

Decision 84 06 091

JUN 6 1984

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application)
 of California-American Water)
 Company for an order authorizing)
 it to increase its rates for water)
 service in its Coronado District.)

Application 83-10-07
 (Filed October 5, 1983)

Steefel, Levitt & Weiss, by Lenard G. Weiss,
 Attorney at Law, for California-American
 Water Company, applicant.
Mary McKenzie, Attorney at Law, and Sung B. Han,
 for the Commission staff.

O P I N I O NSummary of Decision

California-American Water Company (Cal-Am), a California corporation, seeks authority to increase its rates for water service in its Coronado District. The increases proposed are in steps designed to increase annual revenues in test year 1984 over rates now in effect by \$639,800 (16.7%), for test year 1985 by \$269,400 (5.7%) over the proposed 1984, and for test year 1986 by \$261,300 over the 1985 proposed rates. By this decision Cal-Am is authorized to increase its rates by about 6.66% over present rates for 1984, 2.56% over the authorized 1984 rates for 1985 and 1.84% over the 1985 authorized rates for 1986 as compared to the requested increases of 16.70%, 6.00%, and 5.50% respectively.

The rate of return on rate base of 11.78% for 1984, 11.99% for 1985, and 12.08% for 1986 is found reasonable. The authorized return on equity is 14.50%.

I. Background

The Coronado District provides general metered service to the cities of Coronado and Imperial Beach, a portion of the City of San Diego lying south of San Diego Bay, and contiguous unincorporated areas; all in the County of San Diego. All water is purchased from the City of San Diego.

As of December 31, 1982, the Coronado District has 868,203 lineal feet of transmission and distribution mains varying in size from 3/4-inch diameter to 25-inch diameter. The number of service connections as of December 31, 1982 was 16,820.

An informal public meeting, jointly sponsored by Cal-Am and the Commission staff, was held at the Coronado City Hall, November 28, 1983 to discuss the application. Each customer was notified of the meeting by bill insert. Five customers attended the meeting. The Commission received nine letters from customers protesting the granting of any rate relief.

After due notice, public hearings were held in Los Angeles, February 15, 16 and 17, 1984. None of Cal-Am's customers appeared at those hearings. The matter was submitted February 17, 1984 subject to the filing of concurrent briefs due March 12, 1984.

Cal-Am presented testimony and exhibits through its director of rates and revenue, a revenue requirements specialist, and its vice-president of operations. The staff studies were presented by a project manager, a financial examiner, a research analyst, and two utilities engineers.

II. Rate of Return

As it did in its Monterey District rate application filed in February 1982 and continuing with its Los Angeles area rate applications filed in December 1982, Cal-Am requests rates that will produce a return on common equity of 16%. Cal-Am witness Barker testified that the 16% return on equity request is needed because (1) common equity capital is more risky than debt capital (bonds), (2) investors require higher returns on common stock than on bonds to compensate for the higher risk, (3) a common stock investor expects steady dividends that keep up with the rate of inflation and (4) an investor expects an increase in the book value of his original investment through the reinvestment of retained earnings. He also stated that using U.S. Treasury Bonds as a base, the risk premium associated with water utility stock over 10 years and long-term U.S. Treasury Bonds average 440 to 500 basis points above bond interest rates.

Staff witness Mowrey recommended a return on common equity of 14.50%. He stated that rate of return is an expression of a utility's capital costs-debt and equity. The rate of return recommendation results from an estimation of those costs applied to a projected capital structure determined for these proceedings. The cost of debt is contractual and therefore easily determined, although cost assumptions must be made regarding future financing over the test period. He stated the cost of common equity is considerably more difficult to determine and therefore is often the area of greatest differences of opinion. The recommended return on common equity was determined after an analysis of the risk, both business and financial, associated with Cal-Am. ✓

Staff's recommended capital structure and computed rate of return for test years 1984, 1985 and 1986 are as follows:

<u>1984</u>	<u>Component</u>	<u>Capitalization Ratios</u>	<u>Cost</u>	<u>Weighted Cost</u>
	Long-term Debt	52.00%	9.26%	4.82%
	Common Equity	<u>48.00</u>	14.50%	<u>6.96</u>
	Total	100.00%		11.78%
 <u>1985</u>				
	Long-term Debt	52.00%	9.67%	5.03%
	Common Equity	<u>48.00</u>	14.50%	<u>6.96</u>
	Total	100.00%		11.99%
 <u>1986</u>				
	Long-term Debt	52.00%	9.84%	5.12%
	Common Equity	<u>48.00</u>	14.50%	<u>6.96</u>
	Total	100.00%		12.08%

The staff witness used a constant average capital structure for the entire test period which Cal-Am's witness agreed with. Cal-Am's witness also agreed with staff's embedded cost of debt.

Consistent with the return on common equity authorized in Cal-Am's other districts (D.83-08-054 and D.82-12-122), we adopt as reasonable the above financial structure, cost of debt and the staff's recommended return on equity of 14.50%.

III. Summary of Earnings

Revised Exhibit 2 sets forth a comparison of Cal-Am's and staff's summary of earnings for test years 1984, and 1985 at both present and proposed rates. The exhibit indicates items stipulated to and areas of disagreement between Cal-Am and staff.

The following tables sets forth the summary of earnings as estimated by Cal-Am and the staff for test years 1984 and 1985 together with our adopted results:

CALIFORNIA-AMERICAN WATER COMPANY
CORONADO DISTRICT
- TEST YEAR 1984 -

Present Rates

	<u>Applicant</u>	<u>Staff</u>	<u>Diff.</u>	<u>Adopted</u>	<u>Authorized Rates</u>
	(Dollars in Thousands)				
Operating Revenues	\$4,525.2	\$4,525.2	\$ -	\$4,525.2	\$4,826.5
<u>Operating Expenses</u>					
<u>O&M</u>					
Payroll	406.0	398.3	7.7	406.0	406.0
Purch. Water	2,230.7	2,230.7		2,230.7	2,230.7
Purch. Power	.1	.1		.1	.1
S/S	-	-		-	-
Pumping	5.4	5.4		5.4	5.4
Water Treat.	13.6	13.6		13.6	13.6
Tran. & Dist.	107.0	107.0		107.0	107.0
Cust. Accts.	95.5	95.5		95.5	95.5
Subtotal	2,358.3	2,850.6	7.7	2,858.3	2,858.3
<u>A&G</u>					
Payroll	155.5	152.6	2.9	155.5	155.5
Off. Supplies	52.5	52.5		52.5	52.5
Prop. Ins.	.2	.2		.2	.2
Inj. & Damage	21.8	21.8		21.8	21.8
Emp. Pen/Ben.	129.0	126.6	2.4	128.9	128.9
Reg. Comm/Exp.	12.0	9.7	2.3	12.0	12.0
Bus. Tax	-	-		-	-
Outside Ser.	40.8	40.8		40.8	40.8
Misc. Gen. Exp.	5.1	5.1		5.1	5.1
Genl. Plant	21.6	21.6		21.6	21.6
Subtotal	438.5	430.9	7.6	438.4	438.4
General Off. Pro.	211.1	202.1	9.1	206.4	206.4
<u>Taxes - other</u>					
Ad Valorem	57.7	57.7		57.7	57.7
Payroll	42.8	39.4	3.4	42.4	42.4
Subtotal	100.5	97.1	3.4	100.1	100.1
Depreciation	222.1	222.1		222.1	222.1
Uncollectibles	18.4	18.4		18.4	19.6
Franchise Tax	-	-		-	-
SCPT	32.9	35.5	(2.7)	33.3	62.1
FIT	132.6	144.5	(11.9)	134.6	259.4
Total Oper. Exp.	4,014.4	4,001.2	13.2	4,016.6	4,166.4
Operating Income	510.8	524.0	(13.2)	513.6	660.1
Rate Base	5,603.5	5,603.5	-	5,603.5	5,603.5
Rate of Return	9.12%	9.35%		9.17%	11.78%

(Red Figure)

CALIFORNIA-AMERICAN WATER COMPANY
CORONADO DISTRICT
- TEST YEAR 1985 -

<u>Present Rates</u>					<u>Authorized Rates</u>
<u>Applicant</u>	<u>Staff</u>	<u>Diff.</u>	<u>Adopted</u>	(Dollars in Thousands)	
Operating Revenues	\$4,570.8	\$4,570.8	-	\$4,570.8	\$4,999.7
<u>Operating Expenses</u>					
<u>Q&M</u>					
Payroll	444.4	418.4	26.0	444.4	444.4
Purch. Water	2,251.9	2,251.9		2,251.9	2,251.9
Purch. Power	0.1	0.1		0.1	0.1
S/S	-	-		-	-
Pumping	5.7	5.7		5.7	5.7
Water Treat.	14.3	14.3		14.3	14.3
Trans.&Dist.	113.0	113.0		113.0	113.0
Cust. Accts.	98.5	98.5		98.5	98.5
Subtotal	2,927.9	2,901.9	26.0	2,927.9	2,927.9
<u>A&G</u>					
Payroll	170.2	160.3	9.9	170.2	170.2
Office Supplies	55.4	55.4		55.4	55.4
Prop. Ins.	0.2	0.2		0.2	0.2
Inj. & Damage	22.9	22.9		24.0	24.0
Emp. Pen/Ben.	147.7	137.5	10.2	145.9	145.9
Reg. Comm. Exp.	12.0	9.7	2.3	12.0	12.0
Bus. Tax	-	-		-	-
Outside Serv.	43.0	43.0		43.0	43.0
Misc. Gen. Exp.	5.4	5.4		5.4	5.4
Genl. Plant	22.9	22.9		22.9	22.9
Subtotal	479.7	457.3	22.4	479.0	479.0
General Off. Pro.	228.8	212.8	16.0	222.3	222.3
<u>Taxes-other</u>					
Ad Valorem	60.1	60.1		60.1	60.1
Payroll	47.0	41.1	5.9	45.9	45.9
Subtotal	107.1	101.2		106.0	106.0
Depreciation	228.4	228.4		228.4	228.4
Uncollectibles	18.6	18.6	-	18.6	20.3
Franchise Tax	0.0	0.0	-	0.0	-
SCFT	19.3	26.2	(6.9)	20.1	61.1
F.I.T.	76.1	106.1	(30.0)	79.6	257.3
Total Oper. Exp.	4,085.9	4,052.5	33.4	4,081.9	4,302.3
Operating Income	484.9	518.3	(33.4)	488.9	697.4
Rate Base	5,816.8	5,816.8		5,816.8	5,816.8
Rate of Return	8.34%	8.91%		8.40%	11.99%

(Red Figure)

Operating Revenues

Cal-Am stipulated to the staff's operating revenue estimates at present rate of \$4,525,200 for test year 1984 and \$4,570,800 for test year 1985. We will adopt these figures.

Operating Expenses

Payroll Expense

Cal-Am's estimates of total operating and maintenance (O&M) payroll expenses are \$406,000 for 1984 and \$444,400 for 1985 as contrasted to the staffs estimates of \$398,300 and \$418,400 respectively. Cal-Am's administrative and general (A&G), payroll estimates are \$155,500 for 1984 and \$170,200 for 1985 compared to the staff estimates of \$152,600 and \$160,300 respectively. The differences reflect the rate of wage escalation to be adopted to cover anticipated wage increases for the 1984-1986 test period.

Escalation Factors

Escalation factors used by Cal-Am and the staff to project operating expenses for the years 1984, 1985 and 1986 were a major cause for differences in expense estimates and considerable hearing time was devoted to this issue. Though Cal-Am revised downward its original escalation increases, it was still greater than the staff's. Tabulated below is a comparison of the labor escalation factors used by Cal-Am and the staff:

Labor Escalation

	<u>Cal-Am(Original)</u>	<u>Cal-Am(Revised)</u>	<u>Staff</u>
	<u>Percent Increase</u>	<u>Percent Increase</u>	<u>Percent Increase</u>
1984	9.5	9.0	4.11
1985	9.0	8.0	4.98
1986	9.0	8.0	5.13

For nonlabor Cal-Am adopted staff incremental increases for 1985 and 1986 of 1.2% and .4% but used 6.4% as a starting point rather than the staff's 4.5%. The 6.4% figure used by Cal-Am was the CPI for San Diego, November 1982-November 1983. A comparison of the nonlabor escalation factor is as follows:

Nonlabor Escalation

	<u>Cal-Am</u>	<u>Staff</u>
	<u>Percent Increase</u>	<u>Percent Increase</u>
1984	6.4	4.5
1985	7.6	5.7
1986	8.0	6.1

It is Cal-Am's position that the prevailing wages paid its employees is considerably lower than wages paid by other employers in the San Diego area for comparable skills. Cal-Am is in what its witness Foy described as a "catch-up mode" with its employee wages in attempting to bring these wages into line with other employee wages paid throughout the San Diego area.

Staff's labor escalation rates would appear reasonable, assuming that Cal-Am's employees are presently receiving wages comparable to that received by other employees in the other Cal-Am districts. However, staff overlooks Cal-Am's attempt to bring its Coronado district employee wages up to the prevailing other Cal-Am district pay rates, which would ensure better employee morale and low employee turnover thereby benefitting both the company and its ratepayers. ✓

The record fully supports Cal-Am's position that increases to employees in excess of the staff's recommended increases are justified in light of the discrepancies in the present wage levels of Cal-Am employees as compared to the other Cal-Am districts in general. We place Cal-Am on notice, however, that the rate levels authorized here

for the years 1984, 1985, and 1986 are based on revenue requirements providing for the above escalation rates. The wage escalation factors actually effected will be reviewed in conjunction with the annual attrition allowance review and suitable adjustments will be made to such attrition allowances should it be determined that the escalation factors placed into effect are less than set forth in the record in this proceeding.

The staff nonlabor escalation rates are reasonable and we adopt them.

Purchased Water and Power Expenses

Cal-Am stipulated to the staff's estimates for purchased water and power expenses and will be adopted.

Source of Supply, Pumping
and Water Treatment Expenses

Cal-Am's and staff's estimates for source of supply, pumping and water treatment expenses are the same and will be adopted.

Transmission & Distribution and
Customer Accounting Expenses

Cal-Am stipulated to staff's estimates for transmission and distribution and customer accounts expenses except as to staff's projected rate of escalation for nonlabor items and those estimates will be adopted.

Customer Accounts

Initially Cal-Am did not include the cost of third party notification before terminating water service as directed by D.83-06-065. This cost is estimated to be \$6,500 per year. With this and other minor adjustments the staff and Cal-Am agree to the estimated costs for this account.

Administrative and General Expenses

Cal-Am's estimates of administrative and general expenses total \$438,500 for test year 1984 and \$479,700 for test year 1985 contrasted to staff estimates of \$430,900 and \$457,300 respectively.

The estimates are the same for office supplies, property insurance, injuries and damages, business tax, outside services, miscellaneous general expense and general plant. These items total \$142,000 for test year 1984 and \$149,800 for test year 1985. These amounts are reasonable and will be adopted for this proceeding.

Cal-Am's A&G payroll expense was estimated to be \$155,500 for test year 1984 and \$170,200 for test year 1985 as compared to the staff's estimates of \$152,600 and \$160,300 respectively. The differences relate to the proper wage escalation factors to be applied to this expense. As discussed in the section on payroll, we are allocating the adopted payroll expense between O&M and A&G on the basis of Cal-Am's relative values on a one-time adjustment.

Employee pension and benefits expense consists of pensions, group insurance, and other. Cal-Am's estimate for this item was \$129,000 for test year 1984 and \$147,700 for test year 1985 as compared to the staff's estimates of \$126,600 and \$137,500 respectively. Cal-Am stipulated to the staff's pension and group insurance estimated percentages, thus the difference relates to the proper wage escalation factor to be applied to this expense. Again, as discussed in the section on payroll we are allocating the adopted payroll expense on the basis of Cal-Am's relative values on a one-time adjustment.

Regulatory Commission Expense

Cal-Am estimated regulatory expenses at \$25,000 to be amortized over three years. The staff recommends only \$18,000 be allowed, a difference of about \$2,300 per year.

Cal-Am based its estimate on its counsel's best estimate of what expenses would be, anticipating one or possibly two days of hearing without extensive public participation (Exhibit 7.). The staff witness stated he based his estimate on fees and costs for Cal-Am districts in the Los Angeles area for 1983 rate cases and a study of legal costs authorized other water utilities which have lower fees per customer and/or per dollar of revenue.

We believe Cal-Am's estimate of \$25,000 for regulatory expense amortized over three years is reasonable and will be adopted. As pointed out by applicant it is inherently more efficient and less costly to prosecute four rate cases at once, as was done in its Los Angeles area rate cases, than one case at a time. Further the estimates of counsel was for one or two total days of hearing where in fact there were three days of hearing with related prehearing preparation and post hearing briefing.

Outside Services

Cal-Am and staff also stipulated to the estimate for outside services of \$40,800 for test year 1984 and \$43,000 for 1985 and will be adopted.

General Office Prorate

The difference between Cal-Am and staff in general office expense total \$9,100 for 1984 and \$16,000 in 1985. The differences in payroll estimates and related insurance and pension expenses for the corporate office relate to the rate of labor escalation previously discussed. Items of dispute are the amount for California Water Association (CWA) dues, physical examinations for certain corporate officers and expenses related to Cal-Am safety program.

The staff in its estimates disallowed the following charges in Account 795:

Orientation slide show	\$ 850
Newsletter	765
Safety Banquet	200
Physical exams	<u>385</u>
Total	2,200

Staff argues these costs confer no benefit on ratepayers and should not be allowed for ratemaking purposes. Cal-Am states these safety program expenses are justified in that overall expenses are reduced when temporary employees are not required and that it keeps workman's compensation insurance rates at their lowest possible level.

We believe the ratepayers are benefitted indirectly from these programs and therefore we will adopt the Cal-Am estimates as reasonable.

With respect to the CWA dues issue, during the hearing Cal-Am witness Barker introduced Exhibit 8 requesting a portion of the annual dues paid to CWA be allocated to the Coronado District. The exhibit and testimony were received into evidence over the staff's objection. On March 1, 1981 the staff renewed its motion to strike and exclude Exhibit 8 and related testimony.

The staff states that because this item was not included in the application when it was filed it should not be considered. Staff argues that it violates due process of the ratepayers as embodied in the United States Constitution, § 454 of the Public Utilities Code, the Commission's Rules of Practice and Procedure and the Commission's Regulatory Lag Program.

Staff's motion to strike was properly overruled and the renewed motion should be denied. The staff was appraised of Cal-Am's inadvertent error and its desire to recover this expense on February 3, 1984. Staff thus had more than 10 days to consider the reasonableness of the request. Further, the staff was well aware that this item of expense had appeared in prior rate cases without being an issue. Nor is there a violation of due process, § 454 of the Public Utilities Code, or the Commission's Rules of Practice and Procedure. Section 454 requires that ratepayers be noticed of any proposal to increase a rate or charge. Rule 23 requires that the application be amended in the event 'that applicant desires to revise the level of rates shown in the original application...' The total amount of the requested increase is known. This is the amount, or ceiling, that the Commission can consider without any due process violation.

Rate Base

In recent years during hot weather and consequent high water demand, Cal-Am experienced difficulty in keeping its Montgomery and Highland Reservoirs full. To transport water from the Montgomery meter connection to the Highland reservoir, Cal-Am proposes to install an 11,000-foot, 24-inch transmission main in Palm Avenue (Palm Avenue Project). Plans call for the project to be constructed in two phases: 5,500 feet to be in service by June 1984, the remainder ready for service in 1986. Cal-Am included this project in its rate base calculation for this proceeding.

The staff recommends that the Palm Avenue Project be excluded from rate base and the utility be allowed to file advice letters upon completion of each of the two project phases to insure that the rate payers pay for the project only when the project is completed and they receive the benefits of improved service. Cal-Am stipulated to the staff recommendation.

Cal-Am also stipulated to all of the other staff rate base calculations and recommendations.

Taxes

Cal-Am stipulated to the staff's estimates of ad valorem taxes leaving only payroll taxes for determination for this item. Consistent with our adopted payroll, we will adopt as reasonable for this proceeding "taxes-other" of \$100,100 for test year 1984 and \$106,000 for test year 1985.

Depreciation Expense

Cal-Am stipulated to staff's estimate for depreciation. Accordingly we will adopt \$222,100 as reasonable for test year 1984 and \$228,400 for test year 1985 consistent with our Palm Avenue Project exclusion discussed in rate base.

Rate Design

Cal-Am originally proposed to increase the service charge gradually to collect up to 27.6% of revenue with the remaining 72.4% collected from quantity rates by 1986. The staff recommends adoption of a rate design which would maintain the lifeline differential of 25% for residential customers. The staff does not object to increasing the service charge for residential customers so long as no group of users is exposed to excessive increases. The following tabulation compares the rate increases over the the January 1, 1976 level at present and proposed rates, and the lifeline rate increase that will maintain the 25% lifeline differential as recommended by the staff:

At Present Rates:

Total Cumulative Increases	98%
Lifeline Rate Increases	35%
To Maintain a 25% Differential, Lifeline Rate Should have Increased	58%

At Utility's Proposed Rates in 1986:

Total Cumulative Increases	158%
Lifeline Rate Increases	155%
For a 25% Differential, Lifeline Rate Should be This Percentage Above January 1, 1976, Level	106%

Cal-Am stipulated to the staff rate design recommendation.
It is reasonable and will be adopted.

Attrition

An attrition allowance is granted for increased financial costs and increased expenses and rate base items which are not offset by the increases in revenues in the third year of the three-year rate increase. As previously discussed, the test year 1986 financial attrition was computed by staff to be 0.09% which on our adopted financial structure and debt costs requires a rate of return of 12.02% to provide our adopted return on equity of 14.50%.

The operational attrition is derived by extrapolating the two test year estimates without the nonrecurring major plant addition, Industrial Park Reservoir excluded for purposes of calculation. On this basis we adopt as reasonable an operational attrition of 0.77%.

IV. Customer Service

Testimony of the staff witness indicated the number of complaints investigated and resolved by Cal-Am in the Coronado District in 1982 and through August 1983 were as follows:

	<u>1982</u>	<u>Through August 1983</u>
Water Quality	29	77
Pressure	31	42
Billing	332	339
Misc.	<u>225</u>	<u>290</u>
Total	<u>617</u>	<u>648</u>

According to the witness' testimony, most of these complaints were resolved quickly and in a satisfactory manner. There were no formal complaints filed. Staff considers the quality of service provided in the Coronado District to be satisfactory.

Findings of Fact

1. Cal-Am is in need of additional revenue for its Coronado District but the proposed rates set forth in the application are excessive.
2. A rate of return on common stock equity of 14.5% and overall rates of return of 11.78%, 11.99%, and 12.08%, for the years 1984, 1985, and 1986, respectively, are reasonable.
3. Staff's estimates of cost of debt and capital structure are reasonable.
4. The increases in rates and charges authorized by this decision are justified, and are just and reasonable.
5. The labor escalation factor used by Cal-Am to bring its Coronado District employees wages into line with other employee wages in the San Diego area and in line with Cal-Am's other districts is reasonable.

6. Cal-Am's estimate for regulatory expense amortized over three years is reasonable.

7. Cal-Am account 795 expenses that staff would disallow are reasonable.

8. The California Water Association dues were properly considered and allowed as an expense item without violating due process, Public Utilities Code § 454 or the Rules of Practice and Procedure.

9. The authorized increase in rates at the rate of return for test year 1984 is expected to provide increased revenues for Cal-Am's Coronado District of approximately \$301,300 as compared to a requested increase of \$639,800 over present rates.

10. The authorized increase in rates at the 11.99% rate of return for test year 1985 is expected to provide increased revenues for Cal-Am's Coronado District of approximately \$124,600 over the authorized 1984 rates as compared to a requested increase of \$269,400.

11. An allowance of 0.77% in rate of return to compensate for operational test year 1986 is reasonable. Allowing for this operational attrition and a financial attrition of 0.09% in determining the authorized increase in rates at the 12.08% rate of return for test year 1986 is expected to provide increased revenues for Cal-Am's Coronado District of approximately \$92,200 (1.84%) over the authorized 1985 rates as compared to a requested increase of \$261,300 (5.50%) over Cal-Am's authorized 1985 rates.

12. The adopted estimates previously discussed here of operating revenues, operating expenses and rate base for the test years 1984 and 1985 reasonably indicate the result of Cal-Am's operations in its Coronado District in the near future.

13. Adoption of the staff recommended rate design is reasonable.

14. The quality of service provided by Cal-Am in its Coronado District is satisfactory.

Conclusions of Law

1. Revenue increases of 6.66% in 1984, 2.56% in 1985, and 1.84% in 1986 are reasonable.

2. The application should be granted to the extent set forth in the following order.

3. Because of the immediate need for additional revenues, this order is effective today.

O R D E R

IT IS ORDERED that:

1. California-American Water Company (Cal-Am) is authorized to file the revised schedules attached to this order as Appendix A and to concurrently cancel its present schedules for such service. This filing shall comply with General Order (GO) Series 96. The revised schedules shall apply only to service rendered on and after their effective date, which shall be five days after filing.

2. On or after November 15, 1984 Cal-Am is authorized to file an advice letter, with appropriate work papers, requesting the step rate increases attached to this order as Appendix B or to file a lesser increase in the event that the Coronado District rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the 12 months ending September 30, 1984, exceeds the lower of (a) the rate of return found reasonable by the Commission for Cal-Am during the corresponding period in the then most recent rate decision, or (b) 11.78%. This filing shall comply with GO Series 96 and shall include evidence for wage escalation factors actually granted. ✓
Suitable adjustments will be made to the step rate increase should it be determined that the escalation factors placed into effect are less than that set forth in the record. The requested step rates shall be reviewed by the staff and shall go into effect upon staff's determination that they conform with this order. Staff shall inform the Commission if it finds if the proposed step rates are not in accord with this decision, and the Commission may then modify the increase. The effective date of the revised schedule shall be no earlier than January 1, 1985, or 30 days after the filing of the step rate, whichever ✓
is later and shall apply only to service rendered on or after the effective date.

3. On or after November 15, 1985 Cal-Am is authorized to file an advice letter, with appropriate workpapers, requesting the attrition offset rate increases, or to file a lesser increase in the event the Coronado District rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the 12 months ending September 30, 1985, exceeds the lower of (a) the rate of return found reasonable by the Commission for Cal-Am during the corresponding period in the then most recent decision, or (b) the rate of return adopted in this proceeding. This filing shall comply with GO Series 96 and shall include evidence for wage escalation factors actually granted. Suitable adjustments will be made to the attrition rate increase should it be determined that the escalation factors placed into effect are less than that set forth in the record. The requested rates shall be reviewed by the staff and shall go into effect upon staffs determination that they conform to this order. The staff shall inform the Commission if it finds the attrition rate increase is not in accord with this decision, and the Commission may then modify the increase. The effective date of the revised schedule shall be no earlier than January 1, 1986, or 30 days after the filing of the attrition rate increase, whichever is later.

4. Cal-Am is authorized to file an advice letter offset increase upon the completion of Phase I or Phase II of the Palm Avenue Pipeline project.

5. This application is granted as set forth above.

This order is effective today.

Dated June 6, 1984, at San Francisco, California.

LEONARD M. GRIMES, JR.
President

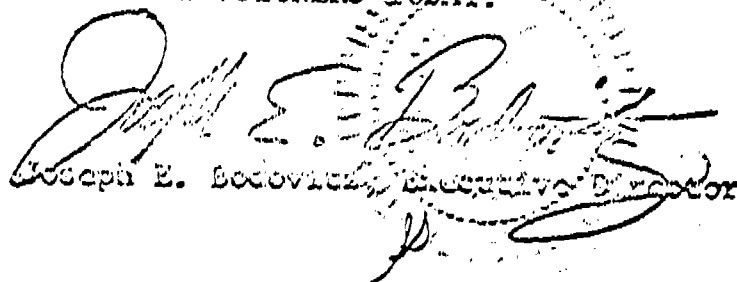
VICTOR CALVO

DONALD VIAL

WILLIAM T. BAGLEY
Commissioners

Commissioner Priscilla C. Grew,
being necessarily absent, did not
participate.

I CERTIFY THAT THIS DECISION
WAS APPROVED BY THE ABOVE
COMMISSIONERS TODAY.


Joseph E. Bodovitz, Executive Director

APPENDIX A
Page 1
California-American Water Co.

Schedule No. CO-1
Coronado District Tariff Area
General Metered Service

Applicability

Applicable to all metered water service.

Territory

Coronado, Imperial Beach, and portions of San Diego, and vicinity,
San Diego County.

Rates

Service Charge:		Per Meter Per Month	
For 5/8 x 3/4-inch meter	\$	2.65	(I)
3/4-inch meter		2.90	
1-inch meter		4.80	
1 1/2-inch meter		8.80	
2-inch meter		20.50	
3-inch meter		37.00	
4-inch meter		66.00	
6-inch meter		88.00	
8-inch meter		141.00	
Quantity Rates:			
First 300 cu. ft., per 100 cu. ft.		0.610	
Over 300 cu. ft., per 100 cu. ft.		0.845	(I)

The Service Charge is a readiness-to-serve charge which is applicable to all metered service and to which is to be added the monthly charge computed at the Quantity Rates.

APPENDIX A
Page 2
California-American Water Co.

Schedule No. CO-4
Coronado District Tariff Area
Private Fire Protection Service

Applicability

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

Territory

Coronado, Imperial Beach, and portions of San Diego, and vicinity, San Diego County, all as set forth on Service Area maps on file with the California Public Utilities Commission.

Rates

	<u>Per Month</u>	
Private Fire Protection Systems:		
For each 4-inch connection or smaller	\$ 12.80	(I)
6-inch connection	26.70	
8-inch connection	39.50	
10-inch connection	58.70	
12-inch connection	85.30	(I)

The rates for private fire service are based upon the size of the service and no additional charges will be made for fire hydrants, sprinklers, hose connections or standpipe connected to and supplied by such private fire service.

APPENDIX A
Page 3
California-American Water Co.

Schedule No. CO-4-H
Coronado District Tariff Area
Private Fire Hydrant Service

Applicability

Applicable to all water service furnished for fire hydrant service.

Territory

Coronado, Imperial Beach, and portions of San Diego, and vicinity, San Diego County, all as set forth on Service Area maps on file with the California Public Utilities Commission.

Rates

Per Month

Private Fire Hydrant Service Installed at Cost
of Applicant.

For each Fire Hydrant Installed

\$ 7.50 (I)

APPENDIX A
Page 4
California-American Water Co.

Schedule No. CO-6
Coronado District Tariff Area
Flat Rate Schedule

Applicability

This rate is available only to a subdivider building a minimum of five (5) homes within a tract approved by the County of San Diego, the cities of Coronado, Imperial Beach and a portion of San Diego, in the area served by the Coronado District.

Territory

This rate shall apply within the cities of Coronado, Imperial Beach and portion of San Diego and vicinity, San Diego County, all as set forth on Service Area maps on file with the California Public Utilities Commission.

Rates

Monthly Charge per Water Connection

\$ 10.70 (I)

APPENDIX B

Each of the following increases in rates may be put into effect on the indicated date by filing a rate schedule which adds the appropriate increase to the rate which would otherwise be in effect on that date.

Effective Dates	
<u>1-1-85</u>	<u>1-1-86</u>

SCHEDULE CO-1 General Metered Service

Service Charges:

For 5/8 x 3/4-inch meter	\$ 0.10	\$ 0.05
3/4-inch meter	0.10	0.10
1-inch meter	0.20	0.10
1 1/2-inch meter	0.30	0.20
2-inch meter	0.50	0.50
3-inch meter	1.00	1.00
4-inch meter	2.00	2.00
6-inch meter	3.00	2.00
8-inch meter	5.00	3.00
10-inch meter	5.00	3.00

Quantity Rates:

For the first 300 cu. ft., per 100 cu. ft.	0.14	0.011
For the over 300 cu. ft., per 100 cu. ft.	0.20	0.015

Schedule CO-4 Private Fire Protection Service

Rates:

For each 4-inch connection or smaller	0.30	0.20
For each 6-inch connection	0.60	0.50
For each 8-inch connection	0.90	0.70
For each 10-inch connection	1.40	1.00
For each 12-inch connection	2.10	1.50

Schedule CO-4-H Private Fire Hydrant Service

For each Fire Hydrant installed	0.20	0.10
---------------------------------------	------	------

Schedule CO-6

Monthly Charge per Water Connection	0.20	0.20
---	------	------

APPENDIX C
Page 1

ADOPTED QUANTITIES

Company: California-American Water Company
District: Coronado

	1984	1985
1.- <u>Water Production:</u> Ccf(1000)	5,116.1	5,164.8
<u>Purchased Water:</u>	5,116.1	5,164.8
Wells:	0	0
2.- <u>Purchased Water</u>		
Cost:	\$ 2,230,700	\$ 2,251,900
S/Ccf:	0.436	0.436
(City of San Diego)		
(Jan. 1, 1984 Rate)		
3.- <u>Purchased Power</u>		
Cost:	\$ 100	\$ 100
4.- <u>Ad Valorem Taxes:</u>	\$ 57,700	\$ 60,100
Tax Rate:	0.8156%	0.8136%

APPENDIX C
Page 2

ADOPTED QUANTITIES

5. <u>Number of Services-Meter Size:</u>	<u>1984</u>	<u>1985</u>
5/8 x 3/4	14,522	14,709
3/4	0	0
1	1,856	1,880
1 1/2	349	353
2	322	326
3	15	16
4	66	67
6	19	19
8	9	9
Total	<u>17,158</u>	<u>17,379</u>

6. <u>Metered Water Sales:</u>	<u>1984</u>	<u>1985</u>
<u>Range-Ccf</u>	<u>Usage-Ccf</u>	
0 - 3	586,000	593,300
Over 3	<u>4,338,200</u>	<u>4,377,800</u>
Total Usage	<u>4,924,200</u>	<u>4,971,100</u>

7. <u>Number of Services:</u>	<u>No. of Services</u>		<u>Usage-KCcf</u>		<u>Avg. Usage-Ccf/yr.</u>	
	<u>1984</u>	<u>1985</u>	<u>1984</u>	<u>1985</u>	<u>1984</u>	<u>1985</u>
Residential	15,571	15,773	2,728.0	2,763.4	175.2	175.2
Business-Nor.	1,331	1,350	806.1	817.6	605.6	605.6
Business-Large	59	59	735.9	735.9	12,473	12,473
Public Auth.-Nor.	142	142	156.2	156.2	1,100.2	1,100.2
Public Auth.-Large	21	21	325.0	325.0	15,476	15,476
Golf	18	18	159.5	159.5	—	—
Other	16	16	13.5	13.5	—	—
Subtotal	<u>17,158</u>	<u>17,379</u>	<u>4,924.2</u>	<u>4,971.1</u>		
Private Fire Prot.	<u>99</u>	<u>107</u>				
Total	<u>17,257</u>	<u>17,486</u>				
Water Loss: 3.75%			<u>191.9</u>	<u>193.7</u>		
Total Water Produced			<u>5,116.1</u>	<u>5,164.8</u>		

Income Tax Calculation

	<u>1984</u>	1985 (Thousands of Dollars)
Operating Revenue	4826.5	4999.7
Expenses		
Payroll	561.5	614.6
Purchased Power	0.1	0.1
Purchased Water	2230.7	2251.0
Other O & M	221.5	231.5
Other A & G	282.9	308.8
Gen. Office Prorated	206.4	222.3
Uncollectible \$ @ 0.406%	19.6	20.3
Payroll Taxes	42.4	45.9
Ad Valorem Taxes @ 0.8156%	57.7	60.1
Capitalized Overhead	26.9	30.0
A.F.U.D.C.	13.8	1.0
Interest	265.3	314.8
Debt Expense	<u>1.4</u>	<u>1.4</u>
Total Deduction	3930.2	4101.8
State Tax Depreciation	249.7	260.7
Net Taxable Income	646.6	637.2
State Corp. Franch. Tax 9.6%	62.1	61.1
Federal Tax Depreciation	253.4	258.6
State Income Tax	62.1	61.1
Net Taxable Income	580.8	578.1
Fed. Income Tax 46%	267.2	265.9
Less Grad. Tax Adj.	2.5	2.5
Less ITC	<u>5.1</u>	<u>5.9</u>
Total Federal Income Tax	259.6	257.5

APPENDIX D
California-American Water Co.
Coronado District

Comparisons of typical bills for residential metered customers of various usage level and average level at present and authorized rates for the year 1984.

General Metered Service
(5/8 x 3/4-inch meters)

:	Monthly Usage	At Present Rates	At Authorized Rates	Percent Increase	:
:					:
<hr/>					
	(Cubic Feet)				
	300	\$ 3.70	\$ 4.48	21.11%	
	500	5.35	6.17	15.26	
	1,000	9.49	10.40	9.56	
	1,460 (Average)	13.29	14.28	7.45	
	2,000	17.76	18.85	6.12	
	3,000	26.03	27.30	4.87	
	5,000	42.57	44.19	3.82	
	10,000	83.92	86.44	3.01	

(END OF APPENDIX D)

The staff in its estimates disallowed the following charges in Account 795:

Orientation slide show	\$ 850
Newsletter	765
Safety Banquet	200
Physical exams	<u>385</u>
Total	2,200

Staff argues these costs confer no benefit on ratepayers and should not be allowed for ratemaking purposes. Cal-Am states these safety program expenses are justified in that overall expenses are reduced when temporary employees are not required and that it keeps workman's compensation insurance rates at their lowest possible level. While there is undoubtedly some benefit to the ratepayers, we believe they are only indirectly benefitted as contrasted to the direct benefit to the shareholders. Under these circumstances we will adopt the staff estimates as reasonable.

With respect to the CWA dues issue, during the hearing Cal-Am witness Barker introduced Exhibit 8 requesting a portion of the annual dues paid to CWA be allocated to the Coronado District. The exhibit and testimony were received into evidence over the staff's objection. On March 1, 1981 the staff renewed its motion to strike and exclude Exhibit 8 and related testimony.

The staff states that because this item was not included in the application when it was filed it should not be considered. Staff argues that it violates due process of the ratepayers as embodied in the United States Constitution, § 454 of the Public Utilities Code, the Commission's Rules of Practice and Procedure and the Commission's Regulatory Lag Program.

6. Cal-Am's estimate for regulatory expense amortized over three years is reasonable.

7. Cal-Am did not show that Account 795 expenses that staff would disallow would confer a direct benefit on the ratepayer.

8. The California Water Association dues were properly considered and allowed as an expense item without violating due process, Public Utilities Code § 454 or the Rules of Practice and Procedure.

9. The authorized increase in rates at the rate of return for test year 1984 is expected to provide increased revenues for Cal-Am's Coronado District of approximately \$301,300 as compared to a requested increase of \$639,800 over present rates.

10. The authorized increase in rates at the 11.99% rate of return for test year 1985 is expected to provide increased revenues for Cal-Am's Coronado District of approximately \$124,600 over the authorized 1984 rates as compared to a requested increase of \$269,400.

11. An allowance of 0.77% in rate of return to compensate for operational test year 1986 is reasonable. Allowing for this operational attrition and a financial attrition of 0.09% in determining the authorized increase in rates at the 12.08% rate of return for test year 1986 is expected to provide increased revenues for Cal-Am's Coronado District of approximately \$92,200 (1.84%) over the authorized 1985 rates as compared to a requested increase of \$261,300 (5.50%) over Cal-Am's authorized 1985 rates.

12. The adopted estimates previously discussed here of operating revenues, operating expenses and rate base for the test years 1984 and 1985 reasonably indicate the result of Cal-Ams operations in its Coronado District in the near future.

13. Adoption of the staff recommended rate design is reasonable.

14. The quality of service provided by Cal-Am in its Coronado District is satisfactory.

Conclusions of Law

1. Revenue increases of 6.66% in 1984, 2.56% in 1985, and 1.84% in 1986 are reasonable.

II. Rate of Return

As it did in its Monterey District rate application filed in February 1982 and continuing with its Los Angeles area rate applications filed in December 1982, Cal-Am requests rates that will produce a return on common equity of 16%. Cal-Am witness Barker testified that the 16% return on equity request is needed because (1) common equity capital is more risky than debt capital (bonds), (2) investors require higher returns on common stock than on bonds to compensate for the higher risk, (3) a common stock investor expects steady dividends that keep up with the rate of inflation and (4) an investor expects an increase in the book value of his original investment through the reinvestment of retained earnings. He also stated that using U.S. Treasury Bonds as a base, the risk premium associated with water utility stock over 10 years and long-term U.S. Treasury Bonds average 440 to 500 basis points above bond interest rates.

Staff witness Mowrey recommended a return on common equity of 14.50%. He stated that rate of return is an expression of a utility's capital costs-debt and equity. The rate of return recommendation results from an estimation of those costs applied to a projected capital structure determined for these proceedings. The cost of debt is contractual and therefore easily determined, although cost assumptions must be made regarding future financing over the test period. He stated the cost of common equity is considerably more difficult to determine and therefore is often the area of greatest differences of opinion. The recommended return on common equity was determined after an analysis of the risk, both business and financial, associated with Cal-Am.

For nonlabor Cal-Am adopted staff incremental increases for 1985 and 1986 of 1.2% and .4% but used 6.4%\$ as a starting point rather than the staffs 4.5%. The 6.4% figure used by Cal-Am was the CPI for San Diego, November 1982-November 1983. A comparison of the nonlabor escalation factor is as follows:

<u>Nonlabor Escalation</u>	
<u>Cal-Am</u>	<u>Staff</u>
<u>Percent Increase</u>	<u>Percent Increase</u>
1984 6.4	4.5
1985 7.6	5.7
1986 8.0	6.1

It is Cal-Am's position that the prevailing wages paid its employees is considerably lower than wages paid by other employers in the San Diego area for comparable skills. Cal-Am is in what its witness Foy described as a "catch-up mode" with its employee wages in attempting to bring these wages into line with other employee wages paid throughout the San Diego area.

Staff's labor escalation rates would appear reasonable, assuming that Cal-Am's employees are presently receiving wages comparable to that received by other employees in the other Cal-Am districts. However, staff overlooks Cal-Am's attempt to bring its Coronado district employee wages up to the prevailing other Cal-Am district pay rates, which would ensure better employee moral and low employee turnover thereby benefitting both the company and its ratepayers.

The record fully supports Cal-Am's position that increases to employees in excess of the staff's recommended increases are justified in light of the discrepancies in the present wage levels of Cal-Am employees as compared to the other Cal-Am districts in general. We place Cal-Am on notice, however, that the rate levels authorized here

2. The application should be granted to the extent set forth in the following order.

O R D E R

IT IS ORDERED that:

1. California-American Water Company (Cal-Am) is authorized to file the revised schedules attached to this order as Appendix A and to concurrently cancel its present schedules for such service. This filing shall comply with General Order (GO) Series 96. The revised schedules shall apply only to service rendered on and after their effective date, which shall be five days after filing.

2. On or after November 15, 1984 Cal-Am is authorized to file an advice letter, with appropriate work papers, requesting the step rate increases attached to this order as Appendix B or to file a lesser increase in the event that the Coronado District rate of return on rate base, adjusted to reflect the rates then in effect and normal ratemaking adjustments for the 12 months ending September 30, 1984, exceeds the lower of (a) the rate of return found reasonable by the Commission for Cal-Am during the corresponding period in the then most recent rate decision, or (b) 14.50%. This filing shall comply with GO Series 96 and shall include evidence for wage escalation factors actually granted. Suitable adjustments will be made to the step rate increase should it be determined that the escalation factors placed into effect are less than that set forth in the record. The requested step rates shall be reviewed by the staff and shall go into effect upon staff's determination that they conform with this order. Staff shall inform the Commission if it finds if the proposed step rates are not in accord with this decision, and the Commission may then modify the increase. The effective date of the revised schedule shall be no earlier than January 1, 1985, or 30 days after the filing of the step rate, whichever is later and shall apply only to service rendered on or after the effective date.

4. Cal-Am is authorized to file an advice letter offset increase upon the completion of Phase I or Phase II of the Palm Avenue Pipeline project.

This order becomes effective 30 days from today.

Dated JUN 6 1984, at San Francisco, California.

LEONARD M. GRIMES, JR.
President
VICTOR CALVO
DONALD VIAL
WILLIAM T. BACLEY
Commissioners

Commissioner Priscilla C. Grow,
being necessarily absent, did
not participate