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Decision No. 82216

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of LAKE GREGORY WATER COMPANY, a California corporation for authority to increase its public utility water rates, and also for authority to issue an unsecured promissory note.	Application No. 53870 (Filed March 2, 1973)

Wyman C. Knapp and Gary H. Giesler, Attorneys at Law, for Lake Gregory Water Company, applicant.
Andrew Tokmakoff and Ichiro B. Nagao, for the Commission staff.

O P I N I O N

Lake Gregory Water Company (LGWC) seeks authority to increase its metered and flat rate water rates approximately $66,000 (61.7 percent) annually; cancel a presently outstanding $129,000, 8½ percent promissory note authorized by Decision No. 77891 dated November 4, 1970; and issue an unsecured promissory note to its parent company, Lake Gregory Land and Water Company (LGLWC), for $281,000 due January 1, 1983 and bearing interest at the rate of 8 percent per annum.

LGWC renders public utility water service in the San Bernardino Mountains adjacent to the village of Crestline approximately 10 miles northeast of the city of San Bernardino. As of January 1, 1973 LGWC served 474 metered and 945 flat rate general service customers, a total of 1419.

After notice, public hearing was held before Examiner Johnson on September 11 and 24, 1973 at San Bernardino, California, and on September 25 and 26, 1973 at Los Angeles, California, and the matter was submitted on October 3, 1973 upon receipt of the transcripts.

Testimony on behalf of LGWC was presented[1/] by two consulting engineers and a manager of a rental agency. Testimony and statements in opposition to the granting of the requested rate relief were made by eight customers of LGWC. The Commission staff presentation was made through a financial examiner and an engineer. In addition, testimony on requirements for the use of lateral wells was given by a supervising sanitary engineer from the State Department of Health.

Promissory Note

As of December 31, 1972 LGWC had outstanding accounts payable totaling $240,863 of which $165,574 was due LGLWC. Of this latter amount $129,073 was paid for plant investment as detailed in Exhibit C of the application.

The accrued interest on the outstanding $129,000, 8½ percent interest, unsecured promissory note authorized by Decision No. 77891 is $22,539.

LGWC seeks authorization to issue an unsecured promissory note to LGLWC in the amount of $281,000 at 8 percent per annum due on or before January 1, 1983 to reduce the above accounts payable amount for plant investment of $129,073 to long-term debt; reduce the accrued interest of $22,539 on the outstanding note to long-term debt; refinance the outstanding note of $129,000; and provide $388 for working capital. A financial examiner testified that the staff had no objection to the issuance of the requested promissory note but recommended that LGWC transfer the remaining balance of accounts payable of $54,414, representing non-interest bearing advances from LGLWC, to capital surplus as a part of common equity

1/ Testimony of one of LGWC's consulting engineers given on December 10, 1970 on Application No. 51979 (LGWC's last general rate increase application) appearing at the transcript pages 7 to 21, and 73 through 128, together with Exhibits 1 through 6 of that matter were incorporated into this record by reference.

to reduce its debt ratio from 85.2 to 71.5 percent. Such a recommendation appears reasonable and will be adopted.

Rates

The rates presently in effect were authorized by Decision No. 78610 dated April 27, 1971 and consist of an annual metered service rate and an annual residential flat rate. LGWC alleges that its present annual metered service rate permits its seasonal metered customers to use the entire minimum amount in the summer months at a time when the local well supply is at its lowest quantity and thereby force additional water purchases. To alleviate this condition, LGWC proposes replacing the annual minimum and entitlement with a quarterly minimum and entitlement. In addition, LGWC proposes one quantity rate for all water used over the minimum entitlement rather than two quantity blocks as in the existing rates.

Testimony in opposition to granting the requested rate increases related primarily to the billing inequities arising from having similar customers on both flat and metered rates and objections to the further raising of rates believed to be excessively high. The latter contention was supported by comparisons with permanent residence bills stated to be considerably less than those rendered by LGWC for intermittent service.

Conversion to Metered Rates

In compliance with Decision No. 78610 LGWC is converting 100 or more flat rate customers a year to metered rates. At this rate the conversion plan could take nine years to complete. In the past LGWC's purchased water costs represented a relatively small portion of its total operating costs. Under these conditions, the cost of providing water service related primarily to the expenses associated with providing the facilities to deliver water to the customers and was essentially independent of the amount of water used by the individual customers. These circumstances justified flat rates and the leisurely conversion to metered rates established by Decision No. 78610. However, at this time increased demands coupled with forced abandonment of wells ordered by the Department of Public Health have resulted in LGWC having to purchase most of its water, resulting in purchased water costs representing a substantial portion of LGWC's total expenses. Reflecting such increases in operating expenses in flat water rates results in the smaller user paying a disproportionate share of total expenses.

Total metering would eliminate this billing discrimination, would tend to prevent consumer wastage of water and thereby reduce operating costs, and would provide a basis for assessing charges in accordance with costs. These factors, coupled with probable increased revenues from those flat rate customers who would use more than the minimum amount of water, fully justify expediting the conversion project. The order that follows will provide for full conversion within three years.

Results of Operation

The following tabulation compares the estimated summary of earnings for the test year 1973, under present and proposed rates, prepared by LGWC and by the Commission staff, and the adopted summary of earnings at present rates:

Summary of Earnings

(Estimated Year 1973)

Item	LGWC Estimated: Present Rates	LGWC Estimated: Company Proposed Rates	Staff Estimated: Present Rates	Staff Estimated: Company Proposed Rates	Adopted Results 1/
Operating Revenues	$107,457	$173,763	$109,350	$176,150	$109,350
Expenses					
Operating Expense	112,646	112,646	88,895	88,895	99,800
Depreciation Expense	12,665	12,665	13,390	13,390	13,490
Taxes Except Income	13,987	13,987	12,770	12,770	13,140
Income Taxes	200	2,427	200	13,530	200
Total Expenses	139,498	141,725	115,565	128,585	126,630
Net Operating Revenue	(32,041)	32,038	(6,215)	47,565	Loss
Average Rate Base	418,663	418,663	410,070	410,070	414,300
Rate of Return	(7.65%)	7.65%	Loss	11.60%	Loss

( ) negative

1/ At present rates. Bases for adopted results are discussed in the following paragraphs.

Operating Revenues

The staff estimate of revenues at present rates exceeds LGWC's by $1,893 or 1.76 percent for the estimated year 1973. Both LGWC and staff estimated future consumption from an analysis of metered water use and projection of continued conversion of flat rate to metered service with all new services metered. Because of the resort-oriented seasonal usage of many of LGWC's customers, neither the staff nor LGWC reflected water usage adjusted for temperature and rainfall in their estimates. The staff estimates based on later recorded data will be adopted as reasonable.

Purchased Water Expense

The currently effective purchased water cost of $250 per acre-foot will be adopted as the basis for computing 1973 test year purchased water expense. This unit figure applied to the staff estimated total water requirement of 231.3 acre-feet minus the six-year average annual yield of 34.1 acre-feet from Lewter, Government Springs, Chamois, Valle Spring, and Cathcart Well results in a purchased water expense of $49,300 for the test year 1973 which will be adopted as reasonable. Should changed conditions permit State Department of Public Health to reverse its present position and permit the continued use of Horst Well, Wilson Wells Nos. 1 and 2, and Jewell Well No. 64 with a combined output of 115.4 acre-feet, LGWC's purchased water costs would be reduced $28,850 below the amount contemplated in this proceeding. To permit the initiation of appropriate timely Commission action should this sizable reduction in expenses occur, the order that follows will require LGWC to file semi-annual reports of the sources of supply of its water.

Other Operating Expenses

The staff estimate of $1,000 for power pumping costs reflects the application of Southern California Edison Company's fuel cost adjustment surcharge applied to total estimated electrical energy consumption decreased by $734 to reflect the elimination of Horst Well pump charges because of the abandonment of this well. LGWC's consulting engineer testified that this pump would be required in conjunction with the Cathcart Well even after the abandonment of the Horst Well. Consequently, we will adopt as reasonable the staff estimate of $1,000 increased by $734 for Horst Well energy.

LGWC's test year 1973 regulatory commission expense of $5,504 consists of the current regulatory expense of $18,996 plus the Application No. 51979 regulatory expense of $8,524, a total of $27,520, amortized over a five-year period. The staff spread an estimated unamortized balance for the current application of $10,000 over a five-year period or $2,000 a year. For the purpose of this application we will adopt the current regulatory expense of $18,996 amortized over a five-year period, or $3,800 for the test year 1973.

A major issue in the proceeding is the appropriate level of operating and maintenance expenses, excluding purchased water, to be utilized for rate making purposes. LGWC utilized the president, general manager, and secretary-treasurer salary levels effected July 1, 1972 and, in general, increased recorded 1972 expenses by 6 percent to approximate an increase in the wholesale commodity index and expected labor increases of at least 6 percent. LGWC's consulting engineer admitted under cross-examination that its estimates of operating and maintenance expenses, excluding purchased water, had increased from $31,328 set forth in Application No. 51979 for the test year 1970 to $62,242 set forth in this application for the test year 1973, an increase of 98.7 percent.

The staff engineer testified that he estimated the 1973 unadjusted payroll expense to be $33,790 to reflect the wages paid the seven employees who charged time to LGWC in each of the four quarters of 1972. The application states that there are 4.6 employees presently engaged in the total utility operation. Multiplying the $33,790 1973 unadjusted payroll expense by the ratio of these 4.6 employees to the above-mentioned seven employees yields an adjusted test year 1973 payroll expense of $22,203.

The staff engineer used this payroll expense as a basis for deriving 1972 adjusted operating expenses of $37,880, excluding purchased water, which, in his opinion, reflected a reasonable increase from the $28,890 amount adopted for rate making purposes in Decision No. 78610 in Application No. 51979.

LGWC's consultant presented a tabulation of Lake Gregory Water Company employees and wages for 1972. This tabulation reflected an apportionment of the salaries of 12 individuals between LGWC and LGLWC and indicated $41,634.75 of $65,876.25 total wages (63.2 percent) being allocated to LGWC. LGWC's consultant then converted this annual salary to an average monthly salary of $717 and compared this to the average salary of $791 for the Crestline Village County Water District and the average monthly salary of $402 based on staff estimates set forth on Exhibit 7.

A review of the annual reports (incorporated in the record of this proceeding by reference) shows salary expense of $23,265 for 1968, $16,937 for 1969, $32,257 for 1970, $24,670 for 1971 and $35,281 for 1972. It will be noted that staff estimated 1973 payroll expense is less than any of the five years except 1969 and LGWC's estimate is higher than for any of these five years. In general, salaries have been increasing on the average approximately five percent per year. Applying this average salary increase of five percent per year through 1973 results in an average payroll expense for the five-year period 1968-1972 of $30,408 which will be adopted as reasonable for this proceeding. For the other operating expenses we will adopt LGWC's estimates totaling approximately $14,600 for office supplies, property insurance, miscellaneous operating expenses, uncollectibles, water treatment costs, and rents. The total of $49,300 purchased water, $1,734 for power for pumping, $3,800 regulatory commission expense, $30,408 payroll expense and $14,600 other operating expense is $99,842 which, rounded, is the $99,800 set forth in the adopted results of operation.

A manager of a rental agency testified that the rental cost, insurance, license fees, etc. of a 1968 pickup truck leased from LGLWC by LGWC was reasonable. Both the staff and LGWC reflected such a lease arrangement rather than the originally contemplated purchase arrangement in their revised estimates.

Depreciation Expense

The staff estimated depreciation expenses reflect the rollback to January 1, 1972 of the retirement of depreciable plant associated with Horst Well and Wilson Wells Nos. 1 and 2, resulting in the staff's beginning-year 1973 gross plant being $8,109 less than shown for LGWC. Both the staff and LGWC's revised summary of earnings reflected the deletion of Jewell Well No. 64 and a $3,500 pickup truck from depreciable plant and expense for the test year 1973. LGWC's consulting engineer testified that the Horst Well booster pump, concrete tank, and chlorinator will have to be retained, even after the Horst Well is abandoned, for use in conjunction with the Cathcart Well which utilizes the same forebay as the Horst Well. The staff revised test year 1973 depreciation expense of $13,390, increased by $100 to reflect retention in rate base of the Horst Well pump and pumphouse, will be adopted as reasonable.

Taxes Other Than Income

These taxes are comprised of payroll taxes and ad valorem taxes. Commensurate with the adopted payroll expense of $30,408 we will adopt $2,200 for payroll taxes for the test year 1973. This amount reflects federal unemployment taxes of .58 percent of the first $4,200; the currently effective LGWC state unemployment tax rate of 3.42 percent of the first $4,200; and FICA taxes of 5.85 percent of the first $10,800 of each employee's annual salary adjusted to reflect apportionment of salaries between LGWC and LGLWC.

The staff estimate of ad valorem taxes is $474 less than LGWC's estimate to reflect the elimination of Wilson Wells Nos. 1 and 2 and Horst Well from the tax base. Consistent with our adopted results for rate base and depreciation expense and reserve we will adopt the staff ad valorem taxes increased by $233 to reflect continued use of a portion of Horst Well plant and decreased by $353 to reflect the elimination of Jewell Well No. 64 from test year 1973 results.

Income Tax

The income tax of $200 for the adopted 1973 test year results is the minimum state franchise tax. The income tax to be applied to authorized rates to arrive at an 8.38 percent rate of return reflects a state income tax rate of 9 percent, a normal federal income tax rate of 22 percent, straight line depreciation on adopted test year plant, average investment tax credit, and annual interest on the proposed note rolled back to the year 1972.

Rate Base

The rate base of $412,454 set forth in the staff's revised summary of earnings as corrected on the record reflects the elimination from rate base for the test year 1973 of Horst Well, Jewell Well No. 64, Wilson Wells Nos. 1 and 2, and a $3,500 pickup truck. The staff estimate also excludes plant disallowed by Decision No. 77891. LGWC's revised rate base of $418,663 reflects the averaging of year-end balances for the Horst Well, Jewell Well No. 64, and Wilson Wells Nos. 1 and 2, and the elimination of the $3,500 pickup truck. The staff treatment of the Horst Well, Jewell Well No. 64, and Wilson Wells Nos. 1 and 2 is consistent with the inclusion of additional purchased water expenses for water to replace the output of these abandoned wells and will be adopted. Those portions of the Horst Well plant, previously discussed, that will continue to be used in conjunction with the Cathcart Well will be added to the staff rate base of $412,454 to yield the adopted rate base of $414,300.

Rate of Return

LGWC's summary of earnings show that the proposed rates would would yield a rate of return of 8.38 percent on a rate base of $423,317. The staff financial examiner testified that this proposed rate of return is not unreasonable and recommended that it be applied to the staff rate base of $419,000. He further testified that he would recommend that this rate of return be applied to the staff revised rate base. We will adopt a rate of return of 8.38 percent on the adopted rate base of $414,300 to produce a return on equity of 10.9 percent.

Findings

1. Lake Gregory Water Company is in need of additional revenue but the proposed rates set forth in the application are excessive.

2. The adopted estimates previously discussed herein of operating revenues, operating expenses, and rate base for the test year 1973 reasonably indicate the results of LGWC's operation for the near future.

3. A rate of return of 8.38 percent on the adopted rate base is reasonable. Such a rate of return will provide a return on equity of approximately 10.9 percent.

4. The increases in 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.

5. The authorized increase in rates would have provided increased revenues of approximately $55,750 had the rates been in effect for the full year 1973.

6. Total metering of LGWC's system would eliminate billing discrimination, curtail the wasting of water, thereby reduce operating costs, provide a basis for apportioning charges in accordance with cost occurrence, and provide additional revenues. The existing conversion program should be accelerated.

7. To achieve a balanced capital structure, LGWC should transfer the non-interest bearing advances of $54,414 from accounts payable to capital surplus as part of its common equity.

8. The proposed promissory note is for proper purposes.

The money, property, or labor to be procured or paid for by the issue of the security authorized by this decision is reasonably required for the purposes specified, which purposes, except as otherwise authorized for the payment of accrued interest, are not, in whole or in part, reasonably chargeable to operating expenses or to income.

The Commission concludes that the application should be granted to the extent set forth in the order which follows.

O R D E R

IT IS ORDERED that:

1. After the effective date of this order, Lake Gregory Water Company is authorized to file the revised rate schedule attached to this order as Appendix A. Such filing shall comply with General Order No. 96-A. The effective date of the revised tariff schedules shall be five days after the date of filing. The revised schedules shall apply only to service rendered on and after the effective date thereof.

2. Applicant, on or after the effective date hereof, for the purposes specified in this proceeding may issue a note in the principal amount of not exceeding $281,000 at 8 percent per annum interest and due on or before January 1, 1983. This note shall be in the same form, or substantially the same form, as Exhibit A attached to the application.

3. The issuer of the promissory note authorized by this order shall file with the Commission a report, or reports, as required by General Order No. 24-Series.

4. Within 90 days of the effective date of this order, applicant shall submit to this Commission and put into effect a program for systematically converting all flat rate services to metered services within a three-year period.

5. Applicant, on or after the effective date hereof, shall transfer $54,414 from accounts payable to capital surplus as part of its common equity.

6. Applicant shall, on or before March 1 and September 1 of each year, submit a report of its water supply sources for the previous calendar year and year ended June 30, respectively.

The authority granted by this order to issue an evidence of indebtedness will become effective when the issuer has paid the fee prescribed by Section 1904(b) of the Public Utilities Code, which fee is $304. In other respects the effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 4th day of DECEMBER, 1973.

President

Commissioners

I abstain

Commissioner.

PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA
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By

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Schedule No. 1 (C)

METERED SERVICE (C)

APPLICABILITY

(C)

Applicable to all metered water service.

TERRITORY

Lake Gregory and vicinity, San Bernardino County.

RATES

	Per Meter Per Quarter	
Quarterly Quantity Rates:		(C)
First 1,200 cu.ft. or less	$24.00	(I)
Over 1,200 cu.ft., per 100 cu.ft.............	.65	
Quarterly Minimum Charge:		
For 5/8 x 3/4-inch meter	24.00	
For 1-inch meter	30.00	
For 1-1/2-inch meter	40.00	
For 2-inch meter	60.00	(I)

The Quarterly Minimum Charge will entitle the customer to the quantity of water each quarter which the quarterly minimum charge will purchase at the Quarterly Quantity Rates. (C)

SPECIAL CONDITIONS

1. The quarterly minimum charge applies to service during the 3-month period and is due in advance. (C)

(Continued)

Schedule No. 1 (C)

METERED SERVICE

SPECIAL CONDITIONS - Contd.

2. The opening bill for metered service, except upon conversion from flat rate service, shall be the established quarterly minimum charge for the service. Where initial service is established after the first day of any quarter, the portion of such quarterly charge applicable to the current quarter shall be determined by multiplying the quarterly charge by one ninety-first (1/91) of the number of days remaining in the quarter. The balance of the payment of the initial quarterly charge shall be credited against the charges for the succeeding quarter. If service is not continued for at least one quarter after the date of initial service, no refund of the initial charges shall be due the customer.

3. Meters will be read on or about the last day of March, June, September, and December. Within ten (10) days thereafter each customer having used water in excess of that quantity, which its Quarterly Minimum Charge will purchase, will be rendered a statement, payable upon presentation, which will show the meter readings and the charges due at the quantity rates. Meters may be read and quantity charges billed during the winter season at intervals greater than 3 months. (C)

Schedule No. 2R (C)

RESIDENTIAL FLAT RATE SERVICE (C)

APPLICABILITY

Applicable to all flat rate residential water service. (C)

TERRITORY

Lake Gregory and vicinity, San Bernardino County.

RATES	Per Service Connection Per Quarter	
For a single-family residential unit, including premises	$27.00	(C) (I) (D)

SPECIAL CONDITIONS

1. The above flat rate applies to a service connection not larger than 5/8-inch in diameter. (C)

2. For service covered by the above classification, if the utility so elects, a meter shall be installed and service provided under Schedule No. 1, Metered Service, effective as of the first day of the following calendar month. Where the flat rate charge for a period has been paid in advance, refund of the prorated difference between such flat rate payment and the minimum meter charge for the same period shall be made on or before that day. (C)

3. The flat rate charge applies to service during each quarter of the calendar year and is due in advance. Flat Rates shall be payable after the beginning of the quarter and shall become delinquent 30 days after the beginning of the quarter. (C) (C)

(Continued)

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Schedule No. 2R

RESIDENTIAL FLAT RATE SERVICE

SPECIAL CONDITIONS - Contd.

4. Where initial service is established after the first day of any quarter, the portion of such quarterly charge applicable to the current quarter shall be determined by multiplying the quarterly charge by one ninety-first (1/91) of the number of days remaining in the quarter. If service is not continued for at least one quarter after the date of initial service no refund of the initial charges shall be due the customer. (C) (C)