

SEP. 16 1988

Decision 88 09 023 SEP 14 1988

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of )  
 by Citizens Utilities Company of )  
 California (U87W) for an order )  
 pursuant to California Public ) Application 85-06-010  
 Utilities Code § 2708 restricting ) (Filed June 6, 1985)  
 the addition of customers to be )  
 furnished with water service in its )  
 Montara-Moss Beach District. )

(For appearances see Decision 86-05-078.)

Replacement Appearance

Ira Kalinsky, Attorney at Law, for the  
 Commission Water Utilities Branch.

INTERIM OPINION IN PHASE IISummary of Phase I Proceedings

On May 28, 1986, the Commission issued Decision (D.) 86-05-078, which imposed a moratorium, with certain exceptions, on connection of additional customers to the Montara-Moss Beach District of Citizens Utilities Company of California (CUCC). The term of the moratorium was six months; however, by D.86-12-069, the Commission extended the moratorium until further order of the Commission. That order is still in effect, but a petition for modification of it was filed by Farallon Vista Associates on January 25, 1988. The petition was protested by the Water Utilities Branch and by CUCC. The matter is now pending before the Commission. Public hearings are expected in the Spring or early Summer.

Summary of Proceedings in Phase II

During hearings in OII 83-11-09, an investigation proceeding involving the water operations of CUCC in California, the staff proposed that Montara District water supply issues in the

investigation be transferred to A.85-06-010. CUCC agreed to the staff proposal.

Following the issuance of the interim opinion on Phase I (D.86-05-078) hearings were held on August 5 and 6, 1986, to consider the issues deferred to this proceeding from OII 83-11-09. During the hearings the Administrative Law Judge (ALJ) directed counsel for CUCC and staff to confer upon a list of issues to be briefed. The list was agreed upon between staff counsel and counsel for CUCC and concurrent opening briefs were filed on or about January 5, 1987. CUCC filed a closing brief on January 20, 1987. The staff, however, elected not to submit a closing brief.

Issues to be Decided

In conference after the close of hearing, counsel for staff and CUCC agreed upon the following issues for briefing:

1. Supply Issues

- A. What is the present supply?
- B. What should the supply be?
- C. Has the company complied with Commission orders regarding supply?
- D. Quality--are there new iron and manganese rules that affect any of the company's sources?

2. Ratemaking Issues

- A. Are rate or rate of return adjustments appropriate in this type of proceeding?
- B. If the answer to "A" is "yes", does the record in this proceeding justify any adjustment.
- C. Is the staff proposal for retirement of the Portola Wells appropriate?
- D. Is the staff proposal for treatment of terminated lease payments to Half Moon Bay Properties appropriate?
- E. Should the company's rate of return be reduced and if so, by what amount?

We will deal with each of these issues in the order presented.

Supply Issue 1A

What is the Present Supply?

Staff Exhibit 22 shows water production statistics for each of the water sources in the Montara District for each year between 1976 and 1985. The statistics are expressed in hundreds of cubic feet (Ccf) and in average annual gallons per minute (gpm). For each water source the staff has indicated what year's production was the highest for each source and has listed those quantities in Exhibit 22, Appendix A, Table 1, Column k, as the highest annual production in gpm. The quantities for each well now producing total 377 gpm. In making this analysis the staff has excluded the output of the Park Well on the ground that the iron and manganese content of this water exceeds DHS standards. (We will address this issue below.) The Park Well output was 6 gpm in 1979 which, if added to the 377 gpm of the other sources, would produce total output of 383 gpm.

CUCC bases its calculation upon staff Exhibit 22, Appendix A, Table 2, which shows well production for the Montara District in gpm for the period 1976 through 1985. CUCC believes that the recorded annual production of its water sources are representative of the true capacities of the well sources listed. To the production figures for wells, CUCC has added the Montara Spring source to obtain the true capacity of all sources in the system. CUCC's method produces a result in the range of 362-387 gpm, using the staff figure of 55 gpm for Montara Spring.

CUCC argues that most of the difference between staff's final estimate and CUCC's estimate for source capacity is accounted for by the staff's exclusion of Montara Spring and the Park Well. CUCC considers it unrealistic to exclude a water source that has produced water in every year for which some evidence was presented, even drought years. In 1983, 1984, and 1985 Montara Spring

produced between 50 and 55 gpm. CUCC also argues that it is necessary to include the Park Well, since this relatively small source is useable under present health rules by blending its water with CUCC's other sources. Therefore, CUCC estimates that the current total source capacity of its water sources is 387 gpm and contends that this figure is the most realistic and should be used.

Staff and CUCC are not far apart on this issue. With Montara Spring and Park Well added, the staff figure is 383 gpm, which compares with the CUCC figure of 387 gpm. We believe that the Montara Spring should be considered a regular source of water for the Montara District since it has produced water in each year during the period 1976 through 1985, except for 1980 when no records were available for this source. In the last three years of the record period the Spring produced between 50 and 55 gpm. This is a significant amount of water which we believe should be considered in calculating CUCC's present supply. Because of our decision below on the issue involving the Park Well, it should be considered as part of the useable water supply sources for this system. We will therefore add 6 gpm to the staff figure to produce a total of 383 gpm, which figure reflects the staff values for the Montara District wells plus the Montara Spring output and the Park Well output. We will adopt the staff figure, as adjusted, for the present supply of CUCC as of the closing date of this record, August 6, 1986.<sup>1</sup>

---

<sup>1</sup> Since the record closed, the California Coastal Commission (CCC) has authorized CUCC to build one of the two wells in the airport plain for which it sought authority. The well has been constructed and is now producing.

Supply Issue 1B

What Should the Supply Be?

CUCC argues that the system's 1,570 customers can be adequately served by the existing water sources providing approximately 383 gpm of water production. However, CUCC concedes that in order to provide reliable service (calculated with one of the largest sources out of service) the system will require water production of 440-465 gpm.

The staff states in its brief that it and CUCC are close in approximating the current shortage of 80 gpm. The staff goes on to say that CUCC's present water supply for the Montara District should be no less than 442 gpm.

The staff's estimate of 442 gpm to provide a reliable level of service to the Montara District customers is based on the assumption that 1,500 customers are to be served. (Staff brief, page 12). CUCC's estimate of 440-465 gpm is based on the assumption that the system presently has 1,570 customers.

The staff in its conclusions states that the Commission should order an additional 200 gpm, as in its prior orders. In the alternative to the 200 gpm, at least an additional 80 gpm to meet current customer demands should be secured.

Assuming that 80 gpm of additional water production will provide a reliable level of service to the existing customers, when added to the current sources of supply, that level of water production, between 440 and 465 gpm, will only provide for existing customers. In other words, it will not provide enough water production to add more customers to the system, either individual lot owners seeking to develop their properties or the Farallon Vista Development involving 147 housing units. As a result even an additional 80 gpm of water production will not spell the end of the moratorium on connecting additional customers in this water system.

Requiring CUCC to develop merely 80 gpm of additional water supplies will also have the effect of creating a potential

conflict between this Commission and the County of San Mateo. One of the conditions for approval of the county permits to build and develop two new wells in the Airport Plain was a requirement that CUCC shall reserve water system capacity specifically for the priority land use known as Farallon Vista Housing Development. If the two new airport wells are developed, 100% of their output may not be available to provide the 80 gpm of additional production that is necessary to provide existing customers with a reliable level of service. This is due to the county's demand that water system capacity be reserved for Farallon Vista Housing Development.

An additional 80 gpm of water production will also be insufficient to provide for normal growth of customers resulting from normal buildout of undeveloped lots within CUCC's service area. Data provided by CUCC, which we discussed in D.86-05-078, shows that such normal growth, excluding major developments such as Farallon Vista, could amount to 50 additional customers each year.

The staff's principal position on the water supply required in the Montara District is that at least 550 gpm should be provided by CUCC. This staff recommendation is based on the order in D.86193 requiring CUCC to provide an additional 200 gpm of well production. (Ordering Paragraph 1, D.86193 in C.10093 et al.) CUCC contends that D.86193 does not contain any reference to development of 550 gpm of total well supply. It also contends that the Commission did not adopt, and it is not clear that the staff even recommended, a 350 gpm figure for existing well capacity that the 200 gpm figure would be added to.

The staff, however, convincingly demonstrated that the Commission's order to require an additional 200 gpm of well production was based on existing well production in 1976 of 350 gpm. The staff furnished for this record a copy of the staff witness' report in C.10093 and a copy of that witness' direct and cross examination (Exhibit 37). From these documents it is clear that the staff witness in C.10093 found that 350 gpm of well

capacity was insufficient for the customers in the Montara District in 1976. He recommended that the Commission order CUCC to provide an additional 200 gpm of well production to provide reliable service to the customers in the Montara District. The Commission adopted the staff recommendation of 200 gpm of additional well production in its order in D.86193. That order can only be construed to require at least 550 gpm of total well production for the number of customers connected to the system in 1976. Therefore, the staff's current position that at least 550 gpm of total water production should be required of CUCC is well founded in D.86193.

D.86193 is not, however, the sole basis in this record for requiring 550 gpm of total water production. We note that on May 28, 1986, we found in D.86-05-078 that: "Four hundred customers have been added to the system since 1976". (Finding 12, page 33.) Two years have now lapsed since D.86-05-078 was signed. Even though that decision imposed a moratorium on water connections it did not forbid all connections. Certain property owners were excluded from the effect of D.86-05-078. Specifically, six lots in the Portola Estates Development were excluded from the effects of the moratorium. In addition, 57 applications for service connections had been approved by CUCC but had not yet been connected to the system. These 57 applicants could become customers while the moratorium was in effect for others. Apparently, some of these prospective customers became actual customers of the system between February, 1986 and January, 1987. While data submitted by CUCC shows 1,502 total connections as of February 1986 (D.86-05-078, page 28a), CUCC's opening brief filed January 5, 1987, states that the system has 1,570 customers. (CUCC Opening Brief, p. 4.) It seems likely that in the year or more that has elapsed since January 1987 a pent up demand for water connections would have accumulated at about the same rate that we estimated in D.86-05-078, that is, about 50 connections per year.

We are satisfied that total water production of 550 gpm for this system is justified by the points that we have mentioned above. In fact, it may in reality be a conservative figure in light of the Farallon Vista Development, another potential development of over 200 units planned by Half Moon Bay properties, normal demand through individual property owners developing their parcels, and the regulatory difficulties that CUCC has experienced in obtaining the approvals necessary to construct wells in the Airport plain. We will therefore require CUCC to develop additional water production capacity to bring its total production to 550 gpm.

Supply Issue 1C

Has the Company Complied With  
Prior Commission Orders Re Supply?

We do not need to belabor this issue, since D.86-05-078 established unequivocally that CUCC had failed to provide new well capacity of 200 gpm. We have appended hereto Findings of Fact 1 through 19, which contain the specific findings on the issue of additional water supply. (See especially Finding 11 and Finding 13 in Appendix A.)

Supply Issue 1D

Quality - Are there new Iron and Manganese  
Rules That Affect Any of the Company's Sources?

Staff has excluded from its list of useable wells the Park Well on the ground that it is contaminated and should not be used for domestic water supply. (Exhibit 22, page 4, paragraph 17.) In a footnote to its water statistics the staff elaborates that the Park Well does not produce potable water because the iron and manganese content exceeds DHS standards. (Exhibit 22, Appendix A, Table 1, Footnote 4.) The staff apparently abandons this position in its brief when it recommends merely "strict surveillance of the Park Well to assure its consumers that it is useable" (Staff Brief, page 13.) In any event CUCC made a



convincing case in its opening brief that DHS regulations do not forbid the use of the Park Well water. In practice, water from the Park Well is blended with other water before it is delivered to the customers. Although the Park Well water is high in iron and manganese at its source, at the point of delivery to the consumer the blended water meets all applicable DHS standards.

Ratemaking Issue 2A

Are Rate or Rate of Return  
Adjustments Appropriate  
in This Type of Proceeding?

During Phase II the staff made three recommendations concerning the rates of CUCC. Regarding water rates the staff recommended that they be permanently reduced to reflect:

- a. The termination of the \$9,800 annual charge for the lease back of HMBP share of the Portola Wells water.
- b. The retirement of the Portola Wells No. 1 and No. 2 from Montara rate base. The depreciation reserve should be credited with only the actual depreciation taken on the wells.
- c. An amortization plan for the remaining cost of the Portola Wells No. 1 and No. 2 should be put into effect as set forth in Appendix D of Exhibit 22.

Because of CUCC's failure to produce additional water supplies, staff also recommended that the Commission reduce the allowable rate of return on equity from 13.2% to 6.6%, thereby reducing the overall rate of return from 12.04% to 7.55%. The staff further recommended that the lower return on equity remain in effect until CUCC complies with D.86193 (1976) to increase production capacity to at least 550 gpm.

CUCC and the staff agreed that one of the issues to be briefed in this proceeding was ratemaking issue 2A: Whether rate

or rate of return adjustments are appropriate in this type of proceeding.

Neither party cites the underlying application proceeding as the basis for ratemaking adjustments. It would clearly not be appropriate to use an application under Public Utilities (PU) Code § 2708 as a vehicle for revising, amending, or modifying the rates of a public utility. Rather, both the staff and CUCC cite OII 83-11-09 as a source of the Commission's authority, if any, to adjust rates in this proceeding.

The staff in particular cites Paragraphs 4(e), 4(g), and 6 of OII 83-11-09 in support of the Commission's authority to adjust rates in in this proceeding. The relevant parts of Paragraph 4 of OII 83-11-09 are as follows:

"4. This investigation will consider:"

\* \* \*

"e. Whether CUCC or its subsidiaries acted in an imprudent manner in the management and development of their Spring and Well resources and watershed lands. This investigation will consider the appropriate ratemaking mechanism(s) and orders if the Commission determines that CUCC or its subsidiaries have been imprudent in the management of the utilities' water sources. We invite the Cal. Dept. of Health Services or any other party to submit evidence on water quality issues which may be relevant to this investigation."

\* \* \*

"g. Whether any other order or orders should be issued by this Commission in the exercise of its jurisdiction."

\* \* \*

"6. The Commission hereby puts each respondent on notice that other rate cases for CUCC's other districts or subsidiaries may be

reopened and consolidated with this proceeding if the Commission finds it appropriate, including consideration of the issue raised in paragraph 4 above."

On the other hand, CUCC argues that in OII 83-11-09 the Commission stated the investigation would consider appropriate ratemaking mechanisms and orders if the Commission determines that CUCC or its subsidiaries have been imprudent in the management of the utilities' water sources. In addition, the Commission reopened A.60220, the most recent case for the Guerneville District, and consolidated it with these proceedings. This was done, according to CUCC, for the express purpose of considering the appropriate ratemaking treatment for the timber harvesting revenues in that district. Finally, in Ordering Paragraph No. 6, the Commission put CUCC on notice that other rate cases might be reopened and consolidated with the OII for consideration of the OII issues now made part of this proceeding. Since the Commission did not reopen the previous Montara rate case, CUCC argues that it is not appropriate to set new rates for Montara.

In taking this position, CUCC states that it is not hiding behind a technicality, but is rather following the Commission's preference for doing ratemaking in general rate cases where there is full public notice that rates may be adjusted, full opportunity for public comment, and where all of the factors that affect rates can be examined and properly balanced. CUCC asserts that the practice of using a test year is predicated on this idea. It cites Southern California Edison Co. (1977) 81 CPUC 749.

CUCC concludes on the basis of the foregoing arguments that this proceeding is not an appropriate one for rate setting. It asserts that the staff has selected one isolated issue, amortization of Portola Wells Nos. 1 and 2, and contends that rates should be reset solely on account of the impact of that issue. However, according to CUCC, there are other important issues affecting rates and rate of return that the parties did not present

evidence on because this is not a general rate case. The resolution of those issues will, according to CUCC, have a decisive impact on water rates in Montara.

In OII 83-11-09 both the Commission and the staff contemplated that ratemaking changes due to the issue of timber harvesting revenues would be likely for the Guerneville District. Accordingly, we consolidated that investigation proceeding with A.60220, the most recent general rate proceeding of the Guerneville District. For other districts of CUCC, where ratemaking adjustments were deemed less likely, we merely included in our OII a notice that other rate cases for CUCC's other districts or subsidiaries may be reopened and consolidated with this proceeding if the Commission finds it appropriate.

Neither the staff nor any other party to this proceeding has filed a motion to consolidate the most recent general rate proceeding of the Montara District with OII 83-11-09 or with this application proceeding. Consequently, there is no backdrop against which the staff's proposed ratemaking adjustments may be viewed.

As a general rule it is desirable to consider a utility's total operations before adjusting rates. Thus, the bulk of the Commission's ratemaking business is conducted in general rate proceedings where all elements of the company's operations can be considered. An exception to this rule is frequently made in offset cases of one kind or another. Where a single factor in a company's results of operations is significant, the Commission may and frequently does consider it in isolation. For instance, energy costs for electric corporations are considered in energy cost adjustment clause proceedings; the cost of natural gas for gas

corporations is considered in gas adjustment clause proceedings; and major additions to the rate base of a public utility are frequently considered in rate base offset proceedings.

We do not have before us in this proceeding either a general rate proceeding or a traditional offset case. Furthermore, the proposed rate base adjustment is not considered in the context of other rate base adjustments made necessary by events taking place in this utility since the last general rate proceeding, as would be the case in a general rate proceeding.

Based upon the foregoing discussion we do not believe that this proceeding is an appropriate vehicle for making rate base or rate of return adjustments. Although our answer to issue 2A would seem to make it unnecessary to consider the specific staff proposals, we will nevertheless discuss the staff proposed adjustments individually. In doing this we will not consider Ratemaking Issue 2B separately, since it consists merely of a general statement that encompasses the three individual issues 2C, 2D, and 2E.

Ratemaking Issue 2C

Is the Staff Proposal for Retirement  
of the Portola Wells Appropriate?

Staff recommends that Portola Wells 1 and 2 be retired from the rate base of the Montara District. The facts upon which the staff recommendation is based are not in dispute. In February 1980 CUCC purchased the four Portola Wells from Half Moon Bay Properties (HMBP). Portola Well No. 1 failed in 1981 and Portola Well No. 2 failed in early 1982. Portola Wells 1 and 2 have

remained inoperative since 1981 and 1982, respectively. Staff contends that the wells should be removed from rate base because they are no longer used and useful. According to the staff, the ratepayers have been paying depreciation, taxes, and a return on these wells, which have not benefitted the ratepayers since they became inoperative. The staff cites D.85-08-046 in PG&E A.83-09-49 in support of the proposition that plant which ceases to be used and useful should be excluded from rate base.

In Exhibit 22, Appendix D, the staff sponsored an amortization plan which it testified would permit CUCC to recover its cost of the Portola Wells 1 and 2 without earning a return on the wells. The staff cites in support of its amortization plan SDG&E (1979) 1 CPUC 2d 644. We have attached a copy of Appendix D to this opinion in which the staff has calculated the historical cost of the two Portola Wells in question at \$72,922. The staff has also calculated the amounts that the ratepayers have paid in earnings, taxes, depreciation, and lease costs during the period 1982 to 1986. The total ratepayer cost based on these calculations is \$84,089. The historical cost of the wells is then subtracted from the cost paid by the ratepayers through rates and the balance of \$11,167 is, according to the staff recommendation, to be amortized over three years to the benefit of the ratepayer.

CUCC contests the staff's proposal concerning Portola Wells 1 and 2, arguing that even if this proceeding was a proper one for general rate adjustments, it is clear that the staff's ratemaking proposal for amortization of some of the costs of Portola Wells Nos. 1 and 2 is not appropriate because it would involve retroactive ratemaking.

We do not generally adjust rate base between general rate cases simply because we have a proceeding before us and a change in rate base. During the period between one decision in a general rate proceeding and another for the same company, we assume that certain plant items will be retired, for obsolescence or other

reasons, and that simultaneously other plant items will go into service by becoming operational plant facilities. If it is deemed appropriate to examine the rate base of a public utility between general rate proceedings, then, as a general rule, all appropriate adjustments to rate base should be examined to account for both additions and retirements.

The staff's proposed rate base adjustment does not result from a major change in rate base or any other exceptional circumstance; it appears instead to be based on an isolated, fairly commonplace, event involving the deterioration of plant presently in rate base. The staff has examined Portola Wells Nos. 1 and 2, which have gone out of service in the period between general rate cases, but has not examined the additions and betterments to plant that have occurred in the same period. It would not be reasonable to reduce rate base to account for the nonoperational status of Portola Wells Nos. 1 and 2 without examining additions and betterments to plant in service that have occurred during the same period. We do not find the present situation unusual enough to warrant exceptional treatment, and therefore decline to make the rate base adjustment requested by staff.

Citations by the staff to D.85-08-046 in PG&E A.83-09-49 and to SDG&E (1979) 1 CPUC 2d 644 are not helpful to the staff's position. D.85-08-046 was cited for general language on the concept of used and useful utility plant in rate base. That decision was issued in PG&E A.83-09-49, which sought authority to increase electric rates to reflect retirement and decommissioning costs of Humboldt Bay Power Plant, Unit 3. In that rate proceeding PG&E sought \$86,086,000 of additional revenue. The Commission authorized the utility to collect \$52,910,000, which it found to be the prudently incurred direct cost of retiring Humboldt Bay Power Plant, Unit 3. The Commission disallowed \$33,176,000 of accrued allowance for funds used during construction. Unit 3 had already been removed from rate base in D.91107 (2 CPUC 2d 596 (1979)),

PG&E's test year 1980 general rate case. The staff has not demonstrated how the PG&E decision is similar and thus should govern any decision arising out of this proceeding.

In like manner the staff's citation of the 1979 SDG&E decision provides no assistance. That decision arose out of a general rate proceeding. The matter quoted by the staff in its brief pertained to the rate treatment of certain costs associated with the abandoned Sundesert Project. The paragraph quoted by the staff contains the following sentence, which we assume is the point the staff wished to emphasize: "We believe that adherence to our past practice of allowing recovery of abandonment costs from ratepayers while denying rate base treatment is an equitable solution to a difficult problem." Again, the factual situation involved in the SDG&E case is dissimilar to that with which we are faced in this proceeding. In SDG&E we addressed the issue of the treatment for ratemaking purposes of plant that was never in rate base and that had to be abandoned. In this case we are faced with plant that is in rate base which has become prematurely obsolescent due to failure of the wells. In addition the SDG&E case was a general rate proceeding, whereas this proceeding is an investigation proceeding the scope of which did not encompass a general inquiry into the entire operative plant of the utility nor the entire results of operations of the utility.

For the reasons that we have discussed we will not adopt the staff's recommendation for amortizing \$11,167 by reducing rates over a 3-year period. Our resolution of this issue means that we need not decide CUCC's retroactive ratemaking arguments. We note, however, that they cause us some concern.<sup>2</sup>

---

<sup>2</sup> Because the staff did not file a closing brief, it did not respond to the arguments on brief of CUCC on the issue of retroactive ratemaking.



Ratemaking Issue 2D

Is the Staff Proposal for Treatment  
of Terminated Lease Payments to  
Half Moon Bay Properties Appropriate?

During hearings in Phase I, CUCC stipulated that lease payments that are now a part of its revenue requirement in the amount of \$9,600 per year may be treated as a deferred credit and accumulated in a balancing account with interest until the next general rate proceeding of the Montara District. At that time, the amount accumulated may be used to reduce CUCC's future revenue requirement. Based on that stipulation, the Commission ordered CUCC to establish a memorandum deferred credit account and to accumulate \$800 per month representing the lease payments on the Portola Wells, with interest at 7%, until the next rate proceeding for Montara. (D.86-05-078, Ordering Paragraph 9.)

In Phase II the staff proposed to reflect in rates the termination of charges paid by CUCC for the lease back of HMBP's share of the water from the Portola Wells. Since CUCC is no longer paying these charges, having purchased HMBP's interest in the Portola Wells, the staff believes that rates should be reduced to reflect this decrease in expense.

This issue involves expenses of about \$9,000 per year, which the Commission has already considered in its decision on Phase I. Pursuant to CUCC's stipulation, we ordered CUCC to establish an account and to accumulate these expenses for later amortization, with interest, to the benefit of the ratepayers. That disposition will fully protect the interests of the ratepayers and will not involve us in item-by-item rate adjustments between general rate proceedings.

During Phase II, a witness for CUCC testified that the balancing account established in D.86-05-078, as described in the preceding paragraph, should contain, in addition to the accumulation of the discontinued monthly lease payments, the

accumulation of costs incurred in the search for the new water sources. Once the search is completed, according to the witness, the charges can be removed from the balancing account and recorded in plant if the search is successful or offset against the lease payments. The remainder of the balancing account can then be handled in Montara's next general rate proceeding. CUCC continues to advocate the same position through its brief.

In its brief the staff opposes the proposal by CUCC. The staff points out that expenses incurred by CUCC in its search for new sources of water should be capitalized and should become a part of the rate base in the next general rate proceeding of CUCC.

It would therefore be inappropriate to offset costs that will be capitalized against the expense items that are accumulating as credits for the benefit of the ratepayers in the balancing account established in D.86-05-078. Accordingly, we will deny the request of CUCC for balancing account treatment of costs incurred in the search for new water sources.

Rate-making Issue 2E

Should the Company's Rate of Return  
Be Reduced and if so, by What Amount?

The staff recommends that the Commission reduce the allowable rate of return on equity from 13.2% to 6.6% thereby reducing the overall rate of return from 12.04% to 7.55%. The staff further recommends that the lower return on equity should remain in effect until such time as CUCC complies with the order in D.86193 (1976) to increase water production capacity to at least 550 gpm. The staff's recommendation is based on CUCC's consistent failure to develop additional supplies of water. As a consequence of this failure CUCC has applied for and received an order imposing restrictions on connection of new customers. (D.86-05-078.) Staff requests that a penalty be imposed on CUCC to provide an incentive for its shareholders to provide reasonable water supplies to its customers. In support of its rate of return penalty recommendation

the staff cites General Telephone Company of California, 4 CPUC 2d 428, wherein the Commission reduced General Telephone's rate of return because of inadequate service. Staff requests similar treatment for CUCC in this proceeding because of its failure to provide reliable water supplies to its customers.

CUCC responds that the staff has not demonstrated that the development of the Portola Wells or any other source was imprudent. Rather, according to CUCC, the evidence shows that CUCC was justified in believing that the Portola Wells would satisfy customer demands for service, but that those sources did not produce as reliably as expected. CUCC asserts that as it became aware that the Portola Wells would not provide adequate supplies, CUCC has continued its efforts to identify and develop other prospective sources. These efforts have included the retention of expert hydrologists and negotiations with Half Moon Bay Properties, the area's largest landowner to obtain additional sites. CUCC has also been seeking the agreement of the County of San Mateo and necessary permits to develop two new wells at Half Moon Bay Airport, the most promising location for the development of new supplies. CUCC believes that there is no basis in this record for penalizing CUCC by reducing its rate of return.

The staff cites General Telephone Company of California, 4 CPUC 2d 428, in support of its request that CUCC's rate of return be reduced. The General proceeding was a general rate case in which all the elements of the company's operations were examined. In the decision in that proceeding the Commission examined the company's capital structure and costs of capital in detail and concluded that the cost factor for common equity was 14.10%. That cost factor, taken together with cost factors for other parts of the capital structure, and weighted in accordance with the adopted capital structure percentages, resulted in a rate of return of 10.53%. The Commission also examined in that proceeding service deficiencies in General's operations that had caused a multitude of

customer complaints. To give General an incentive to take concerted and effective measures to substantially improve its level of service the Commission reduced the authorized return on equity by 0.50% to 13.60%. This adjustment reduced the revenue requirement for General by \$7.4 million. The Commission added that if General showed that its service had been improved to a satisfactory level, the Commission would consider adjusting rates to provide General with an opportunity to earn a 14.10% return on equity. However, the penalty was to be removed no earlier than December 31, 1981. The order was signed and effective October 22, 1980, indicating that the penalty would be in effect for approximately 14 months, assuming that General could show improved service within that period.

There are several major distinctions between the General case and this proceeding. First, the reduction in return on equity ordered in the General case occurred in a general rate proceeding, where all aspects of the company's operations and service were examined and an appropriate balance could be arrived at between the interests of the ratepayer and the interests of the utility shareholders. Second, the reduction in return on equity in the General case reflected the Commission's evaluation of the level of service provided by General to its customers. In contrast, the proposal in this case is to reduce return on equity by 50% for failure to comply with prior Commission orders. Third, the Commission placed a limit on the time during which rates would be reduced to reflect inadequate service. The staff made no such proposal in this case. Fourth, the authorized return on equity, after deducting 0.50% percentage point from the adopted cost factor for common equity of 14.10%, still yielded a 13.60% return on common equity. This value was within the range of recommendations made by the expert witnesses who testified on the subject of cost of capital.

The staff recommendation made in this proceeding to reduce return on equity from 13.2% to 6.6% is not made within the context of an overall study of the cost of capital of CUCC. Moreover, such a reduction of return on equity would produce a penalty of \$70,260 per year.<sup>3</sup> A penalty of this magnitude is proposed at a time when the development of additional water supplies is the primary task of this public utility. Since the development of such supplies is at least in part a function of the availability of funds to use for exploration, test well drilling, and development of new wells, it seems inappropriate to us that such a significant fine is proposed at this juncture. Accordingly, we will not adopt the staff proposal.

However, we do believe that some penalty should be assessed to CUCC for its failures to timely develop the water supplies that are urgently needed for this system. Within the context of a general rate increase application or a general investigation of the rates, operations, and services of the Montara District a more finely tuned rate of return reduction, similar to the one exacted in the General Telephone case, would be appropriate in our view.<sup>4</sup>

---

3 See Appendix E for derivation of this number.

4 The staff proposal to reduce return on equity from 13.2 to 6.6% is in fact an attempt to exact a punitive fine from CUCC for its failure to obey the orders of the Commission. Such punitive fines are ordinarily sought through enforcement proceedings initiated by OII or OSC, wherein due notice of the general orders, orders, rules, regulations, or statutes violated and of the penalties sought by the staff are given in writing to the respondent public utility. Even a liberal interpretation of the language of OII 83-11-09 could not convert it into an enforcement proceeding for the Montara District.

Need for a General Rate Proceeding

The last general rate proceeding for the Montara District was A.60253. In that case, based on a 1982 test year, the Commission found that a revenue increase of \$388,900 or 162.8% was necessary. However, this was reduced by a \$106,100 offset rate increase granted by Resolution W-2809, dated March 17, 1981. The revenue increase was further reduced for 1982 to \$168,700, pursuant to the Commission's policy of holding rate increases in one year to 50%. The Commission authorized the collection of the revenue deficiency (\$146,300, including interest) to be deferred to 1983 and 1984. (D.82-05-076, page 3.)

The Commission based much of its decision in the Montara case on companion decisions arising out of CUCC's Sacramento District (D.82-02-059) and Guerneville District (D.82-03-023) rate increase applications. Accordingly, the discussion and findings in D.82-05-076 were abbreviated. However, the Commission found that an overall rate of return of 12.04% was reasonable, with a return on equity of 13.2%. In addition, the Commission stated:

"... Water quality and system condition at Montara have been improved in the last half decade, and further upgrading of the system is contemplated in Montara's construction budget.

"The enormity of the present rate application stems in large part from the fact that Montara has expended approximately \$878,706 of [CUCC's] funds in completing ordered construction programs in the water district in the last five years. This amounts to about \$685 per customer. During this time there have been no substantial rate increases granted to Montara, with the exception of the offset increase granted March 17, 1981 by Resolution W-2809." (D.82-05-076, page 8.)

In Finding 6 the Commission found that:

"Montara's level of water service is adequate." (Id., page 11.)

There was no discussion of the issue of water supply and no mention of the Commission's prior orders requiring CUCC to provide 200 gpm of additional well production.

Finally, the Commission stated at page 8 that the Montara District had 1,272 customers. The source of the 1272 figure is CUCC Exhibit 7, page 16. The figure represents the number of commercial customers as of December, 1979.

The need for a general rate proceeding is indicated by the following factors:

1. Rate base should be adjusted to reflect the failure of two Portola wells, discussed above.
2. Lease expense should be adjusted to reflect the elimination of lease payments to HMBP and to amortize over a future period the accrued credits, discussed above.
3. Revenues should be adjusted to reflect an increase in customers from 1272 to 1599 or 26%. (CUCC's monthly report for April, 1988.) CUCC's customers have recently reached a high of 1610, based on the monthly report for January, 1988. The increase in customers since 1979 tends to increase sales, and thus actual revenues, beyond those assumed when rates were last set.
4. The return on equity should be adjusted to reflect reduced capital costs in 1988. Returns on equity now being authorized for Class A water companies with equity ratios in CUCC's range (approximately 68%) are about 12%, whereas the return adopted in 1982 was 13.2%. (See, for example, D.87-09-071, wherein Park Water Company was authorized a return on equity of 12% with an equity ratio of 77.16%.)

While these four factors suggest that a rate decrease may be appropriate in the Montara District, the construction and operation of the new airport well and other factors of which we are

unaware may offset them, in whole or in part. Our staff should study Montara's revenue requirement and recommend an Order Instituting Investigation, if appropriate. To assist the staff we will require CUCC to submit a summary of earnings for the Montara District to CACD concurrently with the filing of any general rate application or advice letter for any other CUCC water operation in California.

Petition for Modification by CUCC

On November 12, 1986, CUCC filed a petition to modify D.86-05-078 by extending the date that the moratorium on further water service connections was to end. The moratorium was to expire on November 28, 1986. On December 12, 1986, Farallon Vista Associates (Associates) filed a protest to CUCC's petition. On December 16, 1986, the ALJ issued a ruling setting aside submission of Phase II to consider CUCC's petition and Associates' protest. The ruling also reflects the agreement of counsel for CUCC and Associates that the moratorium could be extended pending further hearings. On December 17, 1986, the Commission issued D.86-12-069, extending the moratorium on service connections until further order of the Commission.

Public hearings on CUCC's petition and Associates' protest were held in San Francisco on January 13 and 27, 1987, and submitted without argument or briefs. After off-the-record discussions the ALJ ruled from the bench:

"...from the two days of hearings that have taken place regarding the petition for modification, the evidence seems to support the continuation of the restriction indefinitely without a need to impose a further cut-off date or a date when the restriction will end by operation of law.

"So I would propose to the parties that the Commission's current decision, Decision 86-12-069, disposes of the petition to modify the earlier decision of the Commission [D.86-05-078], and that the matter can be



submitted on the basis that Decision 86-12-069 has granted to Citizens the relief that [it] sought in [its] petition for modification.

"Is there any response?" (Transcript 6:448-449.)

CUCC agreed that the matter could be submitted on the above terms. Associates stated no objection. The staff attorney stated the position of the Commission Advisory and Compliance Division, as follows:

"Although we don't condone the continuation of the moratorium on Citizens' service area, we realize that if the moratorium were lifted, it would place additional hardships on the current customers. Therefore, at this point, we really have no further objection." (Transcript 6:449.)

Since D.86-12-069 has, in effect, granted CUCC's petition to extend the moratorium, the following order should so state in order to clear the docket of a pending petition.

Petition of Farallon Vista Associates  
for Exemption from D.86-05-078 and D.86-12-069

On January 25, 1988, Associates filed a petition for exemption from the moratorium imposed by D.86-05-078, as extended by D.86-12-069. Associates allege that they have developed a well that will supply all of the needs of their development. They propose to contribute the well to CUCC, together with associated facilities, in exchange for CUCC's commitment to serve their development. On February 24, 1988, the Water Utilities Branch of the Commission staff filed a timely protest to the petition and requested that public hearings be held. On March 3, 1988, CUCC filed a motion for leave to file a late protest, which was granted by ALJ ruling on March 11, 1988.

By letter dated April 15, 1988, (with copies to the ALJ and the staff) counsel for Associates forwarded to CUCC a proposed Agreement for Transfer of Water Source and Commitment to Serve. Presumably, Associates and CUCC are negotiating about the terms of

that agreement. Public hearings await Associates' advice that they have reached an agreement with CUCC and that they are ready for their petition to be heard.

Regulatory Proceedings Affecting CUCC's  
Plans to Develop Two Wells in the Airport Plain

During July, 1985, CUCC sought permits from San Mateo County to develop two new wells in the airport plain. On February 18, 1986, the County issued a Negative Declaration for the project. On March 20, 1986, the Zoning Administrator approved Use Permit 85-31 and Coastal Development Permit 85-59. The action of the Zoning Administrator was appealed to the Planning Commission, which approved the permits on May 28, 1986. (Exhibit 39.) The action of the Planning Commission was appealed to the Board of Supervisors. On July 8, 1986, the Board denied the appeals and approved the permits, subject to 15 conditions. (Exhibit 26.)

On July 28, 1986, a small group interested in the effect of the wells upon the Pillar Point Marsh filed an appeal of the permits with the California Coastal Commission (CCC). (Exhibit 32.) On August 5, 1986, CUCC filed an appeal with CCC seeking to modify Condition 4 so that it would not conflict with Public Utilities Code Section 453. (Exhibit 33.)

On November 14, 1986, CCC voted 11 to 1 to grant the permit sought by CUCC. The permit limits production of the two wells to 400 acre feet per year and is subject to other conditions. The Notice of Intent to Issue Permit (Exhibit 39) states that:

"The actual development permit is being held in the Commission office until fulfillment of the Special Conditions 1a-d, imposed by the Commission. Once these conditions have been fulfilled, the permit will be issued."

Conditions 1a through 1d are attached as Appendix B to this decision.

From correspondence in the file (copies of CUCC's letters to and filings with the CCC were sent to the ALJ by CUCC at his request) it appears that between April 19 and May 8, 1987, unseasonably warm weather resulted in increased water demand in the Montara District. Demand exceeded productive capacity of the well and surface water sources, resulting in a draw down of stored water. Beginning May 3, 1987, between 100 and 150 customers began to experience temporary low pressure or water outages. CUCC began water hauling on May 1, 1987, and by May 5, 1987, all customers were back in service.

Since Condition 1 of the original CCC permit had not yet been fulfilled, CUCC could not obtain the permit to drill, and thus could not drill, the two proposed wells in the airport plain. On May 22, 1987, CUCC filed with CCC an application seeking to amend its permit to allow the development of a single, temporary community water well. The CCC's staff report, filed May 28, 1987, recommended approval of the amendment with conditions. They are attached hereto as Appendix C.

A letter dated July 8, 1987, from counsel for CUCC to the Director of Environmental Management for the County of San Mateo indicates that the CCC acted favorably on its staff report and amended the permit to allow CUCC to construct one well. That letter requests that the County of San Mateo put into effect a moratorium on issuing building permits in the service area of the Montara District. The CCC staff report had recommended as Condition 6:

"The applicant [CUCC] shall not authorize any new connections and shall petition the San Mateo County Board of Supervisors to similarly reduce the number of building permits within their service area as provided by LCP [Local Coastal Plan] Policy 1.19(b)."

Monthly and quarterly reports filed by CUCC pursuant to D.85-05-042 in OII 83-11-09 state that CUCC obtained the amended permit from CCC and, during August, 1987, constructed and put into service a single well at the Half Moon Bay Airport in accordance with CCC permit No. A-3-SMC-86-155. The October report, dated October 15, 1987, states:

"Water from this additional well became available to our system on August 14, 1987 and has been used virtually continuously since that date."

The same reports state that CUCC is continuing its efforts to comply with the conditions precedent to the issuance of a CCC permit for the construction of a second well at the airport. It has also obtained use permits and coastal development permits from San Mateo County to drill two test wells in the San Vincente Creek area. The County has extended these permits until September, 1988.

Findings of Fact

1. The productive capacity of CUCC's water sources is 383 gpm, including the Montara Spring and the Park Well.
2. The Montara system requires 465 gpm of productive capacity to meet the demand of current customers for reliable service. In addition, to meet the demand of individual lot owners who have applied or will apply for service and the demand of the Farallon Vista Housing Development the system requires at least 550 gpm of productive capacity.
3. The combined current production of the wells added to the system since 1976 does not equal 200 gpm. (Finding 11, D.86-05-078, p. 33.)
4. Reliable well production was between 225 and 264 in 1976 and is now about 300 gpm. (Finding 12, Id.)
5. CUCC has not met the requirement of D.88618 to provide new well capacity of 200 gpm. (Finding 13, Id.)

6. Water from Park Well is blended with water from other sources before it is delivered to customers.

7. The blended water meets all DHS standards applicable to it.

8. The staff's proposed amortization plan would reduce CUCC's rate base to reflect the fact that Portola Wells 1 and 2 are no longer used and useful.

9. CUCC's authorized return on equity is 13.2%.

10. D.86-12-069 granted the relief sought by CUCC in its petition for modification filed November 12, 1986.

11. After a regulatory process that consumed almost 2 years CUCC obtained authority from CCC to construct one new well in the airport plain. The well has been constructed and has been operating since August 14, 1987.

12. By D.87-09-071 the Commission authorized Park Water Company to earn a 12% return on equity. Park's capital structure was 77.16% common equity.

13. CUCC's customers were 1,272 in December, 1979, and are now about 1,600.

14. The four factors listed in the section entitled "Need for a General Rate Proceeding" suggest that a rate decrease may be in order for the Montara District.

#### Conclusions of Law

1. The output of the Park Well should be added to the other water sources in computing productive capacity of the system.

2. This proceeding is not an appropriate vehicle for making rate or rate of return adjustments.

3. It would not be reasonable to reduce rate base to account for the nonoperational status of Portola Wells Nos. 1 and 2 without examining additions and betterments to plant in service that have occurred during the same period, since the adjustment at issue would not affect a major portion of CUCC's rate base and since there are no other extraordinary circumstances justifying such an adjustment between general rate cases.

4. D.86-05-078 should not be modified to allow CUCC to include in the account for discontinued lease payments all costs for CUCC's search for new water supplies.

5. The CUCC proposal to include costs of searching for new water sources in the balancing account established in D.86-05-078 should be denied.

6. A punitive fine imposed by reducing return on equity by 50% would not be appropriate in this proceeding.

7. The following order should grant the CUCC petition for modification filed November 12, 1986, so that our docket may be cleared of a pending petition.

8. CUCC should be required to develop additional water production capacity to bring its total production to 550 gpm, as required by D.86193.

INTERIM ORDER

IT IS ORDERED that:

1. Citizens Utilities Company of California (CUCC) shall submit a summary of earnings for the Montara District to the Commission Advisory and Compliance Division concurrently with any general rate application or advice letter for any other CUCC water operation in California.

2. The petition of CUCC for modification of D.86-05-078 is granted, as set forth in D.86-12-069.

3. CUCC shall continue to explore for, develop, and put into service additional water supply sources until the total supply for its Montara District equals 550 gpm.

4. Phase II of this proceeding, including the water supply issues transferred from OII 83-11-09, is concluded.

This order becomes effective 30 days from today.

Dated September 14, 1988, at San Francisco, California.

STANLEY W. HULETT  
President  
DONALD VIAL  
FREDERICK R. DUDA  
G. MITCHELL WILK  
JOHN B. OHANIAN  
Commissioners

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

*[Signature]*  
Vice President  
Jo

APPENDIX A  
Page 1

Findings of Fact

1. In D.86193 (August 3, 1976) in A.55538 and C.10093 CUCC was ordered to acquire new sources of water for its Montara service area capable of producing at least 200 gpm.

2. On September 21, 1976, CUCC notified the Commission that the Drake well (30-44 gpm) was placed in service.

3. In D.88618 (March 21, 1978) in reopened C.10093 CUCC was ordered to continue its efforts to acquire new sources of water for its Montara service area capable of producing at least 200 gpm.

4. In April, 1979, CUCC placed a new South Airport well #2 in operation replacing South Airport well #1 which had failed. The new well involves a net loss to the system since it produces less than the well it replaces produced at its peak capacity.

5. On December 6, 1979, CUCC in A.59321 requested a temporary moratorium on new service connections in Montara. D.91422 (March 18, 1980) established a limited moratorium.

6. On January 30, 1980, CUCC's witness testified in A.59321 that it had added to its system the four Portola Estates wells producing 200 gpm, of which 130 gpm would be available to CUCC.

7. As early as August 29, 1980, the four Portola Estates wells were producing only 180 gpm, of which CUCC were entitled to two-thirds of 120 gpm.

8. CUCC was entitled to HMBP's remaining one-third interest in the well production according to the terms of a lease dated February 5, 1981. However, HMBP retained the right to demand delivery of one-third of the production of the wells.

9. Portola Estates Well No. 1 failed in 1981. Portola Estates Well No. 2 failed in 1982. Portola Estates Well No. 3 is producing at 35% of its original estimated rate. Portola Estates Well No. 4 is producing at 20% of its original estimated rate.

10. The two Portola wells still operating produce between 33-83 gpm.



APPENDIX A

Page 2

11. The combined current production of the wells added to the system since 1976 does not equal 200 gpm.

12. Four hundred customers have been added to the system since 1976. Storage capacity has increased from 328,000 gallons to 762,000 gallons in this same period. Reliable well production was between 225 and 264 gpm in 1976 and is now about 300 gpm.

13. CUCC has not met the requirement of D.88618 to provide new well capacity of 200 gpm.

14. Increased storage has been principally responsible for the system's ability to provide additional service to 400 new customers since 1976.

15. Water service to current customers is not adequate in that it does not meet the maximum day requirements of GO 103 regarding water supply and fire reserve requirements, also in that it does not provide any reserve margin for possible failure of one of the three major wells serving the system. However, a few more customers, i.e., the six Portola Estate lots and the prospective customers who have obtained commitments from CUCC, may be added to the system, without significantly degrading the service currently enjoyed by the existing customers.

16. The customers identified in finding 15 will not be added to the system simultaneously, but rather over a period that may extend to the end of 1986 or beyond.

17. Any further additions to the customer base will seriously degrade the service to the existing customers unless additional water supplies become available.

18. CUCC's Supplemental Agreement with HMBP is advantageous to CUCC, will give CUCC a legal right to additional water supplies and may make available other HMPBP well sites to CUCC for exploration.

19. In D.85-06-042 (June 5, 1985) in OII 83-11-09 we ordered CUCC to proceed with all due diligence to develop and place in operation no later than June 1, 1986, new water supply sources or storage facilities, or both, sufficient to supply existing customers and new customers as they require connection.

(END OF APPENDIX A)

Recommended Conditions

- ADOPTED
1. (a) PRIOR TO THE TRANSMITTAL OF THE PERMIT, a study to determine the safe yield of the Denniston sub-unit of the Half Moon Bay Aquifer shall be completed by a qualified hydrogeologist and biologist. The study shall include an inventory of existing groundwater extraction, recharge rate which includes streamflow figures for Denniston Creek from stream gauges placed in the the upper and lower courses and monitored at regular intervals, and any other information required to produce a thorough study including recommendations for the protection of habitat values as required by the policies of the San Mateo County Local Coastal Program. The proportional costs of the study shall be based upon the average annual water usage of each participant.

ADOPTED

The study shall be submitted to the Executive Director for review and determination that it meets the requirements of Condition 1(a) and the Local Coastal Plan Policies 2.32 and 7.20. Copies of the study shall be provided at the same time to the appellants, the local government, and operators of other wells in the vicinity of the two proposed wells.

ADOPTED

(c) The Executive Director, after having determined that the study is adequate, shall prepare a report to the Commission recommending final pumping rates and conditions of operation for the proposed wells based on the approved study and (1) consistent with LCP policies regarding groundwater extraction and habitat protection, and (2) sufficient to prevent interference with other existing wells in the area. The Executive Director shall send copies of the report to the appellant, the local government, and operators of other wells in the area.

ADOPTED

(a) The Commission shall establish final pumping rates and conditions of operation based on the study, the Executive Director's report, and other evidence submitted at a public hearing. All parties which received a copy of the Executive Director's report shall be permitted to testify at the hearing.

- ADOPTED
2. Prior to the connection of any water supplies to Citizen's Utility Company customers from the wells allowed by this permit, applicant shall provide an additional 200,000 gallons of water storage, in a tank or tanks, for emergency or peak demand use. A Coastal Development Permit for the tank or tanks must be secured from San Mateo County prior to installation.

A-3-SMC-86-155 CITIZEN'S UTILITY COMPANY OF AMERICA Page 5b

Recommended Conditions (Continued)

3. Applicant shall comply with the following conditions attached to the permit by San Mateo County; Conditions numbers 2, 3, 4, 5, 6, 10, 11, 12, 13, 14, and 15 (Board of Supervisors Approval July 1986, see Exhibit 1).

RECOMMENDED FINDINGS

The Commission finds and declares as follows:

A. PROJECT DESCRIPTION

The proposed project involves the development of two community water wells to serve Citizen's Utilities customers. The wells are to be located at the Half Moon Bay Airport, west of Highway One, between the highway and the airport service buildings. The County has conditioned the permit to allow a maximum withdrawal of 400 acre feet a year from the wells until hydrological/biological studies are completed. The proposed wells are located in the Denniston sub-unit of the Half Moon Bay Aquifer. Nearby existing wells include CUC North Airport well (approximately 450' distant); Coastside Community Water District's wells, approximately 1/4 mile to the south; and, a couple of private wells to the west. (Please see Exhibit 4 for well locations in the Airport Area.) The proposed wells are also approximately 1,800 to the north-east of Pillar Point Marsh and approximately 1,500 feet from Denniston Creek (Exhibit 5).

(END OF APPENDIX B)

A-3-SMC-86-155 CITIZENS UTILITIES CO. OF CALIFORNIA Page 2

STAFF RECOMMENDATION

The Staff recommends that the Commission adopt the following Resolution:

Approval with Conditions

The Commission hereby grants, subject to the conditions below, a permit for the proposed development on the grounds that the development, as conditioned, will be in conformity with the provisions of Chapter 3 of the California Coastal Act of 1976, will not prejudice the ability of the local government having jurisdiction over the area to prepare a Local Coastal Program conforming to the provisions of Chapter 3 of the Coastal Act, is located between the sea and the first public road nearest the shoreline and is in conformance with the public access and public recreation policies of Chapter 3 of the Coastal Act, and will not have any significant adverse impacts on the environment within the meaning of the California Environmental Quality Act.

RECOMMENDED CONDITIONSStandard Conditions

See Exhibit A.

Special Conditions

1. PRIOR TO TRANSMITTAL OF THE PERMIT, the applicant shall demonstrate, to the satisfaction of the Executive Director, that they are unable to purchase water from Coastside Community Water District, either from CCWD's own supply or from supplies purchased from the City of San Francisco.
2. PRIOR TO TRANSMITTAL OF THE PERMIT, the applicant shall provide the following information to the satisfaction of the Executive Director:
  - (a) An analysis of why CUC water use rates are above the norm. Analysis shall include recent (1986-1987) meter figures for homes and production figures for wells for the same period.
  - (b) A program to substantially reduce domestic water use and/or repair leaking pipes depending on the recommendations of the analysis prepared to satisfy Condition 2(a). The program, subject to the approval of the Executive Director, shall be implemented upon approval. Progress reports on the effectiveness of the

program shall be submitted on a monthly basis to the Executive Director. Failure to effectively implement the program or to provide Progress Reports shall be grounds for the revocation of this permit.

3. The applicant shall immediately seek permits to construct the storage required by Condition #2 of the original permit. The new storage facility shall be completed and available for service within 120 days of acceptance of this permit.

4. Drilling of a temporary (one year from date of installation) well at the Airport site may only be permitted if the applicant is unable to secure water supplies from CCWD and the program for reducing water use is ineffective in bringing use rates down to the level of the production rates of the existing water sources after one month's operation. Use of the well is limited to periods of peak demand and only in the amount necessary to prevent the disruption of service while maintaining a minimum of 450,000 gallons in storage for fire flows. Reports of the time and amount of withdrawal from this well shall be submitted to the Executive Director within five days of each use.

5. Prior to installation of the proposed water well, the applicant shall submit for Executive Director's review and approval after review by the California Department of Fish & Game a:

- a. Monitoring Program outline for Pillar Point Marsh prepared by a qualified biologist
- b. The monitoring program shall be designed to assess the potential adverse impacts that the water withdrawal from the temporary well will have on the marsh habitat.
- c. Monitoring data shall be collected prior to the well installation, during the time of well use, and up to one year after the well is abandoned, and
- d. The methodology, frequency and type of data collection, and the location of data transects shall be defined in the outline after consultation with the California Department of Fish and Game.

6. The applicant shall not authorize any new connections and shall petition the San Mateo County Board of Supervisors to similarly reduce the number of building permits within their service area as provided by LCP Policy 1.19(b). New connections may be authorized upon demonstration to the County and the Coastal Commission that adequate, new water supplies exist to serve the proposed number of new connections.

(END OF APPENDIX C)

## APPENDIX D

Citizens Utilities Company of California  
Montara District

## AMORTIZATION OF PORTOLA WELLS #1 AND #2

## Plant and Depreciation Rate

:Line:		: Land :	Well :	Structure:	Pumps :	
: No.:	Item	: Ac. 306 :	Ac. 325 :	Ac. 321 :	Ac. 324:	Total :
1	Portola #1	\$ 9,175	\$19,413	\$ 2,774	\$ 5,709	\$37,071
2	Portola #2	9,175	19,413	2,760	4,503	35,851
3	Total	\$18,350	\$38,826	\$ 5,534	\$10,212	\$72,922
4	Depreciation Rates	None	3.36%	3.02%	5.15%	-
5	Monthly Accrual		109	14	44	167

:Line:	Item	: 1982* :	1983 :	1984 :	1985 :	1986 :	Total:
		(a)	(b)	(c)	(d)	(e)	(f)
6	Plant	\$72,922	\$72,922	\$72,922	\$72,922	\$72,922	
7	Depr. Reserve	1,165	3,163	5,161	7,159	7,991	
8	Net Plant	\$71,757	\$69,759	\$67,761	\$65,763	\$64,931	
9	Wgtd. Avg. Plant	72,340	70,758	68,760	66,749	65,347	
10	Rate of Return	2.71%	11.80%	13.29%	13.51%	13.51%	
11	Earnings	1,144	8,349	9,138	9,018	3,678	
12	Taxes	1,209	8,822	9,656	9,529	3,886	
13	Depreciation	1,165	1,998	1,998	1,998	832	
14	Excess Lease Costs**	1,400	1,968	2,841	4,207	1,753	
15	Ratepayer Cost	\$ 4,918	\$21,137	\$23,133	\$24,752	\$10,149	\$84,089
16	Cost of Well						72,922
17	Negative balance to be amortized over three years						(11,167)

\* 7-month period 1982; 5-month period 1986.

\*\* Amount of the lease in D.82-05-076, less amount actually paid.

(END OF APPENDIX D)

APPENDIX E

Adopted Cost of Capital from D.82-02-059 in A.60132 (Sacramento County Water District of Citizen Utilities Company of California)

<u>Component</u>	<u>Component Weight</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Long-term Debt	32.0%	9.57%	3.06%
Common Stock	68.0%	13.20%	8.98%
Rate of Return			12.04%

Effect of Staff's Proposed Reduction in Cost Rate for Common Equity from 13.20% to 6.60%

<u>Component</u>	<u>Component Weight</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Long-term Debt	32.0%	9.57%	3.06%
Common Stock	68.0%	6.60%	4.49%
Rate of Return			7.55%

Dollar Effect of Staff Proposed Reduction

$$12.04\% \times \$1,564,800^* = \$188,401.92$$

$$(\text{Minus}) \quad 7.55\% \times \$1,564,800^* = \$118,142.40$$

$$\$ 70,259.52 \text{ (Annual Penalty)}$$

\* Average depreciated rate base for 1985 (Exhibit 22, Appendix B, Sheet 1 of 2, line 24.)

(END OF APPENDIX E)

or rate of return adjustments are appropriate in this type of proceeding.

Neither party cites the underlying application proceeding as the basis for ratemaking adjustments. It would clearly not be appropriate to use an application under Public Utilities (PU) Code § 2708 as a vehicle for revising, amending, or modifying the rates of a public utility. Rather, both the staff and CUCC cite OII 83-11-09 as a source of the Commission's authority, if any, to adjust rates in this proceeding.

The staff in particular cites Paragraphs 4(e), 4(g), and 6 of OII 83-11-09 in support of the Commission's authority to adjustment rates in in this proceeding. The relevant parts of Paragraph 4 of OII 83-11-09 are as follows:

"4. This investigation will consider:"

\* \* \*

"e. Whether CUCC or its subsidiaries acted in an imprudent manner in the management and development of their Spring and Well resources and watershed lands. This investigation will consider the appropriate ratemaking mechanism(s) and orders if the Commission determines that CUCC or its subsidiaries have been imprudent in the management of the utilities' water sources. We invite the Cal. Dept. of Health Services or any other party to submit evidence on water quality issues which may be relevant to this investigation."

\* \* \*

"g. Whether any other order or orders should be issued by this Commission in the exercise of its jurisdiction."

\* \* \*

"6. The Commission hereby puts each respondent on notice that other rate cases for CUCC's other districts or subsidiaries may be



evidence on because this is not a general rate case. The resolution of those issues will, according to CUCC, have a decisive impact on water rates in Montara.

In OII 83-11-09 both the Commission and the staff contemplated that ratemaking changes due to the issue of timber harvesting revenues would be likely for the Guerneville District. Accordingly, we consolidated that investigation proceeding with A.60220, the most recent general rate proceeding of the Guerneville District. For other districts of CUCC, where ratemaking adjustments were deemed less likely, we merely included in our OII a notice that other rate cases for CUCC's other districts or subsidiaries may be reopened and consolidated with this proceeding if the Commission finds it appropriate.

Neither the staff nor any other party to this proceeding has filed a motion to consolidate the most recent general rate proceeding of the Montara District with OII 83-11-09 or with this application proceeding. Consequently, there is no backdrop against which the staff's proposed ratemaking adjustments may be viewed. In the case cited by CUCC in its brief the Commission stated: "...as a matter of diligent ratemaking practice it is most desirable to examine a utility's total operations before increasing [or decreasing] rates." (Southern California Edison Co. (1977) 81 CPUC 749, 750.)

As a general rule it is desirable to consider a utility's total operations before adjusting rates. Thus, the bulk of the Commission's ratemaking business is conducted in general rate proceedings where all elements of the company's operations can be considered. An exception to this rule is frequently made in offset cases of one kind or another. Where a single factor in a company's results of operations is significant, the Commission may and frequently does consider it in isolation. For instance, energy costs for electric corporations are considered in energy cost adjustment clause proceedings; the cost of natural gas for gas

corporations is considered in gas adjustment clause proceedings; and major additions to the rate base of a public utility are frequently considered in rate base offset proceedings.

We do not have before us in this proceeding either a general rate proceeding or a traditional offset case. The staff's proposed rate base adjustment does not result from a major change in rate base nor is it considered in the context of other rate base adjustments made necessary by events taking place in this utility since the last general rate proceeding, as would be the case in a general rate proceeding. It would be extremely difficult, if not impossible, for the Commission to balance the consumer and investor interests (Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591, 603) where one event affecting rate base is not considered with all events affecting rate base over a given period of time.

Based upon the foregoing discussion we do not believe that this proceeding is an appropriate vehicle for making rate or rate of return adjustments. Although our answer to issue 2A would seem to make it unnecessary to consider the specific staff proposals, we will nevertheless discuss the staff proposed adjustments individually. In doing this we will not consider Ratemaking Issue 2B separately, since it consists merely of a general statement that encompasses the three individual issues 2C, 2D, and 2E.

Ratemaking Issue 2C

Is the Staff Proposal for Retirement  
of the Portola Wells Appropriate?

Staff recommends that Portola Wells 1 and 2 be retired from the rate base of the Montara District. The facts upon which the staff recommendation is based are not in dispute. In February 1980 CUCC purchased the four Portola Wells from Half Moon Bay Properties (HMBP). Portola Well No. 1 failed in 1981 and Portola Well No. 2 failed in early 1982. Portola Wells 1 and 2 have

remained inoperative since 1981 and 1982, respectively. Staff contends that the wells should be removed from rate base because they are no longer used and useful. According to the staff, the ratepayers have been paying depreciation, taxes, and a return on these wells, which have not benefitted the ratepayers since they became inoperative. The staff cites D.85-08-046 in PG&E A.83-09-49 in support of the proposition that plant which ceases to be used and useful should be excluded from rate base.

In Exhibit 22, Appendix D, the staff sponsored an amortization plan which it testified would permit CUCC to recover its cost of the Portola Wells 1 and 2 without earning a return on the wells. The staff cites in support of its amortization plan SDG&E (1979) 1 CPUC 2d 644. We have attached a copy of Appendix D to this opinion in which the staff has calculated the historical cost of the two Portola Wells in question at \$72,922. The staff has also calculated the amounts that the ratepayers have paid in earnings, taxes, depreciation, and lease costs during the period 1982 to 1986. The total ratepayer cost based on these calculations is \$84,089. The historical cost of the wells is then subtracted from the cost paid by the ratepayers through rates and the balance of \$11,167 is, according to the staff recommendation, to be amortized over three years to the benefit of the ratepayer.

CUCC contests the staff's proposal concerning Portola Wells 1 and 2, arguing that even if this proceeding was a proper one for general rate adjustments, it is clear that the staff's ratemaking proposal for amortization of some of the costs of Portola Wells Nos. 1 and 2 is not appropriate because it would involve retroactive ratemaking. CUCC states that the ratemaking authority of the Commission is derived from PU Code § 728, which provides, in relevant part:

"Whenever the Commission, after a hearing, finds that the rates...collected by any public utility for or in connection with any service ...are insufficient, unlawful, unjust, [or] unreasonable...the Commission shall determine

and fix, by order, the just, reasonable or sufficient rates...to be thereafter observed and in force."

CUCC states that the California Supreme Court, citing § 728, has held that the Commission has power to fix rates only prospectively, not retroactively. In PT&T v. PUC (1965) 62 Cal. 2d 634, 649-652 the court held:

"The fixing of a rate in the first instance is prospective in its application and legislative in its character. Likewise the reducing of that rate would be prospective in its application and legislative in its character."

CUCC contends that the practical significance of the prohibition against retroactive ratemaking is that when this Commission fixes the rates a utility may charge by a final, valid order, amounts collected by the utility pursuant to that order are conclusively proper and are not subject to retroactive adjustment by subsequent action. (City of Los Angeles v. PUC (1972) 7 Cal 3d, 331, 338, 356, 359.) According to CUCC, if this Commission were to believe that amounts previously collected pursuant to a valid tariff were excessive, the only recourse available would be to hold a formal rate hearing, consider the evidence on all relevant factors and, if the evidence supported it, set lower rates for the future. It would not be appropriate to order refunds of amounts collected pursuant to the prior tariff. (PT&T v. PUC (1965) 62 Cal 2d, 634, 649, 656.)

It is clear from the contents of Appendix D and from the testimony of the staff witness on cross-examination that the staff's proposed amortization is actually a refund of \$11,167 to the ratepayers of revenues previously collected by CUCC through rates that have been approved and authorized by the Commission. Since the amounts identified in Appendix D have already been collected pursuant to a final order of the Commission, an order to refund such amounts would constitute retroactive ratemaking contrary

to the holdings of the California Supreme Court in the above-cited cases, as such an order would not appear to fall within any of the exceptions to the rule against retroactive ratemaking discussed in subsequent California Supreme Court cases such as Southern California Edison Co. v PUC (1978) 20 Cal. 3d 813).<sup>2</sup>

Even if the staff's amortization proposal were lawful, CUCC alleges that it is otherwise flawed in the following respects:

1. It treats all amounts recovered as capital recovery, when in fact some amounts went for taxes, lease costs, and cost of capital (return);
2. The staff's calculations do not use the correct rates of actual return, so they do not show amounts actually earned by CUCC on the investment in Portola Wells Nos. 1 and 2;
3. The staff witness used an incorrect multiplier for the income tax conversion;
4. The staff has not reflected the earnings lost by CUCC between the time of the installation of the wells and the effective date of the rate order that included them in rate base; and
5. The staff does not offset any operating expenses incurred by CUCC which were not included in the test year expenses used to set rates for Montara.

Since we have already concluded that the staff amortization plan is barred by retroactive rulemaking considerations, we need not discuss or make findings on the other points raised by CUCC. However, they do illustrate the problems encountered when the test year method of ratemaking is set aside

---

<sup>2</sup> Because the staff did not file a closing brief, it did not respond to the arguments on brief of CUCC on the issue of retroactive ratemaking.

and a plant-item by plant-item approach is used in determining the appropriate rate base for ratemaking purposes. During the period between one decision in a general rate proceeding and another for the same company, we assume that certain plant items will be retired, for obsolescence or other reasons, and that simultaneously other plant items will go into service by becoming operational plant facilities. If it is deemed appropriate to examine the rate base of a public utility between general rate proceedings, then all appropriate adjustments to rate base should be examined to account for both additions and retirements. Instead, the staff in this proceeding has examined Portola Wells Nos. 1 and 2, which have gone out of service in the period between general rate cases, but has not examined the additions and betterments to plant that have occurred in the same period. It would not be reasonable to reduce rate base prospectively to account for the nonoperational status of Portola Wells Nos. 1 and 2 without examining additions and betterments to plant in service that have occurred during the same period.

Citations by the staff to D.85-08-046 in PG&E A.83-09-49 and to SDG&E (1979) 1 CPUC 2d 644 are not helpful to the staff's position. D.85-08-046 was cited for general language on the concept of used and useful utility plant in rate base. That decision was issued in PG&E A.83-09-49, which sought authority to increase electric rates to reflect retirement and decommissioning costs of Humboldt Bay Power Plant, Unit 3. In that rate proceeding PG&E sought \$86,086,000 of additional revenue. The Commission authorized the utility to collect \$52,910,000, which it found to be the prudently incurred direct cost of retiring Humboldt Bay Power Plant, Unit 3. The Commission disallowed \$33,176,000 of accrued allowance for funds used during construction. The staff has not demonstrated how the PG&E decision is similar and thus should govern any decision arising out of this proceeding.

Ratemaking Issue 2D

Is the Staff Proposal for Treatment  
of Terminated Lease Payments to  
Half Moon Bay Properties Appropriate?

During hearings in Phase I, CUCC stipulated that lease payments that are now a part of its revenue requirement in the amount of \$9,600 per year may be treated as a deferred credit and accumulated in a balancing account with interest until the next

In like manner the staff's citation of the 1979 SDG&E decision provides no assistance. That decision arose out of a general rate proceeding. The matter quoted by the staff in its brief pertained to the rate treatment of certain costs associated with the abandoned Sundesert Project. The paragraph quoted by the staff contains the following sentence, which we assume is the point the staff wished to emphasize: "We believe that adherence to our past practice of allowing recovery of abandonment costs from ratepayers while denying rate base treatment is an equitable solution to a difficult problem." Again, the factual situation involved in the SDG&E case is dissimilar to that with which we are faced in this proceeding. In SDG&E we addressed the issue of the treatment for ratemaking purposes of plant that was never in rate base and that had to be abandoned. In this case we are faced with plant that is in rate base which has become prematurely obsolescence due to failure of the wells. In addition the SDG&E case was a general rate proceeding, whereas this proceeding is an investigation proceeding the scope of which did not encompass a general inquiry into the entire operative plant of the utility nor the entire results of operations of the utility. Finally, the SDG&E case did not involve refunds of revenues obtained from lawful rates, as is the case with the staff proposal in this instance.

For the reasons that we have discussed we will not adopt the staff's recommendation for a refund of \$11,167 to be amortized by reducing rates over a 3-year period.

Ratemaking Issue 2D

Is the Staff Proposal for Treatment  
of Terminated Lease Payments to  
Half Moon Bay Properties Appropriate?

During hearings in Phase I, CUCC stipulated that lease payments that are now a part of its revenue requirement in the amount of \$9,600 per year may be treated as a deferred credit and accumulated in a balancing account with interest until the next



general rate proceeding of the Montara District. At that time, the amount accumulated may be used to reduce CUCC's future revenue requirement. Based on that stipulation, the Commission ordered CUCC to establish a memorandum deferred credit account and to accumulate \$800 per month representing the lease payments on the Portola Wells, with interest at 7%, until the next rate proceeding for Montara. (D.86-05-078, Ordering Paragraph 9.)

In Phase II the staff proposed to reflect in rates the termination of charges paid by CUCC for the lease back of HMBP's share of the water from the Portola Wells. Since CUCC is no longer paying these charges, having purchased HMBP's interest in the Portola Wells, the staff believes that rates should be reduced to reflect this decrease in expense.

This issue involves expenses of about \$9,000 per year, which the Commission has already considered in its decision on Phase I. Pursuant to CUCC's stipulation, we ordered CUCC to establish an account and to accumulate these expenses for later amortization, with interest, to the benefit of the ratepayers. That disposition will fully protect the interests of the ratepayers and will not involve us in item-by-item rate adjustments between general rate proceedings.

During Phase II, a witness for CUCC testified that the balancing account established in D.86-05-078, as described in the preceding paragraph, should contain, in addition to the accumulation of the discontinued monthly lease payments, the accumulation of costs incurred in the search for the new water sources. Once the search is completed, according to the witness, the charges can be removed from the balancing account and recorded in plant if the search is successful or offset against the lease payments. The remainder of the balancing account can then be handled in Montara's next general rate proceeding. CUCC continues to advocate the same position through its brief.

In its brief the staff opposes the proposal by CUCC. The staff points out that expenses incurred by CUCC in its search for new sources of water should be capitalized and should become a part of the rate base in the next general rate proceeding of CUCC.

It would therefore be inappropriate to offset costs that will be capitalized against the expense items that are accumulating as credits for the benefit of the ratepayers in the balancing account established in D.86-05-078. Accordingly, we will deny the request of CUCC for balancing account treatment of costs incurred in the search for new water sources.

Rate-making Issue 2E

Should the Company's Rate of Return  
Be Reduced and if so, by What Amount?

The staff recommends that the Commission reduce the allowable rate of return on equity from 13.2% to 6.6% thereby reducing the overall rate of return from 12.04% to 7.55%. The staff further recommends that the lower return on equity should remain in effect until such time as CUCC complies with the order in D.86193 (1976) to increase water production capacity to at least 550 gpm. The staff's recommendation is based on CUCC's consistent failure to develop additional supplies of water. As a consequence of this failure CUCC has applied for and received an order imposing restrictions on connection of new customers. (D.86-05-078.) Staff requests that a penalty be imposed on CUCC to provide an incentive for its shareholders to provide reasonable water supplies to its customers. In support of its rate of return penalty recommendation the staff cites General Telephone Company of California, 4 CPUC 2d 428, wherein the Commission reduced General Telephone's rate of return because of inadequate service. Staff requests similar treatment for CUCC in this proceeding because of its failure to provide reliable water supplies to its customers.

CUCC responds that the staff has not demonstrated that the development of the Portola Wells or any other source was

imprudent. Rather, according to CUCC, the evidence shows that CUCC was justified in believing that the Portola Wells would satisfy customer demands for service, but that those sources did not produce as reliably as expected. CUCC asserts that as it became aware that the Portola Wells would not provide adequate supplies, CUCC has continued its efforts to identify and develop other prospective sources. These efforts have included the retention of expert hydrologists and negotiations with Half Moon Bay Properties, the area's largest landowner to obtain additional sites. CUCC has also been seeking the agreement of the County of San Mateo and necessary permits to develop two new wells at Half Moon Bay Airport, the most promising location for the development of new supplies. CUCC believes that there is no basis in this record for penalizing CUCC by reducing its rate of return.

The staff cites General Telephone Company of California, 4 CPUC 2d 428, in support of its request that CUCC's rate of return be reduced. The General proceeding was a general rate case in which all the elements of the company's operations were examined. In the decision in that proceeding the Commission examined the company's capital structure and costs of capital in detail and concluded that the cost factor for common equity was 14.10%. That cost factor, taken together with cost factors for other parts of the capital structure, and weighted in accordance with the adopted capital structure percentages, resulted in a rate of return of 10.58%. The Commission also examined in that proceeding service deficiencies in General's operations that had caused a multitude of customer complaints. To give General an incentive to take concerted and effective measures to substantially improve its level of service the Commission reduced the authorized return on equity by 0.50% to 13.60%. This adjustment reduced the revenue requirement for General by \$7.4 million. The Commission added that if General showed that its service had been improved to a satisfactory level, the Commission would consider adjusting rates

to provide General with an opportunity to earn a 14.10% return on equity. However, the penalty was to be removed no earlier than December 31, 1981. The order was signed and effective October 22, 1980, indicating that the penalty would be in effect for approximately 14 months, assuming that General could show improved service within that period.

There are several major distinctions between the General case and this proceeding. First, the reduction in return on equity ordered in the General case occurred in a general rate proceeding, where all aspects of the company's operations and service were examined and an appropriate balance could be arrived at between the interests of the ratepayer and the interests of the utility shareholders. Second, the reduction in return on equity in the general case was not punitive but rather reflected the Commission's evaluation of the level of service provided by General to its customers. In contrast, the proposal in this case is to reduce return on equity by 50%. Third, the Commission placed a limit on the time during which rates would be reduced to reflect inadequate service. The staff made no such proposal in this case. Fourth, the authorized return on equity, after deducting 0.50% percentage point from the adopted cost factor for common equity of 14.10%, still yielded a 13.60% return on common equity. This value was within the range of recommendations made by the expert witnesses who testified on the subject of cost of capital.

The staff recommendation made in this proceeding to reduce return on equity from 13.2% to 6.6% is not made within the context of an overall study of the cost of capital of CUCC. Moreover, such a reduction of return on equity would produce a penalty of \$70,260 per year.<sup>3</sup> A penalty of this magnitude is

---

<sup>3</sup> See Appendix E for derivation of this number.

proposed at a time when the development of additional water supplies is the primary task of this public utility. Since the development of such supplies is at least in part a function of the availability of funds to use for exploration, test well drilling, and development of new wells, it seems inappropriate to us that such a significant fine is proposed at this juncture. Accordingly, we will not adopt the staff proposal.

However, we do believe that some penalty should be assessed to CUCC for its failures to timely develop the water supplies that are urgently needed for this system. Within the context of a general rate increase application or a general investigation of the rates, operations, and services of the Montara District a more finely tuned rate of return reduction, similar to the one exacted in the General Telephone case, would be appropriate in our view.<sup>4</sup>

#### Need for a General Rate Proceeding

The last general rate proceeding for the Montara District was A.60253. In that case, based on a 1982 test year, the Commission found that a revenue increase of \$388,900 or 162.8% was necessary. However, this was reduced by a \$106,100 offset rate increase granted by Resolution W-2809, dated March 17, 1981. The revenue increase was further reduced for 1982 to \$168,700, pursuant to the Commission's policy of holding rate increases in one year to 50%. The Commission authorized the collection of the revenue

---

<sup>4</sup> The staff proposal to reduce return on equity from 13.2 to 6.6% is in fact an attempt to exact a punitive fine from CUCC for its failure to obey the orders of the Commission. Such punitive fines are ordinarily sought through enforcement proceedings initiated by OII or OSC, wherein due notice of the general orders, orders, rules, regulations, or statutes violated and of the penalties sought by the staff are given in writing to the respondent public utility. Even a liberal interpretation of the language of OII 83-11-09 could not convert it into an enforcement proceeding for the Montara District.

deficiency (\$146,300, including interest) to be deferred to 1983 and 1984. (D.82-05-076, page 3.)

The Commission based much of its decision in the Montara case on companion decisions arising out of CUCC's Sacramento District (D.82-02-059) and Guerneville District (D.82-03-023) rate increase applications. Accordingly, the discussion and findings in D.82-05-076 were abbreviated. However, the Commission found that an overall rate of return of 12.04% was reasonable, with a return on equity of 13.2%. In addition, the Commission stated:

"... Water quality and system condition at Montara have been improved in the last half decade, and further upgrading of the system is contemplated in Montara's construction budget.

"The enormity of the present rate application stems in large part from the fact that Montara has expended approximately \$878,706 of [CUCC's] funds in completing ordered construction programs in the water district in the last five years. This amounts to about \$685 per customer. During this time there have been no substantial rate increases granted to Montara, with the exception of the offset increase granted March 17, 1981 by Resolution W-2809." (D.82-05-076, page 8.)

In Finding 6 the Commission found that:

"Montara's level of water service is adequate." (Id., page 11.)

There was no discussion of the issue of water supply and no mention of the Commission's prior orders requiring CUCC to provide 200 gpm of additional well production.

Finally, the Commission stated at page 8 that the Montara District had 1,272 customers. The source of the 1272 figure is CUCC Exhibit 7, page 16. The figure represents the number of commercial customers as of December, 1979.

The need for a general rate proceeding is indicated by the following factors:

1. Rate base should be adjusted to reflect the failure of two Portola wells, discussed above.
2. Lease expense should be adjusted to reflect the elimination of lease payments to HMBP and to amortize over a future period the accrued credits, discussed above.
3. Revenues should be adjusted to reflect an increase in customers from 1272 to 1599 or 26%. (CUCC's monthly report for April, 1988.) CUCC's customers have recently reached a high of 1610, based on the monthly report for January, 1988. The increase in customers since 1979 tends to increase sales, and thus actual revenues, beyond those assumed when rates were last set.
4. The return on equity should be adjusted to reflect reduced capital costs in 1988. Returns on equity now being authorized for Class A water companies with equity ratios in CUCC's range (approximately 68%) are about 12%, whereas the return adopted in 1982 was 13.2%. (See, for example, D.87-09-071, wherein Park Water Company was authorized a return on equity of 12% with an equity ratio of 77.16%.)

While these four factors suggest that a rate decrease may be appropriate in the Montara District, the construction and operation of the new airport well and other factors of which we are unaware may offset them, in whole or in part. Our staff should study Montara's revenue requirement and recommend an Order Instituting Investigation, if appropriate. To assist the staff we will require CUCC to submit a summary of earnings for the Montara District to CACD concurrently with the filing of any general rate application or advice letter for any other CUCC water operation in California.

Petition for Modification by CUCC

On November 12, 1986, CUCC filed a petition to modify D.86-05-078 by extending the date that the moratorium on further

water service connections was to end. The moratorium was to expire on November 28, 1986. On December 12, 1986, Farallon Vista Associates (Associates) filed a protest to CUCC's petition. On December 16, 1986, the ALJ issued a ruling setting aside submission of Phase II to consider CUCC's petition and Associates' protest. The ruling also reflects the agreement of counsel for CUCC and Associates that the moratorium could be extended pending further hearings. On December 17, 1986, the Commission issued D.86-12-069, extending the moratorium on service connections until further order of the Commission.

Public hearings on CUCC's petition and Associates' protest were held in San Francisco on January 13 and 27, 1987, and submitted without argument or briefs. After off-the-record discussions the ALJ ruled from the bench:

"...from the two days of hearings that have taken place regarding the petition for modification, the evidence seems to support the continuation of the restriction indefinitely without a need to impose a further cut-off date or a date when the restriction will end by operation of law.

"So I would propose to the parties that the Commission's current decision, Decision 86-12-069, disposes of the petition to modify the earlier decision of the Commission [D.86-05-078], and that the matter can be submitted on the basis that Decision 86-12-069 has granted to Citizens the relief that [it] sought in [its] petition for modification.

"Is there any response?" (Transcript 6:448-449.)

CUCC agreed that the matter could be submitted on the above terms. Associates stated no objection. The staff attorney stated the position of the Commission Advisory and Compliance Division, as follows:

"Although we don't condone the continuation of the moratorium on Citizens' service area, we realize that if the moratorium were lifted, it would place additional hardships on the current customers.



Therefore, at this point, we really have no further objection." (Transcript 6:449.)

Since D.86-12-069 has, in effect, granted CUCC's petition to extend the moratorium, the following order should so state in order to clear the docket of a pending petition.

Petition of Parallon Vista Associates  
for Exemption from D.86-05-078 and D.86-12-069

On January 25, 1988, Associates filed a petition for exemption from the moratorium imposed by D.86-05-078, as extended by D.86-12-069. Associates allege that they have developed a well that will supply all of the needs of their development. They propose to contribute the well to CUCC, together with associated facilities, in exchange for CUCC's commitment to serve their development. On February 24, 1988, the Water Utilities Branch of the Commission staff filed a timely protest to the petition and requested that public hearings be held. On March 3, 1988, CUCC filed a motion for leave to file a late protest, which was granted by ALJ ruling on March 11, 1988.

By letter dated April 15, 1988, (with copies to the ALJ and the staff) counsel for Associates forwarded to CUCC a proposed Agreement for Transfer of Water Source and Commitment to Serve. Presumably, Associates and CUCC are negotiating about the terms of that agreement. Public hearings await Associates' advice that they have reached an agreement with CUCC and that they are ready for their petition to be heard.

Regulatory Proceedings Affecting CUCC's  
Plans to Develop Two Wells in the Airport Plain

During July, 1985, CUCC sought permits from San Mateo County to develop two new wells in the airport plain. On February 18, 1986, the County issued a Negative Declaration for the project. On March 20, 1986, the Zoning Administrator approved Use Permit 85-31 and Coastal Development Permit 85-59. The action of the Zoning Administrator was appealed to the Planning Commission, which

approved the permits on May 28, 1986. (Exhibit 39.) The action of the Planning Commission was appealed to the Board of Supervisors. On July 8, 1986, the Board denied the appeals and approved the permits, subject to 15 conditions. (Exhibit 26.)

On July 28, 1986, a small group interested in the effect of the wells upon the Pillar Point Marsh filed an appeal of the permits with the California Coastal Commission (CCC). (Exhibit 32.) On August 5, 1986, CUCC filed an appeal with CCC seeking to modify Condition 4 so that it would not conflict with Public Utilities Code Section 453. (Exhibit 33.)

On November 14, 1986, CCC voted 11 to 1 to grant the permit sought by CUCC. The permit limits production of the two wells to 400 acre feet per year and is subject to other conditions. The Notice of Intent to Issue Permit (Exhibit 39) states that:

"The actual development permit is being held in the Commission office until fulfillment of the Special Conditions 1a-d, imposed by the Commission. Once these conditions have been fulfilled, the permit will be issued."

Conditions 1a through 1d are attached as Appendix B to this decision.

From correspondence in the file (copies of CUCC's letters to and filings with the CCC were sent to the ALJ by CUCC at his request) it appears that between April 19 and May 8, 1987, unseasonably warm weather resulted in increased water demand in the Montara District. Demand exceeded productive capacity of the well and surface water sources, resulting in a draw down of stored water. Beginning May 3, 1987, between 100 and 150 customers began to experience temporary low pressure or water outages. CUCC began water hauling on May 1, 1987, and by May 5, 1987, all customers were back in service.

Since Condition 1 of the original CCC permit had not yet been fulfilled, CUCC could not obtain the permit to drill, and thus

could not drill, the two proposed wells in the airport plain. On May 22, 1987, CUCC filed with CCC an application seeking to amend its permit to allow the development of a single, temporary community water well. The CCC's staff report, filed May 28, 1987, recommended approval of the amendment with conditions. They are attached hereto as Appendix C.

A letter dated July 8, 1987, from counsel for CUCC to the Director of Environmental Management for the County of San Mateo indicates that the CCC acted favorably on its staff report and amended the permit to allow CUCC to construct one well. That letter requests that the County of San Mateo put into effect a moratorium on issuing building permits in the service area of the Montara District. The CCC staff report had recommended as Condition 6:

"The applicant [CUCC] shall not authorize any new connections and shall petition the San Mateo County Board of Supervisors to similarly reduce the number of building permits within their service area as provided by LCP [Local Coastal Plan] Policy 1.19(b)."

Monthly and quarterly reports filed by CUCC pursuant to D.85-05-042 in OII 83-11-09 state that CUCC obtained the amended permit from CCC and, during August, 1987, constructed and put into service a single well at the Half Moon Bay Airport in accordance with CCC permit No. A-3-SMC-86-155. The October report, dated October 15, 1987, states:

"Water from this additional well became available to our system on August 14, 1987 and has been used virtually continuously since that date."

The same reports state that CUCC is continuing its efforts to comply with the conditions precedent to the issuance of a CCC permit for the construction of a second well at the airport. It has also obtained use permits and coastal development permits from

San Mateo County to drill two test wells in the San Vicente Creek area. The County has extended these permits until September, 1988.

Findings of Fact

1. The productive capacity of CUCC's water sources is 382 gpm, including the Montara Spring and the Park Well.
2. The Montara system requires 465 gpm of productive capacity to meet the demand of current customers for reliable service. In addition, to meet the demand of individual lot owners who have applied or will apply for service and the demand of the Farallon Vista Housing Development the system requires at least 550 gpm of productive capacity.
3. The combined current production of the wells added to the system since 1976 does not equal 200 gpm. (Finding 11, D.86-05-078, p. 33.)
4. Reliable well production was between 225 and 264 in 1976 and is now about 300 gpm. (Finding 12, Id.)
5. CUCC has not met the requirement of D.88618 to provide new well capacity of 200 gpm. (Finding 13, Id.)
6. Water from Park Well is blended with water from other sources before it is delivered to customers.
7. The blended water meets all DHS standards applicable to it.
8. The staff's proposed amortization plan would reduce CUCC's rate base to reflect the fact that Portola Wells 1 and 2 are no longer used and useful.
9. CUCC's authorized return on equity is 13.2%.
10. D.86-12-069 granted the relief sought by CUCC in its petition for modification filed November 12, 1986.
11. After a regulatory process that consumed almost 2 years CUCC obtained authority from CCC to construct one new well in the airport plain. The well has been constructed and has been operating since August 14, 1987.

San Mateo County to drill two test wells in the San Vincente Creek area. The County has extended these permits until September, 1988.

Findings of Fact

1. The productive capacity of CUCC's water sources is 383 gpm, including the Montara Spring and the Park Well.
2. The Montara system requires 465 gpm of productive capacity to meet the demand of current customers for reliable service. In addition, to meet the demand of individual lot owners who have applied or will apply for service and the demand of the Farallon Vista Housing Development the system requires at least 550 gpm of productive capacity.
3. The combined current production of the wells added to the system since 1976 does not equal 200 gpm. (Finding 11, D.86-05-078, p. 33.)
4. Reliable well production was between 225 and 264 in 1976 and is now about 300/gpm. (Finding 12, Id.)
5. CUCC has not met the requirement of D.88618 to provide new well capacity of 200 gpm. (Finding 13, Id.)
6. Water from Park Well is blended with water from other sources before it is delivered to customers.
7. The blended water meets all DHS standards applicable to it.
8. The staff's proposed amortization plan involves a refund of revenues collected by CUCC through rates approved and authorized by the Commission.
9. CUCC's authorized return on equity is 13.2%.
10. D.86-12-069 granted the relief sought by CUCC in its petition for modification filed November 12, 1986.
11. After a regulatory process that consumed almost 2 years CUCC obtained authority from CCC to construct one new well in the airport plain. The well has been constructed and has been operating since August 14, 1987.

12. By D.87-09-071 the Commission authorized Park Water Company to earn a 12% return on equity. Park's capital structure was 77.16% common equity.

13. CUCC's customers were 1,272 in December, 1979, and are now about 1,600.

14. The four factors listed in the section entitled "Need for a General Rate Proceeding" suggest that a rate decrease may be in order for the Montara District.

Conclusions of Law

1. The output of the Park Well should be added to the other water sources in computing productive capacity of the system.

2. This proceeding is not an appropriate vehicle for making rate or rate of return adjustments.

3. An order to refund the amount proposed in the staff's amortization plan would constitute retroactive ratemaking and would be contrary to the holdings of the California Supreme Court.

4. D.86-05-078 should not be modified to allow CUCC to include in the account for discontinued lease payments all costs for CUCC's search for new water supplies.

5. The CUCC proposal to include costs of searching for new water sources in the balancing account established in D.86-05-078 should be denied.

6. A punitive fine imposed by reducing return on equity by 50% would not be appropriate in this proceeding.

7. The following order should grant the CUCC petition for modification filed November 12, 1986, so that our docket may be cleared of a pending petition.

8. CUCC should be required to develop additional water production capacity to bring its total production to 550 gpm, as required by D.86193.

12. By D.87-09-071 the Commission authorized Park Water Company to earn a 12% return on equity. Park's capital structure was 77.16% common equity.

13. CUCC's customers were 1,272 in December, 1979, and are now about 1,600.

14. The four factors listed in the section entitled "Need for a General Rate Proceeding" suggest that a rate decrease may be in order for the Montara District.

#### Conclusions of Law

1. The output of the Park Well should be added to the other water sources in computing productive capacity of the system.

2. This proceeding is not an appropriate vehicle for making rate or rate of return adjustments.

3. It would not be reasonable to reduce rate base to account for the nonoperational status of Portola Wells Nos. 1 and 2 without examining additions and betterments to plant in service that have occurred during the same period, since the adjustment at issue would not affect a major portion of CUCC's rate base and since there are no other extraordinary circumstances justifying such an adjustment between general rate cases.

4. D.86-05-078 should not be modified to allow CUCC to include in the account for discontinued lease payments all costs for CUCC's search for new water supplies.

5. The CUCC proposal to include costs of searching for new water sources in the balancing account established in D.86-05-078 should be denied.

6. A punitive fine imposed by reducing return on equity by 50% would not be appropriate in this proceeding.

7. The following order should grant the CUCC petition for modification filed November 12, 1986, so that our docket may be cleared of a pending petition.

8. CUCC should be required to develop additional water production capacity to bring its total production to 550 gpm, as required by D.86193.



INTERIM ORDER

IT IS ORDERED that:

1. Citizens Utilities Company of California (CUC) shall submit a summary of earnings for the Montara District to the Commission Advisory and Compliance Division concurrently with any general rate application or advice letter for any other CUC water operation in California.
2. The petition of CUC for modification of D.86-05-078 is granted, as set forth in D.86-12-069.
3. CUC shall continue to explore for, develop, and put into service additional water supply sources until the total supply for its Montara District equals 550 gpm.
4. Phase II of this proceeding, including the water supply issues transferred from OII 83-11-09, is concluded.

This order becomes effective 30 days from today.

Dated SEP 14 1988, at San Francisco, California.

STANLEY W. HULETT  
President  
DONALD VIAL  
FREDERICK R. DUDA  
C. MITCHELL WILK  
JOHN B. OHANIAN  
Commissioners

APPENDIX A

Page 1

Findings of Fact

1. In D.86193 (August 3, 1976) in A.55538 and C.10093 CUCC was ordered to acquire new sources of water for its Montara service area capable of producing at least 200 gpm.

2. On September 21, 1976, CUCC notified the Commission that the Drake well (30-44 gpm) was placed in service.

3. In D.88618 (March 21, 1978) in reopened C.10093 CUCC was ordered to continue its efforts to acquire new sources of water for its Montara service area capable of producing at least 200 gpm.

4. In April, 1979, CUCC placed a new South Airport well #2 in operation replacing South Airport well #1 which had failed. The new well involves a net loss to the system since it produces less than the well it replaces produced at its peak capacity.

5. On December 6, 1979, CUCC in A.59321 requested a temporary moratorium on new service connections in Montara. D.91422 (March 18, 1980) established a limited moratorium.

6. On January 30, 1980, CUCC's witness testified in A.59321 that it had added to its system the four Portola Estates wells producing 200 gpm, of which 130 gpm would be available to CUCC.

7. As early as August 29, 1980, the four Portola Estates wells were producing only 180 gpm, of which CUCC were entitled to two-thirds of 120 gpm.

8. CUCC was entitled to HMBP's remaining one-third interest in the well production according to the terms of a lease dated February 5, 1981. However, HMBP retained the right to demand delivery of one-third of the production of the wells.

9. Portola Estates Well No. 1 failed in 1981. Portola Estates Well No. 2 failed in 1982. Portola Estates Well No. 3 is producing at 35% of its original estimated rate. Portola Estates Well No. 4 is producing at 20% of its original estimated rate.

10. The two Portola wells still operating produce between 33-83 gpm.

APPENDIX A

Page 2

11. The combined current production of the wells added to the system since 1976 does not equal 200 gpm.

12. Four hundred customers have been added to the system since 1976. Storage capacity has increased from 328,000 gallons to 762,000 gallons in this same period. Reliable well production was between 225 and 264 gpm in 1976 and is now about 300 gpm.

13. CUCC has not met the requirement of D.88618 to provide new well capacity of 200 gpm.

14. Increased storage has been principally responsible for the system's ability to provide additional service to 400 new customers since 1976.

15. Water service to current customers is not adequate in that it does not meet the maximum day requirements of GO 103 regarding water supply and fire reserve requirements, also in that it does not provide any reserve margin for possible failure of one of the three major wells serving the system. However, a few more customers, i.e., the six Portola Estate lots and the prospective customers who have obtained commitments from CUCC, may be added to the system, without significantly degrading the service currently enjoyed by the existing customers.

16. The customers identified in finding 15 will not be added to the system simultaneously, but rather over a period that may extend to the end of 1986 or beyond.

17. Any further additions to the customer base will seriously degrade the service to the existing customers unless additional water supplies become available.

18. CUCC's Supplemental Agreement with HMBP is advantageous to CUCC, will give CUCC a legal right to additional water supplies and may make available other HMBBP well sites to CUCC for exploration.

19. In D.85-06-042 (June 5, 1985) in OII 83-11-09 we ordered CUCC to proceed with all due diligence to develop and place in operation no later than June 1, 1986, new water supply sources or storage facilities, or both, sufficient to supply existing customers and new customers as they require connection.

(END OF APPENDIX A)

Recommended Conditions

- ADOPTED 1. (a) PRIOR TO THE TRANSMITTAL OF THE PERMIT, a study to determine the safe yield of the Denniston sub-unit of the Half Moon Bay Aquifer shall be completed by a qualified hydrogeologist and biologist. The study shall include an inventory of existing groundwater extraction, recharge rate which includes streamflow figures for Denniston Creek from stream gauges placed in the the upper and lower courses and monitored at regular intervals, and any other information required to produce a thorough study including recommendations for the protection of habitat values as required by the policies of the San Mateo County Local Coastal Program. The proportional costs of the study shall be based upon the average annual water usage of each participant.

ADOPTED(b) The study shall be submitted to the Executive Director for review and determination that it meets the requirements of Condition 1(a) and the Local Coastal Plan Policies 2.32 and 7.20. Copies of the study shall be provided at the same time to the appellants, the local government, and operators of other wells in the vicinity of the two proposed wells.

ADOPTED(c) The Executive Director, after having determined that the study is adequate, shall prepare a report to the Commission recommending final pumping rates and conditions of operation for the proposed wells based on the approved study and (1) consistent with LCP policies regarding groundwater extraction and habitat protection, and (2) sufficient to prevent interference with other existing wells in the area. The Executive Director shall send copies of the report to the appellant, the local government, and operators of other wells in the area.

ADOPTED(d) The Commission shall establish final pumping rates and conditions of operation based on the study, the Executive Director's report, and other evidence submitted at a public hearing. All parties which received a copy of the Executive Director's report shall be permitted to testify at the hearing.

- ADOPTED 2. Prior to the connection of any water supplies to Citizen's Utility Company customers from the wells allowed by this permit, applicant shall provide an additional 200,000 gallons of water storage, in a tank or tanks, for emergency or peak demand use. A Coastal Development Permit for the tank or tanks must be secured from San Mateo County prior to installation.

Recommended Conditions (Continued)

- ADOPTED 3. Applicant shall comply with the following conditions attached to the permit by San Mateo County; Conditions numbers 3, 4, 5, 6, 10, 11, 12, 13, 14, and 15 (Board of Supervisors Approval July 1986, see Exhibit 1).

RECOMMENDED FINDINGS

The Commission finds and declares as follows:

A. PROJECT DESCRIPTION

The proposed project involves the development of two community water wells to serve Citizen's Utilities customers. The wells are to be located at the Half Moon Bay Airport, west of Highway One, between the highway and the airport service buildings. The County has conditioned the permit to allow a maximum withdrawal of 400 acre feet a year from the wells until hydrological/biological studies are completed. The proposed wells are located in the Denniston sub-unit of the Half Moon Bay Aquifer. Nearby existing wells include CUC North Airport well (approximately 450' distant); Coastside Community Water District's wells, approximately 1/4 mile to the south; and, a couple of private wells to the west. (Please see Exhibit 4 for well locations in the Airport Area.) The proposed wells are also approximately 1,800 to the north-east of Pillar Point Marsh and approximately 1,500 feet from Denniston Creek (Exhibit 5).

(END OF APPENDIX B)

A-3-SMC-86-155 CITIZENS UTILITIES CO. OF CALIFORNIA Page 2

STAFF RECOMMENDATION

The Staff recommends that the Commission adopt the following Resolution:

Approval with Conditions

The Commission hereby grants, subject to the conditions below, a permit for the proposed development on the grounds that the development, as conditioned, will be in conformity with the provisions of Chapter 3 of the California Coastal Act of 1976, will not prejudice the ability of the local government having jurisdiction over the area to prepare a Local Coastal Program conforming to the provisions of Chapter 3 of the Coastal Act, is located between the sea and the first public road nearest the shoreline and is in conformance with the public access and public recreation policies of Chapter 3 of the Coastal Act, and will not have any significant adverse impacts on the environment within the meaning of the California Environmental Quality Act.

RECOMMENDED CONDITIONSStandard Conditions

See Exhibit A.

Special Conditions

1. PRIOR TO TRANSMITTAL OF THE PERMIT, the applicant shall demonstrate, to the satisfaction of the Executive Director, that they are unable to purchase water from Coastside Community Water District, either from CCWD's own supply or from supplies purchased from the City of San Francisco.
2. PRIOR TO TRANSMITTAL OF THE PERMIT, the applicant shall provide the following information to the satisfaction of the Executive Director:
  - (a) An analysis of why CUC water use rates are above the norm. Analysis shall include recent (1986-1987) meter figures for homes and production figures for wells for the same period.
  - (b) A program to substantially reduce domestic water use and/or repair leaking pipes depending on the recommendations of the analysis prepared to satisfy Condition 2(a). The program, subject to the approval of the Executive Director, shall be implemented upon approval. Progress reports on the effectiveness of the

program shall be submitted on a monthly basis to the Executive Director. Failure to effectively implement the program or to provide Progress Reports shall be grounds for the revocation of this permit.

3. The applicant shall immediately seek permits to construct the storage required by Condition #2 of the original permit. The new storage facility shall be completed and available for service within 120 days of acceptance of this permit.

4. Drilling of a temporary (one year from date of installation) well at the Airport site may only be permitted if the applicant is unable to secure water supplies from CCWD and the program for reducing water use is ineffective in bringing use rates down to the level of the production rates of the existing water sources after one month's operation. Use of the well is limited to periods of peak demand and only in the amount necessary to prevent the disruption of service while maintaining a minimum of 450,000 gallons in storage for fire flows. Reports of the time and amount of withdrawal from this well shall be submitted to the Executive Director within five days of each use.

5. Prior to installation of the proposed water well, the applicant shall submit for Executive Director's review and approval after review by the California Department of Fish & Game a:

- a. Monitoring Program outline for Pillar Point Marsh prepared by a qualified biologist
- b. The monitoring program shall be designed to assess the potential adverse impacts that the water withdrawal from the temporary well will have on the marsh habitat,
- c. Monitoring data shall be collected prior to the well installation, during the time of well use, and up to one year after the well is abandoned, and
- d. The methodology, frequency and type of data collection, and the location of data transects shall be defined in the outline after consultation with the California Department of Fish and Game.

6. The applicant shall not authorize any new connections and shall petition the San Mateo County Board of Supervisors to similarly reduce the number of building permits within their service area as provided by LCP Policy 1.19(b). New connections may be authorized upon demonstration to the County and the Coastal Commission that adequate, new water supplies exist to serve the proposed number of new connections.

(END OF APPENDIX C)

## APPENDIX D

Citizens Utilities Company of California  
Montara District

## AMORTIZATION OF PORTOLA WELLS #1 AND #2

## Plant and Depreciation Rate

Line:		Land	Well	Structure	Pumps	
No.:	Item	Ac. 306	Ac. 325	Ac. 321	Ac. 324	Total
1	Portola #1	\$ 9,175	\$19,413	\$ 2,774	\$ 5,709	\$37,071
2	Portola #2	9,175	19,413	2,760	4,503	35,851
3	Total	\$18,350	\$38,826	\$ 5,534	\$10,212	\$72,922
4	Depreciation Rates	None	3.36%	3.02%	5.15%	-
5	Monthly Accrual		109	14	44	167

Line:	Item	1982*	1983	1984	1985	1986	Total:
		(a)	(b)	(c)	(d)	(e)	(f)
6	Plant	\$72,922	\$72,922	\$72,922	\$72,922	\$72,922	
7	Depr. Reserve	1,165	3,163	5,161	7,159	7,991	
8	Net Plant	\$71,757	\$69,759	\$67,761	\$65,763	\$64,931	
9	Wgtd. Avg. Plant	72,340	70,758	68,760	66,749	65,347	
10	Rate of Return	2.71%	11.80%	13.29%	13.51%	13.51%	
11	Earnings	1,144	8,349	9,138	9,018	3,678	
12	Taxes	1,209	8,822	9,656	9,529	3,886	
13	Depreciation	1,165	1,998	1,998	1,998	832	
14	Excess Lease Costs**	1,400	1,968	2,841	4,207	1,753	
15	Patepayer Cost	\$ 4,918	\$21,137	\$23,133	\$24,752	\$10,149	\$84,089
16	Cost of Well						72,922
17	Negative balance to be amortized over three years						(11,167)

\* 7-month period 1982; 5-month period 1986.

\*\* Amount of the lease in D.82-05-076, less amount actually paid.

(END OF APPENDIX D)



APPENDIX E

Adopted Cost of Capital from D.82-02-059 in A.60132 (Sacramento County Water District of Citizen Utilities Company of California)

<u>Component</u>	<u>Component Weight</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Long-term Debt	32.0%	9.57%	3.06%
Common Stock	68.0%	13.20%	8.98%
Rate of Return			12.04%

Effect of Staff's Proposed Reduction in Cost Rate for Common Equity from 13.20% to 6.60%

<u>Component</u>	<u>Component Weight</u>	<u>Cost Rate</u>	<u>Weighted Cost</u>
Long-term Debt	32.0%	9.57%	3.06%
Common Stock	68.0%	6.60%	4.49%
Rate of Return			7.55%

Dollar Effect of Staff Proposed Reduction

$$12.04\% \times \$1,564,800^* = \$188,401.92$$

$$(\text{Minus}) \quad 7.55\% \times \$1,564,800^* = \$118,142.40$$

$$\$ 70,259.52 \text{ (Annual Penalty)}$$

\* Average depreciated rate base for 1985 (Exhibit 22, Appendix B, Sheet 1 of 2, line 24.)

(END OF APPENDIX E)