expenses per customer to rise. Inasmuch as there is insufficient evidence in the record to evaluate the extent of downward trend in rate of return, we will make no specific allowance but will adopt 7.7 percent as a reasonable rate of return for the test year 1971. This is near the high end of the range recommended by the staff, and is equivalent to about 9.2 percent return on equity after reduction for the acquisition adjustment.

Wage and Price Controls

Governmental wage and price regulations became effective after submission of this proceeding. The 1971 wage levels used by applicant and the staff in their estimates, however, were in effect prior to the effective date of wage controls. It is noted that applicant's present water rates for the San Dimas Division will not have been increased for over five years. The 21 percent increase granted herein represents about 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. Inasmuch as this Commission has not yet received its Certificate of Compliance from the Price Commission, data for use by that agency in any review of the rate increase authorized herein are shown in Appendix B.

Rate Spread

The rates proposed by protestants Vinnell-Pauley and Forest Lawn would result in the sale of water in the large usage block at less than the incremental cost to applicant of purchased imported water. With the relatively fixed amount of local supply available, this would not be appropriate. Some consideration can appropriately be given to such factors as off-peak usage by large customers. This has been accomplished in the rates authorized herein by establishing an additional block for large use by any customer, at a rate lower than the previous blocks but sufficiently high to avoid selling water at lower than applicant's cost of purchased water.

Findings and Conclusion

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. Under the circumstance described in the foregoing opinion, there is no justification for granting applicant's request for deviation from original cost of water rights.

d. A rate of return of 7.7 percent on applicant's rate base for 1971 is reasonable.

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.

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

2. Regular flushing of dead-end mains and other potential points of accumulation is required in the San Dimas Division.

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 advise the Commission of its flushing program.

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 San Dimas 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. Within thirty days after the effective date of this order, applicant shall file in this proceeding an appropriate flushing

schedule covering all dead-end mains and other locations in the San Dimas Division where regular flushing has been found to be required.

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

Dated at San Francisco, California, this 27th
day of JUNE, 1972.

[Signature]
Chairman
[Signature]
[Signature]
[Signature]
Commissioners

Commissioner Thomas Moran, being necessarily absent, did not participate in the disposition of this proceeding.

APPENDIX A
Page 1 of 5

Schedule No. SD-1

San Dimas Tariff Area

GENERAL METERED SERVICE

APPLICABILITY

Applicable to general metered water service.

(T)

TERRITORY

San Dimas, Charter Oak, and vicinity, Los Angeles County.

RATES

Quantity Rates:

	Per Meter Per Month
First 500 cu.ft. or less	\$ 3.40 (I)
Next 4,500 cu.ft., per 100 cu.ft.	0.33
Next 11,000 cu.ft., per 100 cu.ft.	0.24
Next 34,000 cu.ft., per 100 cu.ft.	0.18
Over 50,000 cu.ft., per 100 cu.ft.	0.15 (I)

Minimum Charge:

For 5/8 x 3/4-inch meter	\$ 3.40 (I)
For 3/4-inch meter	4.50
For 1-inch meter	6.40
For 1 1/2-inch meter	11.00
For 2-inch meter	16.50
For 3-inch meter	28.00
For 4-inch meter	43.00
For 6-inch meter	67.00 (I)

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

APPENDIX A
Page 2 of 5

Schedule No. SD-3M

San Dimas Tariff Area

MEASURED IRRIGATION SERVICE

APPLICABILITY

Applicable to all measured irrigation service.

TERRITORY

San Dimas, Charter Oak, and vicinity, Los Angeles County.

RATES

Per Service Connection
Per Month

Quantity Rate:

Per miner's inch hour \$ 0.085 (I)

Minimum Charge:

For each turn on \$ 4.85 (I)

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

SPECIAL CONDITIONS

1. The miner's inch is defined as a rate of flow equal to one-fiftieth of a cubic foot per second.
2. The minimum rate of delivery under this schedule is ten miner's inches.
3. A twenty-four (24) hour advance notice may be required before water is turned on under this schedule.

(Continued)

APPENDIX A
Page 3 of 5

Schedule No. SD-3M

San Dimas Tariff Area

MEASURED IRRIGATION SERVICE

SPECIAL CONDITIONS - Contd.

4. The utility does not represent or guarantee that any water delivered hereunder is potable or of a quality suitable for human consumption. Any customer who uses said water or makes it available to others for human consumption shall take all necessary precautions to make the same potable and shall assume all risks and liabilities in connection therewith.

5. The utility does not guarantee a continuous and uninterrupted supply under this schedule and reserves the right to temporarily suspend the delivery of water when it is necessary to take the whole or part of the water system out of service for the purpose of cleaning, maintaining and repairing or other essential improvements thereon; or for domestic purposes.

6. Water deliveries to customers will be made and measured at the utility's conduits, or as near thereto as practicable.

7. This service is limited to existing irrigation customers who (N)
irrigate all or a reasonable part of their acreage each and every year. (N)

APPENDIX A
Page 4 of 5

Schedule No. SD-4

San Dimas Tariff Area

PRIVATE FIRE PROTECTION SERVICE

APPLICABILITY

Applicable to all water service furnished to privately owned fire protection systems.

TERRITORY

San Dimas, Charter Oak, and vicinity, Los Angeles County.

RATE

	<u>Per Month</u>	
For each inch of diameter of service connection	\$ 1.70	(I)

SPECIAL CONDITIONS

1. The fire protection service connection shall be installed by the utility and the cost paid by the applicant. Such payment shall not be subject to refund.
2. The minimum diameter for fire protection service shall be four inches, and the maximum diameter shall be not more than the diameter of the main to which the service is connected.
3. If a distribution main of adequate size to serve a private fire protection system in addition to all other normal service does not exist in the street or alley adjacent to the premises to be served, then a service main from the nearest existing main of adequate capacity shall be installed by the utility and the cost paid by the applicant. Such payment shall not be subject to refund.

(Continued)

Schedule No. SD-4

San Dimas Tariff Area

PRIVATE FIRE PROTECTION SERVICE

SPECIAL CONDITIONS - Contd.

4. Service hereunder is for private fire protection systems to which no connections for other than fire protection purposes are allowed and which are regularly inspected by the underwriters having jurisdiction, are installed according to specifications of the utility, and are maintained to the satisfaction of the utility. The utility may install the standard detector type meter approved by the Board of Fire Underwriters for protection against theft, leakage or waste of water and the cost paid by the applicant. Such payment shall not be subject to refund.

5. The utility will supply only such water at such pressure as may be available from time to time as a result of its normal operation of the system.

APPENDIX B

DATA REGARDING RATE INCREASE
AUTHORIZED FOR
CALIFORNIA CITIES WATER COMPANY
SAN DIMAS DIVISION

- | (1) | <u>Item</u> | <u>Per Service Per Month</u> | | |
|-----|---|------------------------------|------------|----------------|
| | | <u>Former</u> | <u>Now</u> | <u>% Incr.</u> |
| | General Metered Service: | | | |
| | First 500 c.f. or less | \$2.75 | \$3.40 | 24% |
| | Next 4,500 c.f., per Ccf | .27 | .33 | 22 |
| | Next 11,000 c.f., per Ccf | .20 | .24 | 20 |
| | Next 34,000 c.f., per Ccf | .15 | .18 | 20 |
| | Over 50,000 c.f., per Ccf | .15 | .15 | 0 |
| | Private Fire Protection Service,
per inch diameter of service | 1.40 | 1.70 | 21 |
| | Irrigation Service, per miners
inch-hour | .07 | .085 | 21 |
| (2) | The rate increase is expected to provide \$152,700 of additional annual gross revenue based upon a 1971 test year. | | | |
| (3) | Net revenue as a percent of gross revenue is expected to be 23% as compared with 18% under present rates, a difference of 5%. | | | |
| (4) | Rate of return on total capitalization assignable to this District is expected to be 7.7% as compared with 5.0% under present rates, a difference of 2.7%. | | | |
| (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. | | | |