

Decision 83 08 055 AUG 17 1983**ORIGINAL**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of  
 GERBER WATER WORKS, INC., to increase  
 water rates for an increase in gross  
 revenue of approximately \$19,950 in  
 Tehama County.

Application 82-08-56  
 (Filed August 27, 1982)

Daniel E. Collar, for Gerber Water  
 Works, Inc., applicant.  
Bruce E. Johnson, for Gerber Fire  
 Department, interested party.  
Alexander Chocas, for the Commission  
 staff.

O P I N I O NStatement of Facts

During the year 1911, the Tehama Investment Company installed a water system to serve the unincorporated community of Gerber, nine miles from Red Bluff in Tehama County. The investment company operated the system until 1915 when it was transferred to E. A. Brown as trustee, who then in 1916 transferred it to the Gerber Terminal Townsite Company. In 1922 E. K. Sears purchased the system only to sell it in turn to C. J. Lee in 1923. After C. J. Lee's death in 1942 the system was owned and operated as a sole proprietorship by his widow, Mary Elizabeth Lee (Mrs. Lee, Sr.).

In 1949 Mrs. Lee, Sr., while reserving in herself a life estate, conveyed the utility to her son, John C. Lee, who in turn held it with his wife, Edna B. Lee (Mrs. Lee) as joint tenants with right of survivorship. After the death of John Lee in 1956 and the subsequent death of Mrs. Lee, Sr., Mrs. Lee became the sole proprietor and actual manager of the system. In 1979 the system was incorporated as the Gerber Water Works, Inc., a California corporation, and Mrs. Lee became the sole shareholder (See Decision (D.) 90875 dated October 10, 1979 in Application (A.) 58981).

Water supply is obtained from two wells (with a third in reserve) equipped with deep well turbine pumps. A 22,000-gallon elevated storage tank provides the system pressure and storage. Filtration and chlorination treatment facilities are not required because the wells provide water of satisfactory chemical and bacteriological quality. Approximately 262 active service connections provide water to about 1,000 persons from a distribution system with approximately 24,500 feet of 6-inch, 4-inch, 2-inch, and smaller pipe. The system, however, has serious deficiencies including deteriorated transmission and distribution mains, low water pressure, and inadequate fire protection service.

In 1979, recognizing the service problems, the utility, after using the services of a consulting engineer and the assistance of our Hydraulic Branch, and following a public meeting which indicated public support, applied for and by D.91197 dated January 8, 1980 in A-59038, was granted authorization to borrow \$100,075 under the Safe Drinking Water Bond Act (SDWBA) of 1976 (Water Code Section 13850, et seq.)<sup>1</sup> and to add a surcharge to water rates to repay principal and interest. Thereafter, beginning March 1, 1980 a surcharge of approximately \$2 per month per customer was placed into effect. The last general rate increase was authorized in 1978.<sup>2</sup>

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<sup>1</sup> The proceeds of the loan were to correct the major water system deficiencies. As a result, 4,770 feet of 8-inch main in San Benito Avenue were replaced (eliminating 2 sections of pipe which had produced a high incidence of leaks and failures, thereby conserving water); 5 steamer fire hydrants were placed, spaced along San Benito Avenue through the commercial district; various control valves were installed to facilitate future repairs; and 86 services were relocated to connect to the replaced main.

<sup>2</sup> By Commission Resolution No. W-2394 effective August 8, 1978, and modified December 9, 1978, to reflect a reduction in property taxes.

On April 12, 1982 the Commission received a draft advice letter from applicant requesting an 87.9% increase. However, this draft filing was deficient and did not meet the requirements of the Hydraulic Branch for processing as an Advice Letter. Hydraulics advised applicant that it had revised the metered rate structure proposed to reflect Commission life-line policy, and that staff would be making a more complete analysis, possibly recommending a lesser rate increase. Meanwhile applicant was advised also to mail a notice to its customers of its proposed increase. Applicant made this mailing and in response the Commission received 28 individual letters and a petition with 183 signatures protesting the magnitude of the increase. Considering the volume of protest, the advice letter proceeding was converted to a formal rate application on August 27, 1982.

Because of workload backlog and difficulties initially encountered in obtaining records and data during staff's field survey, the staff report was repeatedly delayed. Then the public hearing of the application first scheduled for May 3, 1983 was rescheduled at the request of applicant until June 21, 1983, at which time, after mailed notice to all customers and local publication, hearing was held in Gerber before Administrative Law Judge (ALJ) John B. Weiss. At conclusion of the hearing the matter was submitted.

According to the utility's application, using its then present rates and expenses, it estimated a \$17,260 negative net operating revenue for year 1982. This represented a 70.5% negative rate of return. If granted the 87.9% rate increase it requested, an increase it estimated would produce additional gross revenues of \$19,950, it estimated its 1982 rate of return would be 11%. (Applicant's Estimated Summary of Earnings figures are set forth in Appendix A.) However, staff encountered areas at issue, particularly in applicant's estimates for purchased power, office supplies, insurance expense, legal and accounting services, general and vehicle

expenses, and depreciation. Applicant and staff were unable to reconcile their differences as hearing time approached. During the time obtained by postponement of the hearing first scheduled for May 3, 1983, applicant attempted to employ qualified outside expert assistance to present its case at the forthcoming hearing. However, it found that the cost would be prohibitive for a company its size. Accordingly, while still insisting upon its need for immediate rate relief, and in the interest of obtaining prompt resolution of its problem, it determined that it would withdraw its initial data, and substantially rely upon staff's data and recommendations. It was apparent that because of the protracted time from inception of this application to hearing, the original data relied upon concerning operations was completely out of date. Furthermore, it was clear that staff agreed that the utility was operating at a substantial loss, although not of the magnitude claimed by applicant.

At the hearing applicant presented evidence drawn from its annual reports to the Commission which indicated operating losses every year except one since 1974. In that one year, 1979, the year following the last general rate increase, applicant showed a positive net return of \$3,810.<sup>3</sup> Applicant also produced evidence that the utility's 1982 Pacific Gas and Electric Company (PG&E) bills totaled \$6,770.78, 12.8% more than staff was forecasting for 1983. Nonetheless, applicant's representative testified that the utility would accept staff's recommendations, believing that if it received the rate of return staff projects, it could remain in business. Further, the representative testified that Mrs. Lee would not expect repayment of her loans all at the same time, but if the utility were producing the return projected she was willing systematically to allocate money to make improvements on a gradual basis.

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<sup>3</sup> Applicant also introduced an exhibit indicating that since June 8, 1981, Mrs. Lee had advanced seven loans totaling \$15,165, and testimony was presented that she "has no more to give." Of this, \$10,000 was for water pumps and wells. These loans were at 13% per annum interest. Only a small amount of interest but no principal has been repaid.

Appendix A, apart from showing for contrast purposes applicant's 1982 estimates, sets forth staff's estimates of 1983 and 1983 results of operations, contrasting the effects of present and recommended revenues. Staff recommended that applicant be allowed a rate of return between 11.25% and 11.75%. Recommended revenues for each year therefore were designed to cover applicant's actual operating expenses and deductions taken from applicant's records, or those expenses which, based on staff's experience, would be more appropriate to a water utility of this size and circumstance, and to provide an approximate 11.5% return on rate base.<sup>4</sup> Staff also proposed retirement of two wells and pumping stations, replaced with part of Mrs. Lee's loans, as well as certain mains abandoned when replaced by the new main on San Benito Avenue paid for out of SDWBA money. These retirements resulted in a substantial decrease in the Depreciation Reserve, and a commensurate increase in the Net Plant in Service Account, thereby increasing rate base for year 1984.

The staff witness, noting that the southern portion of the Gerber System suffers from reverse flows resulting in occasional outages, recommended that applicant give priority to spending \$1,200 to install a slow opening, slow closing Clayton valve so that the pump won't turn on and off so abruptly. On a longer term basis, staff would also like to see midpoint interconnection of the system's laterals to form a grid.

Chief Johnson of the Gerber Fire Department testified that while some increase would be in order, 87.9% was excessive. The chief further testified that the water system does not, as it stands, meet fire fighting standards for the entire Gerber community and therefore jeopardizes the insurance rating of the community. Except for the San Benito Avenue main replaced in 1981 by use of SDWBA loan funds, the rest of the distribution system is undersized by today's

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<sup>4</sup> Staff was also concerned with restructuring metered and flat rates to pick up the \$500 per year formerly collected for fire hydrant service from the local fire protection agency.

standards, using single outlet, 2½-inch wharf hydrants on 2-inch pipe risers. Flow from the latter varies between 260-430 gallons per minute (gpm) whereas less than a 500-gpm flow is not considered ratable by the Insurance Service Office (ISO).<sup>5</sup> The chief would like to see a fair portion of any rate increase authorized be set aside for improvements to the distribution system.

During the hearing, applicant and the chief of the Fire Department agreed to sign the standardized Public Utilities Commission fire hydrant agreement.

Approximately 60 members of the general public attended and sat through the hearing. Initially nine indicated a desire to make statements. However, after listening to the presentations of the parties, only four spoke. One expressed agreement with staff's position. Two recognized the utility's need to make a reasonable return, but would like to see some improvements in service. Of these two, one stressed the retirement nature of the community and the prevailing limited income situation. The last speaker was concerned why a Clayton valve had not been installed when the south end well was added, and why the system was not fully metered. Applicant explained that it was unable to predict that so much of a pressure surge would result when the well and pump were added to the system. The forbidding initial cost of metering the entire community was explained.

#### Discussion

As noted earlier, applicant has decided to adopt staff's estimate of operating and other expenses, and to accept staff's recommendation for a rate of return, asserting that the utility just cannot afford the services of competent expert assistance to present

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<sup>5</sup> The chief testified that in 1976 ISO told the Gerber Fire Protection Agency that while the agency itself rated a six rating, the poor water distribution system in Gerber caused ISO to reduce that rating to an eight, and that unless 500 gpm could be produced through the system by the time of their next rating, Gerber would lose the eight rating, resulting in an increase in local fire insurance premiums.

a case for another result. This is a predicament not uncommon to many small water utilities. While estimates of most operating expenses and calculations of rate base can usually be derived from the utility's own records, the determination of a fair rate of return necessarily is an imprecise art. It is aimed at attaining a viable balance between the divergent interests of the utility's customers and its owners. A fair rate of return depends upon the facts of the particular situation, and in the final reckoning, comes down to an application of informed judgment.

Rates must be determined which protect the short-term interest of the consumers in obtaining the lowest possible charges, while assuring maintenance of good service over the long run. However, these same rates must also produce enough revenue to pay proper and reasonable operating expenses, depreciation, and taxes, maintain credit, pay reasonable dividends, and provide reasonable additions to surplus so that the physical plant can be kept up to date. A reasonably economically healthy utility is essential under all circumstances. But to the extent customers of a utility, say in an economically depressed or a retirement community, are willing to accept and pay for merely tolerable levels of service, the rate of return can be less. But it must be sufficient to maintain a viable utility.

In this situation we have a retirement type community. Its citizens at the hearing and in letters to the Commission have made it clear that they must get by on very limited means. Unfortunately, the water system serving them, installed in 1911, predates modern standards for fire protection and minimum pressure. The system is largely unmetered. To bring the system up to General Order (G.O.) 103 standards would mean having to replace most of the distribution system. At today's costs this would be very expensive. We saw that the 1980-1981 SDWBA loan, at a face cost of \$100,000, replaced only the San Benito Avenue facilities. To duplicate this modernization on the five remaining parallel avenues and six cross streets would involve a very large investment. The Commission favors metering. It is the most fair way to assure that each customer pays for what he

uses. But to meter the balance of utility customers would require a further investment of \$70,000 to \$115,000. Mrs. Lee has invested all that she can. The utility has produced a loss every year since 1974 but one. It is unlikely that anyone can be found to purchase the utility and invest even more money to bring it up to G.O. 103 standards. The people of Gerber could form a water district, if they wished, and either purchase or obtain the water system by eminent domain. But either way they would have to pay for the system and then tax themselves to obtain the very substantial amounts of money which would be required to modernize the system. But the funds required are just not there.

It appeared to our ALJ at the hearing that the consensus of those present was that they recognized the limitations forced by economics and that they were willing to accept generally existing limitations, but that they wanted to see some gradual improvements as time advanced and that they were willing reasonably to pay for these. Mrs. Lee made it clear that she remains interested in the community and is willing to work along with it to bring gradual improvement. She has advanced funds to the extent of her ability to do so to keep the system afloat in recent years. She invested in new wells and pumps. She expressed her willingness to stretch out repayment on her notes if given a reasonable return on her investment, and to continue to invest in improvements (for example, the claymore valve needed to control the surging that has caused recent outages).

After consideration of all the evidence and statements from the public, we conclude that for these times and circumstances an approximate 11.5% return on depreciated rate base would be just and reasonable for this utility, applicable to both 1983 and 1984.

Although applicant adopted staff's estimates for 1983 and 1984 operating and other deductible expenses, thereby obviating any resolution of controversy on these items, it is nonetheless for this Commission itself to make a finding as to their reasonableness and justness relative to the increased rates staff recommends.

Staff determined its estimated operating and other expenses by taking into consideration both this utility's historical use and levels commensurate for comparable water utilities of this size and circumstance. In estimating purchased power, staff also took into consideration PG&E's General Service Schedule A tariff filed April 6, 1983. This tariff includes an energy component. On April 6, 1983 this component was reduced 30%, substantially lessening power costs. This difference accounts for staff's 1983 and 1984 estimates being lower than applicant's actual 1982 power bill.<sup>6</sup>

Salaries and operational/maintenance labor costs are another major item of expense. Operating a business of this size requires discretionary use of informed judgment as well as physical labor. While not required on a constant use basis, labor nonetheless must be available in standby status when needed, which requires adequate compensation. As noted, staff's estimates are commensurate with those for comparable water utilities. The estimate for office supplies was calculated by staff based upon average requirements for stationery, billing, mailing, and telephone use. Insurance expenses were based on data obtained from applicant's insurance agent. Vehicle expenses took into consideration the particular needs of this utility. Legal and Accounting as well as General expense estimates are on a comparable level relative to other water utilities. If applicant can substantiate a need for higher expenses applicable to specific rate filings or other requirements, these should be identified and requested in subsequent general rate proceedings. Staff used the same 2.3% depreciation rate used by applicant in its annual reports. Property taxes were taken from the 1982-83 tax bills and increased by the 2% legal limit allowed. Income taxes were calculated based on the Economic Recovery Tax Act of 1981.

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<sup>6</sup> Should there be future changes in this energy component, or other aspects of PG&E's billing, applicant should upon notice from PG&E immediately file an advice letter request for commensurate adjustment to its rates.

In determining rate base, staff used applicant's accounts, although it also reduced the depreciation reserves by retiring the two wells (\$6,400) and two pump stations replaced by Mrs. Lee and the 5,000 feet of main (\$2,370 displaced by SDWBA loan installations), and allowed for the improvements to the elevated storage tank. These changes served in effect to increase the net plant in service, and thereby raised the rate base, particularly in 1984.

Returning to the estimates of operating revenues, we note that in determining the revenues required in 1983 and 1984 to support staff's estimates of operational and other expenses for each of the years, and the rate of return we found to be presently appropriate for this utility, staff has used applicant's 1981 water use table for the metered customers, and applicant's 1983 customer roster for 1983 and 1984 flat rate service.<sup>7</sup> Finally, having examined thoroughly the reasoning and calculations behind each of staff's estimates applicable to 1983 and 1984 operations, as set forth in Appendix A, we find these to be reasonable and adopt them.

Considering the desperately precarious financial position of this financially distressed water utility, without sufficient funds to enable it currently to function<sup>8</sup> or to meet current PG&E bills, it is apparent that there is an immediate need for a rate increase. Accordingly, the effective date of the following order should be the date of signature.

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<sup>7</sup> Having determined total revenue requirements, staff then provided for equitable distribution of the increases found necessary. The resulting rates proposed by staff, which follow recent Commission rate design principles, are set forth in Appendix B. These rates represent an average 50.3% increase in 1983 and a 3.2% increase in 1984.

<sup>8</sup> The utility's financial position is so bad that although there are six would-be customers inside its service area who want to be hooked up for service to existing mains, at present the utility lacks the money to invest in the connection, i.e., to pay for a tractor to come and put in the connection.

Findings of Fact

1. Gerber is a compactly sited, residential retirement community of approximately 1,000 persons with no industry and few commercial enterprises.
2. The Gerber Water Works, Inc. system was originally installed in 1911.
3. Since 1974 the system, except for 1979, has failed to earn a positive return.
4. The last general rate increase was authorized in 1978.
5. In 1980-1981 part of the system was brought up to G.O. 103 standards by means of an SDWBA loan; the bulk of the system, however, does not meet standards.
6. By this application the applicant sought a 27.9% increase in rates, but the rates it proposes would produce an unjustified rate of return.
7. Staff's projections of 1983 and 1984 expenses and rate base are reasonable, and being based on more current data, should be adopted over applicant's.
8. Applicant accepts staff's projections of 1983 and 1984 Summary of Earnings (Appendix A).
9. Staff's recommended rates of return of 11.58% and 11.54%, respectively for 1983 and 1984 are reasonable.
10. Staff's recommended rate design is reasonable (Appendix B).
11. The adopted rates of return will yield additional revenues in the amount of \$11,580 (50.3%) in 1983 and \$1,100 (3.2%) in 1984.
12. Applicant sorely requires immediate rate relief to continue operations.

Conclusions of Law

1. The application should be granted, based on staff's recommendations, to the extent provided by the following order, the adopted rates being just, reasonable, and nondiscriminatory.
2. The effective date of the following order should be the date of signature since there is an immediate need for the rate increase.

O R D E R

IT IS ORDERED that:

1. After the effective date of this order, applicant Gerber Water Works, Inc., is authorized to file the revised rate schedules listed under 1983 in Appendix B attached to this order. Such filing shall comply with General Order 96-A. The effective date of the revised schedules shall be four days after the date of filing. The revised schedules shall apply to service rendered on and after their effective date.

2. On or after November 15, 1983 applicant is authorized to file the revised rate schedules listed under 1984 in Appendix B attached to this order. Such filing shall comply with General Order 96-A. The effective date of the revised schedules shall be no earlier than January 1, 1984. The revised schedules shall apply to service rendered on and after their effective date.

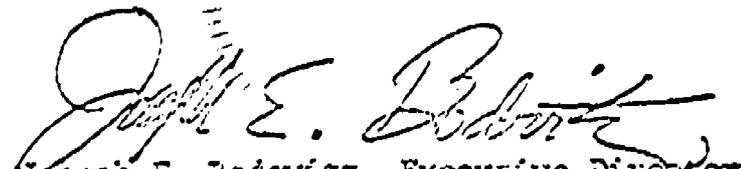
This order is effective today.

Dated AUG 17 1983, at San Francisco, California.

VICTOR CALVO  
PRISCILLA C. GREW  
DONALD VIAL  
WILLIAM T. BAGLEY  
Commissioners

Commissioner Leonard M. Grimes, Jr.,  
being necessarily absent, did not  
participate.

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

  
Joseph E. Bodovitz, Executive Director

APPENDIX A

GERBER WATER WORKS, INC.

Summary of Earnings

A.82-08-56  
ALJ/jc \*

	Applicant's		Staff's			
	Estimated 1982		Estimated 1983		Estimated 1984	
	Present Rates	Proposed Rates	Present Rates	Recommended*	Present Rates	Recommended*
<u>Operating Revenues</u>						
Metered Water	\$ 2,900	\$ 5,450	\$ 3,260	\$ 4,890	\$ 3,260	\$ 5,055
Unmetered Water	19,300	36,260	19,760	29,710	19,760	30,645
Fire Protection	500	940	-	-	-	-
<b>Total Operating Revenues</b>	<b>22,700</b>	<b>42,650</b>	<b>23,020</b>	<b>34,600</b>	<b>23,020</b>	<b>35,700</b>
<u>Operating Expenses</u>						
Power	7,625	7,625	6,000	6,000	6,000	6,000
Opr. & Maint. Employee Labor	8,400	8,400	8,400	8,400	8,400	8,400
Materials	1,000	1,000	800	800	1,000	1,000
Contract work	585	585	600	600	700	700
Management Salaries	7,200	7,200	7,200	7,200	7,200	7,200
Office Supplies	2,725	2,725	1,200	1,200	1,200	1,200
Insurance Expense	1,425	1,425	1,000	1,000	1,000	1,000
Legal & Accounting	1,950	1,950	200	200	200	200
General Expense	1,200	1,200	600	600	600	600
Vehicle Expense	3,300	3,300	1,200	1,200	1,200	1,200
<b>Total Expenses</b>	<b>35,410</b>	<b>35,410</b>	<b>27,200</b>	<b>27,200</b>	<b>27,500</b>	<b>27,500</b>
Depreciation Expense	1,890	1,890	1,110	1,110	1,140	1,140
Property Taxes	835	835	1,510	1,510	1,560	1,560
Payroll Taxes	1,625	1,625	1,615	1,615	1,615	1,615
Cal. Corp. Franch. Tax	200	200	200	200	200	215
Income Taxes	-	-	-	184	-	304
<b>Total Operating Expenses</b>	<b>\$39,960</b>	<b>\$39,960</b>	<b>\$31,635</b>	<b>\$31,819</b>	<b>\$32,015</b>	<b>\$32,334</b>
<u>Net Operating Revenue</u>	(17,260)	2,690	(8,615)	2,781	(8,975)	3,366
<u>Rate Base</u>	24,450	24,450	24,030	24,030	29,180	29,180
<u>Rate of Return</u>	(70.5%)	11.0%	(35.8%)	11.58%	(30.8%)	11.54%

(Red Figures)

\*and adopted

(END OF APPENDIX A)

## APPENDIX B

GERBER WATER WORKS, INC.

## Schedule of Rates

<u>Metered Service</u> <u>Monthly Quantity Rates</u>	<u>Per Meter Per Month</u>		
	<u>Present</u>	<u>1983</u>	<u>1984</u>
First 300 cu.ft., per 100 cu.ft.	\$0.32	\$ 0.50	\$ 0.50
Over 300 cu.ft., per 100 cu.ft.	0.42	0.66	0.70
<u>Service Charge</u>			
For 5/8 x 3/4-inch meter	2.50	3.80	3.80
For 3/4-inch meter	2.75	4.20	4.20
For 1-inch meter	3.75	5.70	5.70
For 1 1/2-inch meter	5.00	7.60	7.60
For 2-inch meter	6.75	10.25	10.25

The service charge is a readiness-to-serve charge, which is applicable to all metered service and to which is to be added the monthly charge computed at the quantity rates.

<u>Monthly Flat Rate Service</u>	<u>Per Month</u>		
	<u>Present</u>	<u>1983</u>	<u>1984</u>
For a single-family residence including premises not exceeding 7,500 sq.ft. in area	\$6.15	\$9.20	\$9.50
For each 100 sq.ft. of area in excess of 17,500 sq.ft.	0.026	0.04	0.05
For each small business	4.60	6.90	7.15

(END OF APPENDIX B)

standards, using single outlet, 2½-inch wharf hydrants on 2-inch pipe risers. Flow from the latter varies between 260-430 gallons per minute (gpm) whereas less than a 500-gpm flow is not considered ratable by the Insurance Service Office (ISO).<sup>5</sup> The chief would like to see a fair portion of any rate increase authorized be set aside for improvements to the distribution system.

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7. Staff's projections of 1983 and 1984 expenses and rate base are reasonable, and being based on more current data, should be adopted over applicant's.
8. Applicant accepts staff's projections of 1983 and 1984 Summary of Earnings (Appendix A).
9. Staff's recommended rates of return of 11.58% and 11.54%, respectively for 1983 and 1984 are reasonable.
10. Staff's recommended rate design is reasonable (Appendix B).
11. Applicant sorely requires immediate rate relief to continue operations.

Conclusions of Law

1. The application should be granted, based on staff's recommendations, to the extent provided by the following order, the adopted rates being just, reasonable, and nondiscriminatory.
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Insurance Expense	1,425	1,425	1,000	1,000	1,000	1,000
Legal & Accounting	1,950	1,950	200	200	200	200
General Expense	1,200	1,200	600	600	600	600
Vehicle Expense	3,300	3,300	1,200	1,200	1,200	1,200
<b>Total Expenses</b>	<b>35,410</b>	<b>35,410</b>	<b>27,200</b>	<b>27,200</b>	<b>27,500</b>	<b>27,500</b>
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Payroll Taxes	1,625	1,625	1,615	1,615	1,615	1,615
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<u>Net Operating Revenue</u>	(17,260)	(2,690)	(8,615)	(2,781)	(8,975)	(3,366)
<u>Rate Base</u>	24,450	24,450	24,030	24,030	29,180	29,180
<u>Rate of Return</u>	(70.5%)	11.0%	(35.8%)	11.58%	(30.8%)	11.54%

(Red Figures)

<sup>a</sup>and adopted

(END OF APPENDIX A)