

Decision 84 11 089 NOV 21 1984**ORIGINAL**

## BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Hillview Water Co.,	)	
Inc., Oakhurst, California, for an	)	
Emergency Adjustment of Rates or Rate	)	
Structure, in order to increase	)	
revenues collected by approximately	)	Application 84-04-023
24% to the \$182,651.00 authorized by	)	(Filed April 4, 1984;
Decision No. 82-08-083, dated	)	amended April 19, 1984)
August 18, 1982. No increase in	)	
<u>Authorized Revenue or Authorized Rate</u>	)	
<u>of Return is being requested.</u>	)	

John D. Reader and Roger Forrester, for  
Hillview Water Company, applicant.  
Evelyn Lee, Attorney at Law, and Richard Tom,  
for the Commission staff.

O P I N I O NProcedural History

By Application (A.) 84-04-023 filed April 4, 1984, Hillview Water Company, Inc. (Hillview), is seeking authority to increase its rates by approximately 24%. On April 19, 1984, Hillview amended its application to include a request that the utility be authorized to consolidate its four rate areas into one with a uniform meter rate schedule.

Hillview, in A.84-04-023, asked the Commission to authorize the requested increase at the earliest possible time. After learning that the Hydraulic Branch (Branch) of the Commission staff was recommending that an evidentiary hearing be held to evaluate Hillview's request, the utility filed, on May 29, 1984, a petition requesting that the Commission grant, ex parte, emergency interim relief.

Responding to Hillview's petition, the Branch, on June 18, 1984 issued a report. The Commission, after review of Hillview's

pleadings and the Branch report, declared on July 5, 1984, by Decision (D.) 84-07-013, that the Commission was not convinced that a need for emergency interim relief had been sufficiently documented and denied Hillview's petition, pending an early hearing.

An evidentiary hearing was held before an administrative law judge (ALJ) on July 19, 1984 and the matter was submitted upon receipt of the transcript on August 10, 1984. Hillview and the staff attorney representing the Branch each filed a concurrent brief.

Hillview mailed notices of its proposed increases in rates to each customer in its four serving areas on April 26, 1984, and a public notice was published in the Sierra Star, an Oakhurst newspaper, on June 7. The rates contained in the notices were from the consolidated rate schedule requested by the amendment to A.84-04-023.

The Commission received 51 individual letters opposing the increase, of which 42 were from the utility's Indian Lakes Estates system, eight from the Oakhurst systems, and one from Raymond. Many of the letters, particularly those emanating from Indian Lakes, complained about water quality as well as about increased rates. There were two letters supporting the Hillview request, one from a local real estate developer in the Hillview service area who was concerned about Hillview's ability to continue to render service, and one from Hillview's insurance agent.

#### Hillview's Request

In A.84-04-023, Hillview stated that the decision in its last general rate case, D.82-08-083, authorized the utility to increase its rates to a level which the Commission staff projected would produce \$182,651 in operating revenue from the 1982 count of 528 customers. Instead, 1983 water revenue was only \$150,004 and year-end metered customers numbered 612. Further, the \$150,004

figure included the 1.5% Public Utility Commission Reimbursement Fee (PUCRF) established by newly enacted Public Utilities (PU) Code §§ 401-415 (which sections became effective January 1, 1983). Realized revenues were thus approximately \$35,000 less than Hillview had been authorized. Hillview also claimed that it suffered a financial loss of \$19,403 in 1983 and similar losses would occur in 1984, absent rate relief.

In the amendment to the application, Hillview referred to the Commission staff report in the last rate case, which report, Hillview claimed, implied that consolidation of its rate areas is inevitable. According to Hillview, this is an opportune time to accomplish consolidation. It would be more effective and efficient, Hillview urged, to deal with one set of books, instead of four, and every aspect of accounting and billing would be more efficient with one rate schedule. Also, according to the utility, customer relations would be better served with one uniform rate schedule rather than four different schedules. Further, Hillview said, it operates as one company and one service area and, therefore, believes it appropriate to have but one rate schedule.

#### Description of Applicant

Hillview operates seven separate water systems in the foothills of Madera County. Four are clustered about the community of Oakhurst and two are located about 11 miles south of Oakhurst at Coarsegold Highlands and Indian Lakes Estates. A seventh system serves the Madera County community of Raymond, which is located about 23 miles by road southwest of Oakhurst. At the end of 1983 the seven systems together served a total of 612 metered customers. As of December 31, 1983, water plant in service amounted to \$1,544,401 and accumulated depreciation of water utility plant was \$307,082.

#### Present and Proposed Rate Schedules

As if Hillview's rate structure were not already complex enough, billing its 612 metered customers under four basic rate schedules, the rate structure is further complicated by the fact that

portions of the water systems in two of the rate areas were financed to varying extent by a Safe Drinking Water Bond Act (SDWBA) loan from the state's Department of Water Resources. According to established Commission policy, this loan is being serviced by means of separately identified surcharges to customers. The amounts of the surcharges are determined by allocating the SDWBA loan costs to customers in proportion to the share of funds from the loan expended in their immediate serving areas. The costs thus apportioned are further allocated to customers within the benefitting area based on meter size, but since 95% of Hillview's customers are served through 3/4-inch meters, this refinement is not of great relative significance.

Hillview's present rates, for service through a 3/4-inch meter, are:

Royal Oaks-Sunnydale, Goldside-Hillview,  
and Sierra Lake Tariff Areas (Oakhurst Systems):

Quantity Rates:

First 300 cu. ft. - \$0.87 per 100 cu. ft.  
Over 300 cu. ft. - \$1.16 per 100 cu. ft.

Service Charge: \$8.50 per month

SDWBA Surcharge:

Royal Oaks-Sunnydale - \$8.80 per month  
Goldside-Hillview - \$3.00 per month  
Sierra Lakes - \$0.85 per month

Coarsegold Highlands Tariff Area:

Quantity Rates:

First 300 cu. ft. - \$1.53 per 100 cu. ft.  
Over 300 cu. ft. - \$2.03 per 100 cu. ft.

Service Charge: \$12.90 per month

Indian Lakes Tariff Area:

Quantity Rates:

First 300 cu. ft. - \$0.79 per 100 cu. ft.

Over 300 cu. ft. - \$1.06 per 100 cu. ft.

Service Charge: \$6.50 per month

Raymond Tariff Area:

Quantity Rates:

First 300 cu. ft. - \$1.97 per 100 cu. ft.

Over 300 cu. ft. - \$2.62 per 100 cu. ft.

Service Charge: \$10.00 per month

SDWBA Surcharge: \$6.15 per month

The total monthly water bill, at present rates, for a customer in each of the rate areas using a minimal 600 cu. ft. per month (or 150 gallons per day) in each of the tariff areas, including the 1.5% PUCRF is:

<u>Tariff Area</u>	<u>Quantity Charge</u>	<u>Service Charge</u>	<u>SDWBA Charge</u>	<u>PUCRF Charge</u>	<u>Total Charge</u>
Royal Oaks - Sunnydale,	\$6.09	\$8.50	\$8.80	\$0.22	\$23.61
Goldside - Hillview,	6.09	8.50	3.00	0.22	17.81
Sierra Lakes	6.09	8.50	0.85	0.22	15.66
Coarsegold Highlands	10.68	12.90	-	0.35	23.93
Indian Lakes	5.55	6.50	-	0.18	12.23
Raymond	13.77	10.00	6.15	0.36	30.28

Data furnished by Hillview's consulting engineer showed average water use for the month of August 1983 to be 2,390 cu. ft. per customer. The total charges for this average quantity would run from \$36.73 in Sierra Lakes to \$77.88 in Raymond.

The uniform rate for a 3/4-inch meter that Hillview proposes for all of its districts is:

Quantity Rates:

First 300 cu. ft. - \$1.05 per 100 cu. ft.

Over 300 cu. ft. - \$1.31 per 100 cu. ft.

Service Charge - \$12.00

SDWBA Surcharge (no change proposed)

Royal Oaks-Sunnydale - \$8.80 per month

Goldside-Hillview - \$3.00

Sierra Lakes - \$0.85

Indian Lakes - -

Raymond - \$6.15

Evidentiary Hearing

At the evidentiary hearing testimony was received from a registered civil engineer retained by Hillview, from Hillview's president, and from a senior utilities engineer of the Branch. The staff engineer is also a registered civil engineer.

Because the first affirmative evidence received in this proceeding was the staff report, rather than the applicant's showing, the proceeding developed in a sequence unconventional when compared with the usual Commission rate case. Because the utility's direct testimony was in part in the nature of comment on and rebuttal to the staff report, this decision will follow the sequence in which the record was addressed.

Staff Report

The Hydraulic Branch, in defining the scope of its June 18 report, stated that since Hillview was not requesting general rate relief, the Branch confined its investigation to the alleged revenue shortfall and to whether that shortfall is creating an emergency cash flow situation. The Branch did not, in the report, investigate the

other items involved in the ratemaking process, such as expenses, depreciation, and rate base, as such an investigation would constitute a study appropriate for a general rate increase proceeding, a type of proceeding that Hillview was not requesting. Rather the Branch, in its analysis, used the expenses, depreciation, and rate base adopted in D.82-08-083 as being items not in contention.

The Branch did not disagree with Hillview's claim of reduced consumption but the Branch noted discrepancies in various revenue data submitted by Hillview. In A.84-04-023, Hillview claimed 1983 metered revenue of \$150,004 but, using the water use tables attached to the application, the staff calculated revenue of \$230,641. Hillview, at the Branch's request, then submitted revised water use tables which, when Hillview's rate schedules were applied, supported a revenue estimate of \$147,819. When increased by 1.5% for the PUCRF, this estimate was substantially identical to the \$150,004 claimed by Hillview. The revenue situation is further confused by Hillview's having reported, in its Annual Report to the Commission for the Year Ended December 31, 1983, metered water revenues of \$164,204.

The Branch stated, in the report, that it believed that some reduction in consumption has taken place, causing revenues to decline. There are two factors which could have caused a reduction in consumption. The first factor is that 1983 was a year of abnormally heavy rainfall. (The revenue level adopted in D.82-08-083 was based on experienced 1981 rainfall, which was a dry year, rather than a normalized level of rainfall.) The total rainfall for the nearest weather station (North Fork Ranger Station) in 1983 was 30 inches above the normal. The second factor is the relatively large increase in rates in 1982. The increases authorized in 1982 totaled over 70%. Experience by the Branch indicates that whenever a large increase in rates has been applied the consumption decreases. This repression is generally temporary, the Branch believes, and consumption usually recovers and continues at or near the same rate

as before the increase. In Hillview's case, however, the Branch does not preclude the possibility that the revenue repression may be permanent. ✓

The Branch noted that it is present Commission practice to determine a water utility's revenue requirement on a normal year of operation that is intended to be reflective of the conditions under which the utility will operate under during the future period for which rates are set. Normally the revenues, expenses, and investment tend to track each other, and recorded rates of return approach these authorized. After about 12 months, revenues at rates last authorized start to fall short, resulting in a diminution of rate of return. Currently, the Branch observed, the Commission has offset procedures which protect a water utility against increases in major, nondiscretionary expense items such as purchased power and water. The Branch believes these procedures provide adequate rate relief between general rate filings. The Commission has not authorized a revenue adjustment procedure or mechanism that guarantees against shortfalls in revenue for water utilities, and it is the Branch's contention that revenue adjustment mechanisms act as disincentives for prudent management. The Branch recommends that the Commission, in the event that it should grant emergency relief, make it absolutely clear that its action is not to be taken as an endorsement of revenue adjustment mechanisms for water utilities.

Although the staff did not investigate the reasonableness of Hillview's expenses, it compiled the following comparison of 1983 expenses as reported by Hillview in its Annual Report to the Commission (the expenses claimed in A.84-04-023), and the 1982 expense levels adopted by the Commission in D.82-08-083:



<u>Expenses</u>	<u>1983 per Application</u>	<u>1982 Adopted</u>	<u>Applicant Exceeds 1982 Adopted</u>
Source of Supply	\$ -	\$ -	\$ (2,100)
Purchased Water	1,275	-	1,275
Purchased Power	26,766	27,970	(1,204)
O&M Labor	25,892	22,200	3,692
O&M Materials	3,370	4,600	(1,230)
O&M Contract	2,620	6,765	(4,145)
Office Salaries	15,319	12,000	3,319
Management Salaries	18,319	12,000	6,319
Office Supplies	11,596	8,468	3,128
Insurance	12,270	5,750	6,520
Accounting, Legal	2,577	2,590	(13)
General	830	600	230
Vehicle	19,802	10,746	9,056
Office & Stor.	3,926	3,660	266
Subtotal	144,563	119,449	25,114
Depreciation	18,543	12,840	5,703
Taxes			
Property	3,761	1,380	2,381
Payroll	105	-	105
Other	245	4,665	(4,420)
Calif. Corp. Franc. Tax	5	-	5
Federal Income Tax	0	11,613	(11,613)
Subtotal	4,116	17,658	(13,542)
Total	\$167,222	\$149,947	\$ 17,275

Noting that much of the increase in expenses consists of salaries and other discretionary areas, the staff, for its 1983 realized rate of return determination, adjusted the Commission adopted 1982 expenses of \$149,947 to eliminate the \$11,613 Federal income tax since Hillview had declared that 1983 income taxes were zero. Using the \$138,334 thus determined, and the D.82-08-083 adopted rate base of \$278,330, the staff determined its realized rate of return for Hillview of 3.4%.

The Branch, in its report, conceded that its determination may not truly reflect Hillview's current situation. The 3.4% return

represents the best case, assuming revenues are correct. To the extent that expenses and rate base have escalated, the 3.4% return figure would be reduced.

As to Hillview's request for consolidation of districts, the Branch observed that one rate schedule for all of Hillview's districts would mean an approximately 35% increase for the Indian Lakes District, a 20% decrease for Coarsegold and Raymond, and a restructuring of the tariffs. The Branch believes that this proposal would be better handled in a general rate case.

At the end of its report the Branch reached the following conclusions:

"Conclusion

The Branch concludes the following:

- (1) Consumption is down due to the large rate increases in 1982 and the heavy rainfall in 1983.
- (2) The accuracy of Hillview's submitted revenue is suspect.
- (3) There is a possibility that the repression in revenues is permanent.
- (4) Based on Hillview's submitted 1983 revenues and 1982 adopted expenses and rate base, it is not losing money but is earning 3.4% on rate base. This is significantly lower than the 11.75% last authorized for Hillview.
- (5) Hillview's expenses as submitted for 1983 are higher than adopted and a real emergency cash flow problem may exist. However, the scope of this proceeding will not allow a detailed investigation into the reasonableness of Hillview's expenses; this should be done in a general rate proceeding."

and recommended:

"Recommendations

"The Branch recommends that should the Commission decide to grant rate relief, it make absolutely clear that its action is not to be taken as an

endorsement of revenue adjustment mechanisms for water utilities. Because there is still some question about the revenue figures submitted by Hillview, the Branch recommends that any relief granted be subject to refund pending an audit of Hillview's revenue accounting books and procedures for 1983. Given staffing limitations, the Branch recommends that an independent Certified Public Accountant (CPA) be retained to perform this audit at Hillview's expense. This CPA, by an affidavit and within 30 days, would inform the Commission of its findings and conclusions about the accuracy of Hillview's submitted revenue. The cost of this audit should be addressed in Hillview's next general rate case. If the audit is not provided as required above, then the authorization for rate relief should be rescinded subsequently."

Showing by Hillview's Consultant

Immediately upon receipt of the Branch report, Hillview's consultant (Consultant) prepared a letter to the Commission, dated June 19, 1984, by which he professed to reconcile metered water revenue figure of \$164,204 shown in the 1983 Annual Report with the \$150,004 claimed in A.84-04-023. Subsequently, on July 6, 1984, the Consultant distributed prepared testimony for the hearing scheduled for July 19. At the hearing both the letter and the prepared testimony were received into evidence and supported by the Consultant's oral testimony.<sup>1</sup>

The Consultant testified that there were several explanations for the revenue discrepancies that bothered the staff. The annual report revenues were the amounts of billed revenues, and included some uncollectible revenue and also PUCRF. In addition, because of an error in entering billing data into the utility's computer, revenues reported in the annual report were overstated.

---

<sup>1</sup> Prior to his recent retirement and establishment of an engineering practice, the Consultant had been the Commission's Chief Hydraulic Engineer and Branch Chief.

The Consultant prepared the following table to correct for these inadvertent errors.

Revenue reported in 1983 A.R.	\$164,707
Computer input error*	(9,396)
PUCRF	(2,752)
Uncollectibles for last quarter	<u>(326)</u>
Adjusted A.R. revenue	152,233

\*\$1,044.55 was entered as \$10,440.55, thus introducing a \$9,396.00 error.

Having adjusted the annual report for these errors, the Consultant then proceeded to reconcile the reported revenues as billed with the revenues as actually collected in 1983, which collected revenues were used in the application. This reconciliation follows:

Revenue Billed and Revenue Collected in 1983

	<u>Revenue Billed</u>	<u>Revenue Collected</u>	<u>Difference</u>
Metered Revenue			
Oakhurst Systems	\$ 90,709	\$ 88,125	\$2,584
Raymond	15,383	15,051	332
Coarsegold Highlands	6,787	6,666	121
Indian Lakes	41,603	40,162	1,441
Total Metered	<u>154,482</u>	<u>150,004</u>	<u>4,478</u>
Flat Rate Revenue	<u>503</u>	<u>503</u>	<u>-</u>
Total Revenue	\$154,985	\$150,507	\$4,478
PUCRF	<u>(2,752)</u>	<u>(2,687)</u>	<u>65</u>
Total Rev. Excluding PUCRF	\$152,233	\$147,820	\$4,413

The Consultant calculated the 1983 average annual billing per customer for Hillview's combined system as being \$259.34 per

customer per year, compared to the \$345.93 contemplated by D.82-08-083. To illustrate the drop in consumption between 1981 and 1983 he prepared the following table:

<u>Service Area</u>	<u>Average Monthly Water Use Ccf</u>		<u>1983 Decrease in Water Use</u>
	1981	1983	
Oakhurst Systems	19.5	10.6	45.6%
Coarsegold Highlands	14.4	7.8	45.8%
Indian Lakes	14.4	13.1	9.0%
Raymond	9.2	6.5	29.3%
Combined Utility	17.0	11.0	35.3%

Consumption estimates upon which D.82-08-083 revenues were estimated were taken from recorded 1981 results. The calendar year 1981 was drier than usual and, therefore, more water was used for landscape irrigation. To illustrate this effect, he obtained the following rainfall data taken from the Forest Service station at Batterson, which station is located just north and at a slightly higher elevation than Hillview's Oakhurst service area:

<u>Calendar Year</u>	<u>Rainfall - Inches Spring, Summer, &amp; Fall</u>	<u>Total Year</u>
1981	10.20	30.54
1982	27.87	64.37
1983	29.00	48.26

The ranger at this station advised the Consultant that normal rainfall at Batterson is 37 inches and that rainfall at Oakhurst would be slightly less. The Consultant presented the rainfall data for combined spring, summer, and fall separate from total year since the level of precipitation in those months determines water use. The Consultant also determined that 1981 temperatures were higher than 1983, further contributing to high 1981 water usage. The 1983 temperatures he considered as constituting a normal year.

From his studies of customer usage, rainfall, and temperature, the Consultant concluded that 1981 was an above average water use year and that future revenue estimates should be based on 1983 water use.

Using 1983 water use tables, and Hillview's requested rates, the Consultant calculated total utility revenue of \$189,200. The Consultant testified that applying the 1983 average number of customers of 585 to the 1981 average revenue per customer developed from D.82-08-083 would have produced \$202,870. The magnitude of the proposed increase for each Hillview's service areas (net of the SDWBA surcharges and the PUCRF) for average water use would be:

<u>Service Area</u>	<u>Average Water Use Ccf</u>	<u>Average Bill</u>		<u>Increase</u>	
		<u>Present Rates</u>	<u>Proposed Rates</u>	<u>\$</u>	<u>%</u>
Oakhurst Systems	10.6	\$19.93	\$25.11	\$5.18	26.0%
Coarsegold Highlands	7.8	27.23	21.44	(5.79)	(21.3)
Indian Lakes	13.1	19.58	28.38	8.80	44.9
Raymond	6.5	25.08	19.74	(5.34)	(21.3)

It can be seen that Indian Lakes would experience a sizeable increase under Hillview's proposal and Raymond and Coarsegold Highlands would experience decreases.

The Consultant explained the \$12.00 service charge requested for the 3/4-inch meters is necessary to reduce the wide fluctuation of revenue between summer and winter months. To illustrate the revenue fluctuation he plotted revenue and expense on a graph which demonstrated that in 1983 billed revenues were less than monthly expense for eight months of the year and revenues were below expenses by as much as \$3,000 in the months of January and March. He also plotted the effect of a 24% increase for all district rates, and showed that the monthly expenses would still exceed revenues for five months.

As explanation for the increase in 1983 expenses, as stated on the application, over those adopted in D.82-08-083, the consultant included the table below. The first column was intended to allow for the 12.5% increase in customers and the second to allow for a general 10% increase in price level.

	Adopted Expenses <u>D.82-08-083</u>	Adopted Expenses <u>Increased 12.5%</u>	With 10% Inflation and Expenses <u>Increased 12.5%</u>
Recorded 1983 Revenue		\$152,233	\$152,233
Expenses			
Purchased Power	\$ 27,970	31,466	31,466
O&M Labor	22,200	24,975	24,975
Office & Mgt. Payroll	24,000	27,000	27,000
Other O&M Exp.	45,279	50,939	56,033
Depreciation	12,840	14,445	14,445
Property Taxes	1,380	1,553	1,708
Other none Income Taxes	<u>4,665</u>	<u>5,248</u>	<u>5,773</u>
Subtotal	138,334	155,626	161,410
Income Taxes	<u>11,613</u>	-	-
Total Expenses	\$149,947	\$155,626	\$161,410
Net Revenue (Loss)		(\$3,393)	(\$9,177)

Alternate Rate Proposal by  
Hillview's Consultant

At the conclusion of his direct testimony, the Consultant presented an alternate rate proposal that would produce the same amount of revenue as would the consolidated rate. According to this proposal, all of the rate areas except Indian Lakes would be combined into one rate area, and Indian Lakes would have its own separate schedule. Because Indian Lakes has the largest consumption it would, under Hillview's original proposal, have the biggest increase in average bill. As shown earlier, the impact of one consolidated schedule in Indian Lakes would be an increase of 44.9%. In order to

mitigate this increase, the consultant developed his two-rate area proposal. The proposed rates for a 3/4-inch meter, not including the SDWBA surcharge and 1.5% PUCRF, are

	<u>Oakhurst Systems, Coarsegold Highlands, Raymond</u>	<u>Indian Lakes</u>
Quantity Rates:		
First 300 cu. ft.	\$1.15 per 100 cu. ft.	\$1.00 per 100 cu. ft.
Over 300 cu. ft.	\$1.48 per 100 cu. ft.	\$1.18 per 100 cu. ft.
Service Charge	\$12.00 per month	\$9.50 per month

The magnitude of the consultant's proposed increase for each of the Hillview systems, for average water use would be:

<u>Service Area</u>	<u>Average Water Use Ccf</u>	<u>Average Bill</u>		<u>Increase</u>	
		<u>Present Rates</u>	<u>Proposed Rates</u>	<u>\$</u>	<u>%</u>
Oakhurst Systems	10.6	\$19.93	\$26.70	\$6.77	33.97%
Coarsegold Highlands	7.8	27.23	22.55	(4.68)	(17.19)
Indian Lakes	13.1	19.58	24.42	4.84	24.72
Raymond	6.5	25.08	20.63	(4.45)	(17.74)

Testimony of Hillview's President

From time to time, as the utility's Consultant testified, Hillview's President (President) supplied information for the record from the counsel table. At the conclusion of the Consultant's testimony, the President was called as a witness for Hillview and at that time adopted his previous remarks as being under oath.

Before being sworn, the President explained that he had made the \$9,396 error in posting revenues that caused, in part, the erroneous revenue figure in the annual report. Also, he responded to a question by staff counsel by saying that the utility owed the United States Internal Revenue Service (IRS) approximately \$7,000 for



income and social security taxes withheld from employees' wages but not paid over to the IRS. In addition, the utility was at present not making its regular monthly payments of employees' withholding tax.

After taking the witness stand, the President testified that Hillview owed its insurance broker approximately \$10,000 for insurance (including workers' compensation) and had not been able to pay the County of Madera for its property taxes. There were also other smaller accounts payable. In response to a question by staff counsel he agreed that Hillview had increased salaries in 1982 and 1983 to meet increases in living costs. Because of lowered power costs, however, the utility had not sought a wage and energy offset from the Commission.

The ALJ queried the President as to alleged revenue shortfall. From this exchange it was developed that Hillview was including the SDWBA surcharges as revenue and interest on the SDWBA as interest expense. The President indicated that both he and his accountant disagreed with this practice but they were following what they believed to be the requirements of this Commission's Uniform System of Accounts for Water Utilities.

Reminded by the ALJ about customer complaints about dirty water in the Indian Lakes service area, the President explained that the "dirty water" was caused by a high concentration of manganese. Any surge will knock manganese deposits loose from the pipe walls and impart a purplish cast to the water. The State Department of Health Services (Health Services) has twice met with Indian Lakes customers, once in 1980 and again in 1983, to persuade them to initiate a SDWBA project, but without success. The high concentration of manganese is aesthetically unappealing and it stains fixtures but it does not constitute a health hazard and Health Services has informed Indian Lakes residents that, if they do not wish to finance system improvements by means of a SDWBA loan, they should not contact that agency further about water quality.

Upon receipt of customer complaints about "dirty water," the President testified, the utility sends a serviceperson down to Indian Wells from Oakhurst. The serviceperson then flushes the offending mains by means of bleeding hydrants. Should the complaints emanate from one or two residences, the house lines are flushed and the occupants given credit for water used.

Testimony of Staff Engineer

Although the staff report was the first piece of formal evidence to come before the Commission in this proceeding, the staff witness was the last to testify. The staff witness had also prepared the staff report in Hillview's previous rate case, A.61148.

The Engineer explained that it was not the policy of the Commission to grant emergency adjustments for rates. In the context of a general rate case an emergency interim adjustment is sometimes granted, but those interim increases are subject to refund at the conclusion of the proceeding. He also recounted how the Branch had reviewed Hillview's draft application and informed Hillview's President of the deficiencies that the Branch had found. The most important deficiency was the water use table<sup>2</sup> which the staff believed to be incorrect.

The water use table submitted with the filed application was a different table that had been redone to conform to the staff's suggestions. It was using this application water use table and Hillview's presently effective rate structure that the staff witness calculated, as described in the staff report, revenues in the order of \$230,000, as compared to the Hillview claim of \$147,819, net of

---

<sup>2</sup> A water use table is a compilation of the number of customers in each 100 cu. ft. consumption block. It is used to estimate revenues that would be produced from a given rate structure.

surcharges, and PUCRF. When asked to explain the discrepancy, Hillview commented there was a computer problem and supplied a third water use table which indicated much lower consumption. This third table was hand-done, whereas the first two were computer printouts, and Hillview's president indicated that the first two were the result of computer error. According to the staff witness, the only method that could be used to verify experienced consumption would be to construct a new water use table directly from the meter books.

After noting that experienced discretionary expenses were greater than D.82-08-083 adopted, the staff witness said that there was an established offset procedure for nondiscretionary items but the recovery of discretionary expenses should be by means of a general rate case.

He opposed further consolidation of Hillview's rate areas. In A.61148, the prior rate case, the staff had investigated consolidation of Hillview's then six rate areas. The staff recommendation at that time was to combine three of the rate areas and leave the other three alone, a recommendation adopted by the Commission in D.82-08-083. The staff, after making a study of the service area, concluded that major differences in geography, rate base, and some of the expense items could not recommend complete consolidation at that time. Also he advised that consolidation should only be considered on a general rate case or in a special application for that purpose alone.

As to the 10% escalation factor used by Hillview's Consultant to adjust D.82-08-083 adopted expenses to current price levels, the staff witness testified that the Branch uses factors updated monthly by the Commission staff, and these factors are considerably lower than the 10% used by the Consultant. He also questioned the 12.5% growth factor used by the Consultant, inasmuch as some expense items, such as depreciation and ad valorem taxes are

not directly related to increased customers. In any event, he declared, this type of analysis is properly the subject of a general rate case.

Should the applicant get the relief it was seeking in this application, it would be tantamount to the relief ordinarily obtained in a general rate case. Should the Commission grant such relief, in his opinion, "...we would have a lineup with water companies outside our front door so long that it would take years to catch up." The Branch position is that there probably is a revenue shortfall, but because of the inaccuracies that the staff felt were in the water use table, they do not feel that they can come up with a solid recommendation as to whether or how much of a shortfall there is. They agree that there is a reduction in consumption but they do not know whether this reduction will be permanent or temporary. They do feel, however, that relief should not be granted to the utility on an emergency basis. Should the Commission decide to grant relief to Hillview, it should be made clear that such action was not to be taken as an endorsement of the revenue adjustment mechanism for water utilities. The Branch was also recommending, as a condition for any rate relief, that an outside CPA, one well versed in water utility work, be retained by the utility at its expense to audit Hillview's 1983 revenue accounting books and procedures.

Finally, in response to a question by the ALJ, the staff witness compared Hillview's present rates with those of other foothill region water utilities. He considered Raymond and Coarsegold Highlands to be high, and Indian Lakes and Oakhurst to be about average.

#### Closing Statements and Briefs

Hillview's Consultant and the staff counsel made closing statements and both parties filed briefs. Hillview's Consultant indicated that the utility had no objection to relief being granted.

subject to refund. The staff emphasized the inconsistency between the various revenue estimates and claimed that applicant had demonstrated neither a financial emergency nor how the relief requested would cure the alleged emergency. The staff also declared that Hillview's request to consolidate rate areas should be denied because the water company has shown no change in the circumstances which led to denial of such a request in the utility's last general rate case.

Identification of Issues

Despite the many degressions by both parties in presenting their cases, it is clear that there are only five issues before the Commission, as follows:

1. Is Hillview's request properly before the Commission?
2. Is there a revenue shortfall and, if so, what amount of revenue augmentation would be appropriate?
3. Is it reasonable to consolidate Hillview's four rate areas into one?
4. What would a proper rate structure be in the event revenue augmentation was found to be required?
5. Should the Commission require an audit by a private CPA?

Is Hillview's Request Properly Before the Commission?

PU Code, requires, in § 451, that all charges by a public utility shall be just and reasonable. The Commission's Rules of Procedure state, in Rule 87, that the rules "shall be liberally construed to secure just, speedy, and inexpensive determination of the issues presented."

Considering that it is evident that Hillview has made a sincere effort to place its claim of a revenue shortfall before the

Commission in a manner satisfactory to the Commission, considering that an ongoing significant revenue shortfall would be an indication that the charges rendered were not just and reasonable, and considering that the Commission's rules are intended to promote effective utility regulation, the Commission finds that the issue of revenue shortfall of Hillview is properly before it.

Is There a Revenue Shortfall?

The Commission has before it five separate revenue estimates, as follows:

<u>1983 Revenue</u>	<u>Source</u>
\$150,003.92	Application
150,037.04	Petition
152,233	Exh. 2 (Hillview)
164,707	1983 Annual Report
233,000	Exh. 1 (Staff)

(In addition, the staff, in its brief, contends that the third water use table submitted by Hillview indicated 1983 revenue of \$151,863. No reference was given as to where this figure could be found in the record.)

The Consultant for Hillview reconciled the Annual Report figure to his determination and then reconciled this determination to the billed revenues. The staff remains skeptical, because of the large difference between Hillview's revenue claims and the revenues computed by the staff from the application water use table. The figures supplied to the Commission by the consultant on the witness stand and by Hillview in the Annual Report were submitted under oath and penalty of perjury. For the purpose of this proceeding the Commission will accept the Consultant's \$152,233 as a reasonable representation of Hillview's 1983 revenues, and accept the explanation that the application water use table is wrong because of a computer error.

Hillview's Consultant has calculated that, had the authorized rates produced the revenue per customer they were intended by D.82-08-083 to produce, \$345.93 per customer, the total revenue for Hillview's 1983 average number of customers of 585 would have been \$202,870.<sup>3</sup> Hillview's requested rate would produce \$189,200, or 93% of the requested amount.

In looking for the reason for the shortfall, the Commission notes that 1981 was a low rainfall year and 1982 and 1983 were higher ones. Because dry year 1981 water consumption was used for D.82-08-083, instead of normalized consumption, and because more water from rainfall was available to Hillview's customers in 1982 and 1983, the utility's revenues per customer were lower than those contemplated by D.82-08-083. Also, the \$345.93 of revenue per customer would not represent the average customer's total bill. To the basic charge for water must be added the 1.5% PUCRF and the large SDWBA surcharges. Although not excessive when compared to costs of other essential components making up the total cost of living, or to those of other foothill water utilities, the rates are high compared to those of utilities serving more metropolitan areas.

For Hillview to function it must have revenues commensurate with these authorized by D.82-08-083, however, it is important to note that only a single element of operations, i.e. revenues, has been examined in this proceeding. We will accept this circumstance and authorize a revenue augmentation. The Commission is mindful of the fact that dry-year consumption figures were used to project revenues and for that reason it is appropriate to adjust the single element of revenues rather than reviewing expenses also. Although increases in expenses have not been investigated by the staff it is obvious that they have occurred. The Commission finds that present

---

<sup>3</sup> This figure includes \$503 for nine very small flat-rate customers. A review of Hillview's filed tariffs reveals no flat-rate schedule.

rates are producing a revenue shortfall and that Hillview's requested annual meter revenue level of \$189,200 or \$345.93 per customer is reasonable. Hillview's revenues should be augmented to produce \$345.93 per customer. The increase in rates to produce such revenue will be subject to refund to the extent that annual revenues exceed \$345.93 per customer. The increase will continue in effect until December 31, 1986 unless further extended by the Commission upon a showing by Hillview that an extension is warranted. At the end of 1986, the present estimates of expenses will have been in effect four plus years and should be reviewed again.

The relief being granted by this decision is in response to the special circumstances described in detail in this decision and is not to be taken as a general endorsement of revenue adjustment mechanisms for water utilities.

Is Consolidation of Rate  
Areas Reasonable?

At the end of 1983, Hillview's four rate area were serving 612 customers, distributed as follows:

Oakhurst Systems	367
Coarsegold Highlands	20
Indian Lakes	177
Raymond	<u>48</u>
	612

All of the systems are located in the foothill region of Madera County, and all are located within the circumference of a 17-mile diameter circle. They are all serviced from the same central office in Oakhurst and maintained by the same two-person crew. There is an obvious community of interest among all of the areas. Prior to D.82-08-083, Hillview maintained six individual rate areas. As related earlier, in A.61148 the staff recommended combining three of these areas into the Oakhurst System but, after making a study of the



service, the staff concluded that there were major differences in geography, rate base, and some other expense items that could not allow for consolidation of the other three at that time. The Commission adopted that recommendation in D.82-08-083. In this proceeding the staff recommends that the issue be left for a general rate case or a separate application.

Having reconsidered the issue, the Commission concludes that the present fragmentation of Hillview's service area into four separate rate areas, one of which has only 20 customers, another 48, should not continue. While there may be differences in rate base or pumping costs between areas, the same situation applies to utilities whose serving areas are contiguous. The Commission does not attempt to scrutinize such utilities to identify areas of low or high rate base per customer and set rates accordingly. It is feasible in Hillview's case because the small foothill communities it serves, while close together, are not geographically contiguous.

The staff objects to the Consultant's proposal of two rate areas on grounds that no formal notice of the proposal had been disseminated. While the Commission does not concur that every alternate rate proposal brought forth in the course of a rate proceeding must be subjected to the notice procedure required by PU Code § 454(a), it will not accept the Consultant's proposal. The only virtue of that proposal is expediency, the mitigation of the impact of the new rates on the customers of Indian Lakes. The Commission could not make a finding that such rates are just and reasonable. Further, lower than warranted rates based on expediency alone would not meet the Commission's objective of conservation-encouraging rate designs.

Accordingly, the Commission will find that Hillview is operated and maintained as a single water system and that a single

rate schedule (except for the SDWBA surcharges) is appropriate, just, and reasonable for the entire Hillview water system.

What is a Proper Rate Structure For Hillview's Consolidated Operations?

The thrust of the Commission's water rate policy over the last several years has been to minimize service charges and to maximize that part of the quantity rate over the 300 cu. ft. lifeline block. As can be gathered from the this proceeding, severely inverted rates tend to destabilize revenues. When usage drops, revenue drops disproportionately. Disproportionate drops in revenue, whether due to conservation by customers or to climatic conditions, can cause hardships on small utilities that must service high fixed costs from slender financial resources. Further, as illustrated by Hillview's Consultant, relatively low service charges, combined with relatively high quantity rates, can and do result in wide fluctuations in revenue over a year or a climatic cycle. The revenue deficit months must be financed by maintaining a large cash reserve or more commonly by borrowing. Thus, the art of designing rates to promote conservation while at the same time not straining the financial resources of the small business entities providing water utility service requires a balance between revenue raised through the service charge and that generated by the quantity rate. Also, the quantity rate should not be set so high, relative to the service charge as to cause a repression in revenues below the amount intended.

In retrospect, it is obvious that the combination of a drier than average test year and an aggressive rate structure intended to foster conservation has reduced Hillview's water sales to a point that the revenues require enhancement. The most favorable mix of service charge and quantity rates will depend on local climate, community patterns, and other factors that may not be readily apparent. A reasonable balance can only be determined by

means of experiment. Inasmuch as the rates being authorized by this decision will be subject to refund, and the previously authorized rate structures have proven to be unbalanced, the rate structure and rates proposed by Hillview provide a reasonable second approximation of the optimum rate structure. Should they yield excess revenue, this order makes provision for refund of such excess revenues.

The Commission will find Hillview's present rate structure and rates to be, for the future, unjust and unreasonable, and the rate schedule proposed by Hillview to be just and reasonable.

Should the Commission Require an  
Audit by an Independent CPA?

It is apparent from the diverse revenue estimates for 1983 and the staff's inability to verify them that Hillview's operations, and particularly its revenue accounting, is in need of audit. Should the Commission direct Hillview to engage an independent CPA, as the staff witness recommends, then Hillview is entitled to claim the expense of hiring this auditor in its next general rate case, and if authorized, to collect the expense from its ratepayers. This is not necessarily in the best interests of the ratepayers and instead, the Evaluation and Compliance Division will be directed to make the audit. Because of staffing limitations, however, the 180-day limitation for the performance of this audit, which the staff witness recommends, will not be adopted.

Findings of Fact

1. The request of Hillview for a revenue augmentation to realize the revenue level authorized by D.82-08-083 is properly before the Commission.

2. Hillview realized revenues of \$152,233 in 1983. Had the level of \$345.93 per customer by D.82-08-083 been maintained, Hillview would have realized \$202,870. Hillview thus experienced a

1983 revenue shortfall of \$50,637 below the level contemplated by D.82-08-083.

3. Hillview's requested 1983 annual rate level of \$189,200, requiring an augmentation revenues of \$36,967 or 24.3%, is reasonable for a limited period to offset the use of 1981 dry-year consumption estimates.

4. To the extent Hillview's realized meter revenues in any one calendar year exceed an average of \$345.93 per metered customer, the excess should be credited to customers' bills for the month of April of the following year. The April credit, per customer, should be determined by dividing the prior year gross revenue by the average number of customers in that year. Rate increases subsequent to this order should not be considered in the above calculation. The credit should be based on relative water use in excess of 3,600 cu. ft. per year for the calendar year for which the credit is calculated.

5. Revenues was the only element of Hillview's results of operation examined in this proceeding.

6. Revenues estimated in D.82-08-083 were based on dry-year consumption.

7. Hillview's expense estimates from D.82-08-083 will have been in effect four plus years by December 31, 1986 and should be reexamined .

8. Hillview is operated and maintained as a single water system and a single rate schedule (except for the SDWBA surcharge) is appropriate, just, and reasonable for the entire Hillview system. Hillview's request to consolidate its rate areas is reasonable.

9. Hillview's present rates and rate structure are, until December 31, 1986, unjust and unreasonable.

10. The rate schedule proposed by Hillview is, until December 31, 1986, just and reasonable.

11. Hillview has no tariffs on file for flat rate service.

12. The Evaluation and Compliance Division of the Commission should be directed to cause to be completed an audit of Hillview's revenue accounting.

Conclusion of Law

Based on the foregoing findings of fact, the rates and special condition set forth in the rate schedule comprising Appendix A of this decision are just and reasonable for Hillview and should be adopted.

O R D E R

IT IS ORDERED that Hillview Water Company shall:

1. File the revised rate schedule in Appendix A in compliance with General Order Series 96 after the effective date of this order. The revised schedules shall apply only to service rendered on and after their effective date, which shall be 5 days after filing. The revised schedule will expire automatically on December 31, 1986 unless further extended by the Commission based on a complete showing by Hillview that an extension is justified. In the event that the revised rate schedule expires, the rates will revert to the levels authorized by D.82-08-083.
2. File revised service area maps that correctly describe the areas in which Hillview is presently holding out to provide public utility water service.
3. File a tariff schedule setting forth flat rates presently being charged.

IT IS FURTHER ORDERED that:

4. The Evaluation and Compliance Division of the Commission is directed to cause to be completed an audit of Hillview's revenue accounting.

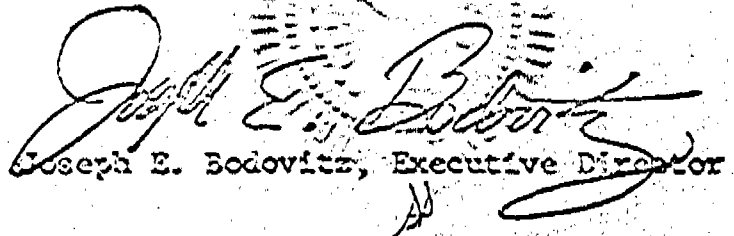
This order is effective today.

Dated NOV 21 1984, at San Francisco, California.

PRISCILLA C. GREW  
DONALD WIAL  
WILLIAM T. BAGLEY  
Commissioners

Commissioner Victor Calvo,  
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

Schedule No. 1

METERED SERVICEAPPLICABILITY

Applicable to all metered water service until December 31, 1986. ✓

TERRITORY

Coarsegold Highlands, Indian Lakes Estates, Raymond and four subdivisions in and near Oakhurst, Madera County.

RATES

## Quantity Rates:

First 300 cu. ft., per 100 cu.ft. ....	\$1.05
Over 300 cu. ft., per 100 cu.ft. ....	\$1.31

Per Meter  
Per Month

## Service Charge:

For 5/8 x 3/4-inch meter .....	\$ 12.00
For 3/4-inch meter .....	12.00
For 1-inch meter .....	18.00
For 1½-inch meter .....	24.00
For 2-inch meter .....	32.40
For 3-inch meter .....	60.00
For 4-inch meter .....	81.60
For 6-inch meter .....	135.60

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.

## APPENDIX A

Page 2

Schedule No. 1

METERED SERVICE

## Surcharge:

	<u>Royal Oaks Sunnydale</u>	<u>Goldside Hillview</u>	<u>Sierra Lakes</u>	<u>Raymond</u>
For 5/8 x 3/4" meter	\$ 8.80	\$ 3.00	\$0.85	\$ 6.15
For 3/4" meter	8.80	3.00	.85	6.15
For 1" meter	15.00	5.10	1.45	10.50
For 1 1/2" meter	29.05	9.90	-	20.30
For 2" meter	46.65	15.90	-	32.60
For 3" meter	88.00	30.00	-	-
For 4" meter	147.00	50.10	-	-
For 6" meter	211.00	-	-	-

The surcharge is in addition to the regular monthly metered water bill. The total monthly surcharge must be identified on each bill. The surcharge is specifically for the repayment of the California Safe Drinking Water Bond Act loan authorized by Decision 91560.

Special Condition

To the extent that the utility's annual meter revenues in any calendar year exceed \$345.93 per metered customer, the excess shall be credited to customers' bills rendered for metered service for the month of April of the following year. The credit shall be based on relative water use in excess of 3,600 cu. ft. per year for the calendar year for which the credit is calculated.

(END OF APPENDIX A)



other items involved in the ratemaking process, such as expenses, depreciation, and rate base, as such an investigation would constitute a study appropriate for a general rate increase proceeding, a type of proceeding that Hillview was not requesting. Rather the Branch, in its analysis, used the expenses, depreciation, and rate base adopted in D.82-08-083 as being items not in contention.

The Branch did not disagree with Hillview's claim of reduced consumption but the Branch noted discrepancies in various revenue data submitted by Hillview. In A.84-04-023, Hillview claimed 1983 metered revenue of \$150,004 but, using the water use tables attached to the application, the staff calculated revenue of \$230,641. Hillview, at the Branch's request, then submitted revised water use tables which, when Hillview's rate schedules were applied, supported a revenue estimate of \$147,819. When increased by 1.5% for the PUCRF, this estimate was substantially identical to the \$150,004 claimed by Hillview. The revenue situation is further confused by Hillview's having reported, in its Annual Report to the Commission for the Year Ended December 31, 1983, metered water revenues of \$164,204.

The Branch stated, in the report, that it believed that some reduction in consumption has taken place, causing revenues to decline. There are two factors which could have cause a reduction in consumption. The first factor is that 1983 was a year of abnormally heavy rainfall. (The revenue level adopted in D.82-08-083 was based on experienced 1981 rainfall, rather than a normalized level of rainfall.) The total rainfall for the nearest weather station (North Fork Ranger Station) in 1983 was 30 inches above the normal. The second factor is the relatively large increase in rates in 1982. The increases authorized in 1982 totaled over 70%. Experience by the Branch indicates that whenever a large increase in rates has been applied the consumption decreases. This repression is generally temporary, the Branch believes, and consumption usually recovers and

continues at or near the same rate as before the increase. In Hillview's case, however, the Branch does not preclude the possibility that the revenue repression may be permanent.

The Branch noted that it is present Commission practice to determine a water utility's revenue requirement on a normal year of operation that is intended to be reflective of the conditions under which the utility will operate under during the future period for which rates are set. Normally the revenues, expenses, and investment tend to track each other, and recorded rates of return approach these authorized. After about 12 months, revenues at rates last authorized start to fall short, resulting in a diminution of rate of return. Currently, the Branch observed, the Commission has offset procedures which protect a water utility against increases in major, nondiscretionary expense items such as purchased power and water. The Branch believes these procedures provide adequate rate relief between general rate filings. The Commission has not authorized a revenue adjustment procedure or mechanism that guarantees against shortfalls in revenue for water utilities, and it is the Branch's contention that revenue adjustment mechanisms act as disincentives for prudent management. The Branch recommends that the Commission, in the event that it should grant emergency relief, make it absolutely clear that its action is not to be taken as an endorsement of revenue adjustment mechanisms for water utilities.

Although the staff did not investigate the reasonableness of Hillview's expenses, it compiled the following comparison of 1983 expenses as reported by Hillview in its Annual Report to the Commission (the expenses claimed in A.84-04-023), and the 1982 expense levels adopted by the Commission in D.82-08-083:

Hillview's Consultant has calculated that, had the authorized rates produced the revenue per customer they were intended by D.82-08-083 to produce, \$345.93 per customer, the total revenue for Hillview's 1983 average number of customers of 585 would have been \$202,870.<sup>2</sup> Hillview's requested rate would produce \$189,200, or 93% of the requested amount.

In looking for the reason for the shortfall, the Commission notes that 1981 was a low rainfall year and 1982 and 1983 were higher ones. Because 1981 water consumption was used for D.82-08-083, instead of normalized consumption, and because more water from rainfall was available to Hillview's customers in 1982 and 1983, the utility's revenues per customer were lower than those contemplated by D.82-08-083. Also, the \$345.93 of revenue per customer would not represent the average customer's total bill. To the basic charge for water must be added the 1.5% PUCRF and the large SDWBA surcharges. Although not excessive when compared to costs of other essential components making up the total cost of living, or to those of other foothill water utilities, the rates are high compared to those of utilities serving more metropolitan areas. Repression of consumption resulting because of high rates and conservation by customers may be permanent.

For Hillview to function it must have revenues commensurate with these authorized by D.82-08-083. Although increases in expenses have not been investigated by the staff it is obvious that they have occurred. The Commission finds that present rates are producing a revenue shortfall and that Hillview's requested annual meter revenue level of \$189,200 is reasonable. Hillview's revenues should be

---

<sup>2</sup> This figure includes \$503 for nine very small flat-rate customers. A review of Hillview's filed tariffs reveals no flat-rate schedule.

augmented to produce this level of revenues. The increase in rates to produce such revenue will be subject to refund to the extent that annual revenues exceed this amount.

The relief being granted by this decision is in response to the special circumstances described in detail in this decision and is not to be taken as a general endorsement of revenue adjustment mechanisms for water utilities.

Is Consolidation of Rate Areas Reasonable?

At the end of 1983, Hillview's four rate area were serving 612 customers, distributed as follows:

Oakhurst Systems	367
Coarsegold Highlands	20
Indian Lakes	177
Raymond	48
	<hr/>
	612

All of the systems are located in the foothill region of Madera County, and all are located within the circumference of a 17-mile diameter circle. They are all serviced from the same central office in Oakhurst and maintained by the same two-person crew. There is an obvious community of interest among all of the areas. Prior to D.82-08-083, Hillview maintained six individual rate areas. As related earlier, in A.61148 the staff recommended combining three of these areas into the Oakhurst System but, after making a study of the service, the staff concluded that there were major differences in geography, rate base, and some other expense items that could not allow for consolidation of the other three at that time. The Commission adopted that recommendation in D.82-08-083. In this proceeding the staff recommends that the issue be left for a general rate case or a separate application.

Having reconsidered the issue, the Commission concludes that the present fragmentation of Hillview's service area into four separate rate areas, one of which has only 20 customers, another 48, should not continue. While there may be differences in rate base or pumping costs between areas, the same situation applies to utilities whose serving areas are contiguous. The Commission does not attempt to scrutinize such utilities to identify areas of low or high rate base per customer and set rates accordingly. It is feasible in Hillview's case because the small foothill communities it serves, while close together, are not geographically contiguous.

The staff objects to the Consultant's proposal of two rate areas on grounds that no formal notice of the proposal had been disseminated. While the Commission does not concur that every alternate rate proposal brought forth in the course of a rate proceeding must be subjected to the notice procedure required by PU Code § 454(a), it will not accept the Consultant's proposal. The only virtue of that proposal is expediency, the mitigation of the impact of the new rates on the customers of Indian Lakes. The Commission could not make a finding that such rates are just and reasonable. Further, lower than warranted rates based on expediency alone would not meet the Commission's objective of conservation-encouraging rate designs.

Accordingly, the Commission will find that Hillview is operated and maintained as a single water system and that a single rate schedule (except for the SDWBA surcharges) is appropriate, just, and reasonable for the entire Hillview water system.

What is a Proper Rate Structure For Hillview's Consolidated Operations?

The thrust of the Commission's water rate policy over the last several years has been to minimize service charges and to

maximize that part of the quantity rate over the 300 cu. ft. lifeline block. As can be gathered from the this proceeding, severely inverted rates tend to destabilize revenues. When usage drops, revenue drops disproportionately. Disproportionate drops in revenue, whether due to conservation by customers or to climatic conditions, can cause hardships on small utilities that must service high fixed costs from slender financial resources. Further, as illustrated by Hillview's Consultant, relatively low service charges, combined with relatively high quantity rates, can and do result in wide fluctuations in revenue over a year or a climatic cycle. The revenue deficit months must be financed by maintaining a large cash reserve or more commonly by borrowing. Thus, the art of designing rates to promote conservation while at the same time not straining the financial resources of the small business entities providing water utility service requires a balance between revenue raised through the service charge and that generated by the quantity rate. Also, the quantity rate should not be set so high, relative to the service charge as to cause a repression in revenues below the amount intended.

In retrospect, it is obvious that the combination of a drier than average test year and an aggressive rate structure intended to foster conservation has reduced Hillview's water sales to a point that the revenues require enhancement. The most favorable mix of service charge and quantity rates will depend on local climate, community patterns, and other factors that may not be readily apparent. A reasonable balance can only be determined by means of experiment. Inasmuch as the rates being authorized by this decision will be subject to refund, and the previously authorized rate structures have proven to be unbalanced, the rate structure and rates proposal by Hillview provide a reasonable second approximation

of the optimum rate structure. Should they yield excess revenue, this order makes provision for refund of such excess revenues.

The Commission will find Hillview's present rate structure and rates to be, for the future, unjust and unreasonable, and the rate schedule proposed by Hillview to be just and reasonable.

Should the Commission Require an Audit by an Independent CPA?

It is apparent from the diverse revenue estimates for 1983 and the staff's inability to verify them that Hillview's operations, and particularly its revenue accounting, is in need of audit. However, if we direct Hillview to engage an independent CPA, as the staff witness recommends, then Hillview is entitled to claim the expense of hiring this auditor in its next general rate case, and if authorized, to collect the expense from its ratepayers. This is not necessarily in the best interests of the ratepayers and instead, the Evaluation and Compliance Division will be directed to make the audit. However, because of staffing limitations, the 180-day limitation for the performance of this audit, which the staff witness recommends, will not be adopted.

Tariff Deficiencies

The review made of Hillview's tariffs made in connection with this proceeding reveals several errors, as follows:

1. There is no tariff service area map for the Indian Lakes area.
2. Schedule CH-1, Cal PUC Sheet 204-W (The Coarsegold Highlands tariff) does not carry forward the SDWBA surcharge from cancelled Sheet Cal PUC Sheet No. 181-W.
3. Cal PUC Sheet 204-W opens with the heading "Appendix A" and closes with "End of Appendix A." Apparently these notations were not removed when copied from some other document.

4. Although reference was made in the course of the proceeding to several customers being served at flat rates, no tariff is on file for such service as required by PU Code § 532.

These deficiencies should be rectified.

Findings of Fact

1. The request of Hillview for a revenue augmentation to realize the revenue level authorized by D.82-08-083 is properly before the Commission.
2. Hillview realized revenues of \$152,233 in 1983. Had the level of revenues intended by D.82-08-083 been maintained, Hillview would have realized \$202,870. Hillview thus experienced a 1983 revenue shortfall of \$50,637 below the level contemplated by D.82-08-083.
3. Hillview's requested 1983 annual rate level of \$189,200, requiring an augmentation revenues of \$36,967 or 24.3% based on 1983 consumption, is reasonable.
4. To the extent Hillview's realized meter revenues in any one calendar year exceed the revenues adopted here, the excess should be refunded to customers.
5. Hillview is operated and maintained as a single water system and a single rate schedule (except for the SDWBA surcharge) is appropriate, just, and reasonable for the entire Hillview system. Hillview's request to consolidate its rate areas is reasonable.
6. Hillview's present rates and rate structure are, for the future, unjust and unreasonable.
7. The rate schedule proposed by Hillview is, for the future, just and reasonable.
8. Hillview has no tariffs on file for flat rate service.



9. The Evaluation and Compliance Division of the Commission should be directed to cause to be completed an audit of Hillview's revenue accounting.

Conclusion of Law

Based on the foregoing findings of fact, the rates and special condition set forth in the rate schedule comprising Appendix A of this decision are just and reasonable for Hillview and should be adopted.

O R D E R

IT IS ORDERED that Hillview Water Company shall:

1. File the revised rate schedule in Appendix A in compliance with General Order Series 96 after the effective date of this order. The revised schedules shall apply only to service rendered on and after their effective date, which shall be 5 days after filing.
2. File revised service area maps that correctly describe the areas in which Hillview is presently holding out to provide public utility water service.
3. File a tariff schedule setting forth flat rates presently being charged.

IT IS FURTHER ORDERED that:

4. The Evaluation and Compliance Division of the Commission is directed to cause to be completed an audit of Hillview's revenue accounting.

This order becomes effective 30 days from today.

Dated \_\_\_\_\_, at San Francisco, California.

APPENDIX A

Page 1

Schedule No. 1

METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Coarsegold Highlands, Indian Lakes Estates, Raymond and four subdivisions in and near Oakhurst, Madera County.

RATES

Quantity Rates:

First 300 cu. ft., per 100 cu.ft. ....	\$1.05
Over 300 cu. ft., per 100 cu.ft. ....	\$1.31

Per Meter  
Per Month

Service Charge:

For 5/8 x 3/4-inch meter .....	\$ 12.00
For 3/4-inch meter .....	12.00
For 1-inch meter .....	18.00
For 1 1/2-inch meter .....	24.00
For 2-inch meter .....	32.40
For 3-inch meter .....	60.00
For 4-inch meter .....	81.60
For 6-inch meter .....	135.60

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.