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Decision No. 86004

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of

DOMINGUEZ WATER CORPORATION,
a California corporation,

for authorization to increase its rates for water service.

Application No. 55336
(Filed November 20, 1974;
amended September 26, 1975)

Gibson, Dunn & Crutcher, by Raymond L. Curran, Attorney at Law, for applicant.
James T. Quinn, Attorney at Law, and Andrew Tokmakoff, for the Commission staff.

O P I N I O N

By its original application filed November 20, 1974 applicant, Dominguez Water Corporation, requested authority to increase rates in its Dominguez service area in order to increase gross revenues by $763,100 to produce a 9.63 percent rate of return on its rate base for the test year 1975. By amendment filed September 26, 1975 applicant lowered its request to $757,000 estimated to produce a 9.98 percent rate of return on its rate base for the test year 1976.

Public hearing was held before Examiner Carol T. Coffey at Carson, California, on November 17, 18, and 19, 1975 and the matter was submitted upon oral statements on November 19, 1975. Notice of hearing had been mailed to all customers of the applicant on October 31, 1975.

Testimony on behalf of applicant was presented by its president, a vice president of finance, its consulting engineer, and a vice president of Pacific Mutual Life Insurance Company (a major investor in applicant's first mortgage bonds). The Commission staff recommendations were supported by testimony of a rate of return expert from the Finance and Accounts Division and two engineers from the Utilities Division.

Public Testimony

Five customers of applicant gave statements or testimony regarding various service complaints and advised the Commission of their views on the requested rate increase. On November 18, 1975 applicant presented the results of its investigations of specific customer complaints. By Exhibit 12, supplemented by testimony on the record, applicant denies that any substantial problems regarding taste and odor of water exist in the distribution system involved in a taste and odor complaint (Exhibit 12). The investigation of the high bill complaint of another customer established that there was, in fact, a leak within the residence of the customer. The customer's meter was removed and tested 99.66 percent accuracy (Exhibit 13). Applicant's witness stated that the customer would be made aware of why his bill is high so that he would be able to take corrective action.

General Information

The operations of applicant were reviewed extensively in Decision No. 80370 dated August 15, 1972 in Application No. 52888. The description of applicant's operations, service area, water systems, and general sources of supply are substantially as set forth in Decision No. 80370. Applicant's number of metered customers on December 31, 1974 was 28,270.

Applicant has adjudicated rights to produce from wells in the West Coast and Central Basins, but since annual production from its wells does not meet applicant's requirements, applicant purchases Metropolitan Water District (MWD) water in substantial quantities to meet its water supply needs.

Results of Operations

Applicant had based its original rate increase request upon estimated results of operations for the calendar year 1975. The amended application was based upon estimated results of operations for the calendar year 1976. At the hearing applicant presented its supplemental revenue requirements study (Exhibit 7) and the staff presented its 1976 estimates (Exhibit 10). The estimates of applicant and the staff differed. At the hearing the applicant conceded that certain of the staff's estimates were based on more recent data that should be adopted. The areas of disagreement and our adopted estimates are discussed below.

Operating Revenues

At the hearing both the staff and applicant presented revenue estimates based on rates in effect subsequent to Advice Letter No. 71 (effective July 13, 1975). The differences in the operating revenues are attributable to differences in estimated average number of customers and differences in estimated water usage per customer. Those differences are set forth in detail in the staff Exhibit 10, page 3. The principal differences between the applicant and staff result from the staff's use of the larger water usage per residential customer for 1976 and the fact that the staff's estimated 1976 industrial water sales were substantially higher than applicant's estimate.

A staff engineer testified that applicant had not furnished a detail breakdown of its large industrial water users. In preparation for hearings the staff conducted a thorough investigation of industrial usage for both 1975 and 1976. The staff engineer stated that 80 percent of industrial water for sales by volume are concentrated in approximately the top 10 percent of industrial customers. The staff engineer contacted key officials of the largest industrial accounts. In addition to its review of anticipated industrial customer water usage, the staff engineer reviewed the anticipated usage of the County Sanitation District of Los Angeles County (District), a large public authority customer. The District estimated its projected water usage in 1976 to be greatly in excess of its past water usage (Exhibit 15, page 2).

Both the applicant and the staff estimated a decline in residential water sales per customer from 1975 to 1976. The applicant, according to the staff engineer, used a modified graphical analysis with a negative slope with data points for 1970 to 1974. The staff presented a residential usage multiple regression analysis using six sets of each year weather data normalized. The staff witness projected a decline in residential usage for test year 1976 (Exhibit 16).

Neither the staff's nor the applicant's witnesses were able to determine the factors involved which brought about the anticipated decline in water usage. They were in agreement that there was a trend downward in residential usage for the short-term future.

The recent recorded data is consistent with the staff's results, in that the staff's normalized estimates are above the recorded sales. In contrast, applicant's estimated usage is below the recorded sales. Under tho circumstances, we will adopt the staff's estimated water sales.

Regulatory Expenses

Applicant amortized (over three years) consultant fees of $25,000 for preparation of its original revenue requirements studies (Exhibit 4) in this proceeding. Applicant included a total of $30,000 of such fees (over three years) in its amended showing. The staff disallowed $10,000 of these costs on the grounds that applicant itself revised the original revenue requirement study and relied upon its own revenue requirement study (Exhibit 7) in these proceedings. Both applicant and the staff would amortize this regulatory expense item over a three-year period.

The evidence is that the original revenue requirement study dated October 1974 (Exhibit 4) was required at the time of filing of the original application, and that applicant did not have in-house capability of preparing such a study. The amended application required a revised revenue requirement study when the calendar year 1976 was included with the original 1975 test year. Applicant expects to be able to prepare necessary exhibits in-house in future regulatory proceedings. Under the circumstances, we cannot conclude that applicant's regulatory commission expense in this case is an unreasonable item. We expect that applicant's future costs in this area will be substantially reduced as a result of its experience derived, in part, from working with its consultant in this proceeding.

We find it reasonable to allow the regulatory expense requested by applicant.

Additional Administrative and General Expenses

Under Account 799, Miscellaneous Administrative and General Expenses, the staff disallowed dues and donations paid to organizations of a nonutility nature and fees paid to company officials for participation in board of directors' meetings. We adopt these disallowances as recommended by the staff. Dues and donations paid for nonutility purposes are not chargeable to the ratepayers. Moreover, we adopt the staff's view that regular company officials should not be compensated by additional payments for attending meetings of the board of directors.

Under Account 812, applicant proposed to reduce capitalized payroll to $25,000 annually. The staff noted that the amounts formerly transferred from payroll expense to capitalized expense had been $50,000 to $55,000 annually. The staff engineer recommended a gradual reduction in capitalized payroll to $40,000 in 1975 and $30,000 in 1976. In view of the continuing high level of construction expenditures by applicant, the record supports the staff recommendation.

Payroll Expenses

The difference between applicant and staff arose from the staff's use of a 6 percent payroll increase for all employees except officers for 1976. The staff also excluded expense of two part-time workers and did not allow overtime for administrative and general personnel. Applicant's 1976 payroll expenses assume a 6.5 percent general pay increase in the year 1976 and allowed more overtime. The staff estimates were based upon more recent information and will be adopted.

Rate Base Items

Applicant and the staff differed on the proper treatment of plant items upon retirement from service of two wells. Applicant continues to carry in its plant accounts equipment at the well sites. Applicant stated that this equipment was still useful and would ordinarily be transferred to the materials and supplies account (and thus remain in rate base). The staff reviewed the material available and recommended a transfer to materials and supplies of a smaller amount than carried by applicant in the plant accounts. The staff would retire the additional remaining plant.

Additional differences arose from the staff's use of more recent data on plant additions. The capitalization of administrative and general payroll, discussed above, would also result in some rate base differences. For the reasons stated above we will adopt the staff estimates on capitalization of administrative and general payroll.

The staff witness specifically reviewed the plant items in arriving at his estimates. We find the staff's estimates of 1976 rate base to be reasonable.

Conclusion on Summary of Earnings

Our conclusions on the estimated 1976 summary of earnings are incorporated in Table I. The staff's recommended rate of return (9.5 percent) would require a gross revenue increase of $606,900 (12.1 percent). The applicant's requested increase of $757,000 would increase gross revenues 15.58 percent. Based on our adopted estimates and rate of return allowance, applicant will be authorized to increase gross revenues $634,300 annually (12.65 percent).

Table I

Summary of Earnings
Year 1976 Estimated

Item	Applicant Present Rates	Staff Present Rates	Adopted Present Rates	Adopted Rates
	(Dollars in Thousands)			
Operating Revenues	$ 4,860	$ 5,014.7	$ 5,014.7	$ 5,649.0
Operating Expenses				
Operating & Maintenance	2,598	2,742.4	2,742.4	2,746.4
Administrative & General	496	467.8	470.8	470.8
Taxes Other Than Income	454	433.6	433.6	433.6
Taxes on Income	91	151.6	143.6	475.7
Allocation to Subsidiaries	(23)	(23.0)	(23.0)	(23.0)
Depreciation	464	458.5	458.5	458.5
Total Oper. Expenses	$ 4,080	$ 4,230.9	$ 4,225.9	$ 4,562.0
Net Operating Revenue	$ 780	$ 783.8	$ 788.8	$ 1,087.0
Depreciated Rate Base	$11,375.5	$11,321.8	$11,321.8	$11,321.8
Rate of Return	6.86%	6.92%	6.97%	9.60%

(Red Figure)

Rate of Return

The staff presented the testimony of a financial examiner from the Finance and Accounts Division on the issue of rate of return. The staff witness differed from applicant's witness regarding the reasonable return to be adopted in establishing rates for the test year 1976. The assumed capital costs of applicant (Table II) and staff (Table III) are set forth below:

Table II

Recommended Range for Rate of Return

Item	Capital Ratios	Cost Factors	Weighted Cost	Allowance for Common Stock Equity: 12.00%	12.50%	13.00%	13.50%	14.00%
				Weighted Totals				
Long-Term Debt	50.61%	7.97%	4.03%					
Preferred Stock	5.90	5.00	.30					
Common Stock Equity	43.49			5.22%	5.44%	5.65%	5.87%	6.09%
Subtotal	56.51		4.33	4.33	4.33	4.33	4.33	4.33
Total	100.00%			9.55%	9.77%	9.98%	10.20%	10.42%

Table III

Recommended Range for Rate of Return

Item	Capital Ratios 1/	Cost Factors 2/	Allowance for Common Stock Equity: 11.47%	11.71%	11.94%	12.18%
			Weighted Totals			
Long-Term Debt	51.31%	7.99%	4.10%	4.10%	4.10%	4.10%
Preferred Stock	5.98	5.00	.30	.30	.30	.30
Common Stock Equity	42.71		4.90	5.00	5.10	5.20
Total	100.00%		9.30%	9.40%	9.50%	9.60%

1/ Consolidated capital structure as estimated by the staff.

2/ As developed in Table 3, Staff Exhibit 11.

The staff witness recommended that a rate of return of 9.50 percent be adopted for ratemaking purposes from his recommended range of 9.30 to 9.60 percent. Applicant's requested rates were designed to produce a rate of return of 9.98 percent (13 percent assumed earnings on common equity).

It is apparent that the staff witness recognized that a substantial increase in the allowed rate of return was required for the applicant. Decision No. 80370 dated August 15, 1972 in applicant's last general rate case adopted a rate of return of 7.90 percent. That rate of return incorporated a 10.16 percent equity allowance.

In common with all other companies requiring additional capital, applicant has been faced with substantially increasing cost of capital in recent years. Applicant's last issue of first mortgage bonds, Series G, bears an effective rate of 10.29 percent (see Exhibit 11, Table 3). Applicant's last issue of sinking fund notes bear an effective rate of 10.30 percent. These substantially increased rates are reflected in the weighted cost of long-term debt in the exhibits set forth above.

Applicant's witnesses testified that in November 1974 applicant issued and sold common stock in order to improve its capital structure. The staff's Finance and Accounts witness stated that applicant had a good capital ratio. We conclude that the staff agrees that applicant's sale of additional common stock was desirable. The difficulty with the past allowance for common equity is that investors are not willing to invest in common stock when senior securities might have a better return. The actual issue of common stock in November of 1974 was below the book value that existed at that time. There was a substantial dilution in book value and applicant did not sell all shares that were offered.

We do not accept the proposition of applicant's witness that very high allowances should be made on common equity with the expectation that such high allowances will result in market values in excess of book. However, we must recognize that applicant has had substantial capital requirements in recent years and will have substantial capital construction requirements in the future. The existing high interest costs of long-term debt support the staff's recommended increase in the allowance for common equity.

Under all the circumstances, we will adopt rates in this proceeding based upon an allowed rate of return of 9.6 percent. This is the top of the staff's range. We recognize that applicant has been in a good financial condition in recent years, and if applicant continues to achieve a rate of return within the staff's range (9.3 to 9.6 percent) we anticipate that applicant will continue to be in a sound financial position. Our selection of the top of staff's range is based on our conclusion that applicant should be afforded an opportunity to earn a return on its common equity of 12.18 percent under present conditions.

Rates

Applicant's present and proposed rates were set forth in Exhibit 3. Applicant does not propose to increase the rates for private and public fire protection. Applicant's president testified that the present rates on such fire protection were higher than generally used in the State of California. Applicant proposed to double the service charge on general metered and metered irrigation service. Quantity rates for general metered service would not be increased in the first block (first 25 Ccf per month) and the second and third blocks would be increased 8.4 percent and 13.3 percent, respectively.

The staff's prepared testimony had no recommendation regarding rate structure. At hearing a staff witness commented on an inquiry from the examiner regarding the concept of lifeline rates. The staff witness suggested that the minimum service charge rate be increased from $1 to $1.50 per month and the first two rate blocks for general metered service be combined at single rate of approximately 0.361.

The concept of lifeline rates suggests that charges for a certain minimum quantity of water for average residential use will not be increased until the average system rate is significantly increased (compare Section 739, California Public Utilities Code). Although our record is far from exhaustive on this matter, some evaluation of the respective rate recommendations is possible.

The evidence indicates that average residential usage is 15 Ccf per month. The staff's recommendation at 15 Ccf per month would result in a monthly residential charge of $6.92, the applicant's $7.28. At 25 Ccf per month, the staff's recommendation results in $10.53, applicant's $10.80. At 50 Ccf per month, the staff's rate totals $19.55, applicant's $19.23. We note that the available water use analysis indicates that the 50 Ccf per month usage includes 99.6 percent of residential bills and 98 percent of residential water consumption (Exhibit 4, page 35, Table 5-5). Among business users, the water use analysis indicates 50 percent of billings fall within the first 25 Ccf rate block with total water consumption of five percent.

Applicant's requested increase in the service charge is based on the contention that the proposed rate of $2 per month is below allocated customer costs. The staff did not dispute this claim. Failure to recover this customer cost is, in effect, a subsidy to all low volume nonresidential users.

The impact of the proposed increases upon an average residential use appears substantially the same under the two proposals. We will adopt the proposed increase in the service charges and combine the first two rate blocks. We adopt the applicant's requested increased quantity rate in the tail block for general metered service (over 5,000 Ccf per month).

The new initial block quantity rate (up to 5,000 Ccf per month) is the average of the present quantity rates for the first two blocks. We adopt the staff's recommendation and combine the first two blocks. The result is that the average residential user at 15 Ccf per month will receive an increase from $6.28 (present) to $6.97 (adopted). At 25 Ccf the increase is $9.80 (present) to $10.28 (adopted). The tail block rate will be increased for large users under general metered service 13.3 percent and the quantity rate for metered irrigation service is increased 13.4 percent. These increases are reasonable since the required revenue increase is 12.65 percent.

<u>Findings</u>

1. Applicant's adopted 1976 operating revenues, expenses, and rate base as set forth in Table I are reasonable estimates.

2. Applicant is entitled to rates estimated to produce a rate of return of 9.6 percent on its 1976 rate base (an allowance of 12.18 percent on common equity).

3. Based on adopted 1976 estimates, an increase of approximately $634,300 (12.65 percent) will produce a rate of return of 9.6 percent.

4. The increased rates set forth in Appendix A attached hereto are reasonable, and the present rates and charges, insofar as they differ from those prescribed herein, are for the future unjust and unreasonable.

The Commission concludes that the application should be granted to the extent set forth in the order which follows, and in all other respects denied.

O R D E R

IT IS ORDERED that after the effective date of this order, applicant Dominguez Water Corporation is authorized to file 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 of the revised schedules.

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

Dated at San Francisco, California, this 29th day of JUNE, 1976.

William Symons Jr.
President

Vernon L. Sturgeon

[illegible]

John Batinovich

Commissioners

Commissioner D. W. Holmes, being necessarily absent, did not participate in the disposition of this proceeding.

Schedule No. 1

General Metered Service

APPLICABILITY

Applicable to all metered water service excepting metered irrigation service. (T)

TERRITORY

Portions of Carson, Los Angeles, Long Beach, Torrance, and vicinity, Los Angeles County.

RATES

	Per Meter Per Month	
Service Charge:		
For 5/8 x 3/4-inch meter	$ 2.00	(I)
For 3/4-inch meter	3.00	
For 1-inch meter	5.00	
For 1½-inch meter	10.00	
For 2-inch meter	16.00	
For 3-inch meter	32.00	
For 4-inch meter	42.00	
For 6-inch meter	70.00	
For 8-inch meter	104.00	
For 10-inch meter	130.00	
For 12-inch meter	200.00	
For 18-inch meter	300.00	(I)
Quantity Rates:		
First 500,000 cu.ft., per 100 cu.ft.	$ 0.331	(C)
Over 500,000 cu.ft., per 100 cu.ft.	0.222	(I)

The Service Charge is applicable to all metered service. It is a readiness-to-serve charge to which is added the charge, computed at the Quantity Rates, for water used during the month.

Schedule No. 3M

METERED IRRIGATION SERVICE

APPLICABILITY

Applicable to all metered irrigation water service. (T)

TERRITORY

Portions of Carson, Los Angeles, Long Beach, Torrance, and vicinity, Los Angeles County.

RATES

	Per Meter Per Month	
Service Charge:		
For 1-inch meter or smaller	$ 5.00	(I)
For $1\frac{1}{2}$-inch meter	10.00	
For 2-inch meter	16.00	
For 3-inch meter	32.00	
For 4-inch meter	42.00	
For 6-inch meter	70.00	
For 8-inch meter	104.00	
For 10-inch meter	130.00	
For 12-inch meter	200.00	
For 18-inch meter	300.00	(I)
Quantity Rates:		
For all water delivered, per 100 cu.ft.	$ 0.144	(I)

The Service Charge is applicable to all metered service. It is a readiness-to-serve charge to which is added the charge, computed at Quantity Rates, for water used during the month.