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ORIGINAL

Decision No. 86807

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Investigation on the Commission's own motion into the operations, practices, service, equipment, facilities, rules, regulations, contracts, and water supply of the MONTEREY PENINSULA DISTRICT OF CALIFORNIA-AMERICAN WATER COMPANY, a corporation, and of RANCHO DEL MONTE DIVISION OF WATER WEST CORPORATION.	Case No. 9530 (Filed April 3, 1973)

(See Appendix A for Appearances.)

I N D E X

SEVENTH INTERIM OPINION

POSTURE OF PROCEEDING

Synopsis of Events Since Second Interim Opinion

Since our second interim decision in this investigation (Decision No. 84527 dated June 10, 1975) a total of 18 additional days of hearing have been held at Seaside before Commissioner Holmes and Examiner Boneysteele. A total of 56 witnesses testified in these additional hearings and 55 additional exhibits were received into the record. At the most recent hearing, that of September 23, 1976, the current issues pending were submitted for interim decision.

The proceeding so far has fallen into three discrete phases: the two days of hearing leading to our first interim order Decision No. 81443 dated May 30, 1973; the second phase of 21 days developing the evidence in which our second interim order was based, and this third phase of 18 days that addressed the evidence we are considering in formulating this decision.

During the third phase the Commission issued three interim decisions relating to specific events and conditions that arose subsequent to the second interim Decision No. 84527. In addition, we have issued three procedural decisions making minor modifications to Decision No. 84527 and the examiner has issued three written examiner's rulings dealing with environmental matters. We have also added the Rancho del Monte Division of Water West Corporation (Water West) as a respondent in this proceeding.

On August 17, 1976 we issued Decision No. 86249 in California American Water Company's (Cal-Am) Application No. 54942 for a general rate increase for all of its water operations throughout the state.

Attached to this decision as Appendix B is a table listing all decisions issued in this proceeding and also the status of all other proceedings initiated since the commencement of Case No. 9530 on April 3, 1973 which relate to the Monterey Peninsula water supply. The records of this and collateral cases have grown to be quite complex and therefore will not be summarized herein except insofar as explanation may be necessary for an understanding of the issues of which we are disposing.

Water Conservation and Rationing

In our second interim order we directed Cal-Am to prepare plans for a water conservation program and for a standby rationing plan. The water year commencing shortly after our second interim order was issued on June 10, 1975, turned out to be the driest ever experienced in Northern California. Between July 1, 1975 and

April 30, 1976 9.20 inches of rain fell at Los Padres Reservoir in the Carmel River watershed and 8.33 inches at Pacific Grove Reservoir in the urban service area.[1/] The dry year, plus growth in usage which occurred despite our second interim decision resulted in a demand on the system that Cal-Am could not supply through its limited transmission facilities. As a result the Commission, after emergency hearings held pursuant to Sections 350 through 358 of the Water Code, ordered, by Decision No. 86051 dated July 2, 1976, Cal-Am to institute a water rationing plan. When it became apparent that the prescribed plan, while sufficient to mitigate the effects of limited transmission capacity, would still permit the depletion of the upstream reservoirs on the Carmel River, Los Padres, and San Clemente at an unduly rapid rate, we modified, by Decision No. 86270 dated August 17, 1976, the rationing plan to provide for conservation of the available supplies of water. The water rationing plan will be in effect until further order of the Commission.

The water conservation and rationing program is proving to be effective, as the following figures, supplied by Cal-Am pursuant to the initial standby water rationing plan required by Ordering Paragraph 7 of Decision No. 84527, show:

1/ Figures for the entire water year July 1, 1975 to June 30, 1976, the previous water year, and the mean annual rainfall are:

	Los Padres Reservoir	Pacific Grove Reservoir
1975-1976	9.32 inches	8.54 inches
1974-1975	30.11	14.92
Mean Annual	26.65	16.91

Historical deliveries from all Company sources in each of the months of July, August, and September of the current and five preceding years (Total Water Produced to System in Acre-Feet)

	1976	1975	1974	1973	1972	1971
July	1,578.6	1,732.5	1,734.9	1,900.3	1,899.6	1,743.5
Aug.	1,464.5	1,699.9	1,720.6	1,723.8	1,853.7	1,742.5
Sept.	1,343.4	1,527.5	1,532.8	1,523.2	1,522.8	1,657.7
Total for year	15,891.7*	15,359.7	15,083.7	15,693.2	16,183.7	15,607.6

*Total for 12 months ended September 1976.

Deliveries for September, under Phase One-Half, the minimal of the four phases provided in the conservation and rationing program are 184 acre-feet less than deliveries for the previous September, a reduction of 12 percent. Deliveries have, likewise, failed to reach the level of 16,500 acre-feet predicted in Decision No. 84527 for the year 1975[2/] doubtless because of water conservation efforts of a concerned water using public.[3/]

In Decision No. 86270 dated August 17, 1976 we noted that, after a review of the operation of the rationing plan, we might wish to make further modifications to the rationing program. While the program has naturally caused some inconvenience to many people, we conclude that some such inconvenience is inevitable and we will make no change in the program in this order.

2/ Decision No. 84527, mimeo. page 21.

3/ The Monterey Peninsula Herald, the area's leading daily newspaper reported the details of the water situation most completely and, during the most acute stages published daily readings of the water levels in the Forest Lake and Pacific Grove Reservoirs.

Water Management Agency and
Local Governmental Actions

In our third interim Decision No. 85409 dated February 3, 1976 (which decision denied a request of the mayors of the six Peninsula cities that the connection ban be lifted), we described the formation of the Monterey Peninsula Water Management Agency, a joint powers agency created by the six cities and Monterey County. The Water Management Agency was formed as a separate public agency to plan for, and deal with, the water supply problem on the Monterey Peninsula.

In addition to the formation of Water Management Agency, the cities of Monterey, Pacific Grove, Del Rey Oaks, and Seaside, as well as the county of Monterey,[4/] have enacted ordinances requiring the use of water saving devices in new or reconstructed residential, commercial, industrial, or public buildings. The city of Monterey has also passed an ordinance designed to minimize water used for irrigation of new landscaping.

Del Monte Observation Well

In compliance with our Ordering Paragraph 6 of Second Interim Decision No. 84527, Cal-Am, after receiving an extension of time, completed, in December of 1975, the Seaside aquifer observation well recommended by the Department of Water Resources (DWR). This test well, designated the Del Monte Observation Well, is located between the Playa wells and the ocean and is intended to give warning of any impending sea water intrusion into the Seaside aquifer.

4/ The county ordinance is applicable to the unincorporated portion of Zone 11 of the Monterey County Flood Control and Water Conservation District.

Cal-Am's monthly reports of its monitoring of the test well, together with the chloride ion content of one of the Playa wells, are shown below:

Month	Del Monte Obs. Well: Static Water Level In Feet Above Sea Level	Del Monte Obs. Well: Chloride Ion Concentration in Milligrams per Liter	Playa Well #3: Chloride Ion Concentration in Milligrams per Liter	Production from Seaside Aquifer in Acre-Feet: For the Reported Month	Production from Seaside Aquifer in Acre-Feet: For the Previous 12 Months
1976 January	2.083	56.4	134.0	211.6	3,411.1
February	1.958	50.0	NA	155.0	3,365.3
March	1.833	55.6	136.0	248.9	3,179.4
April	1.417	58.1	131.0	295.5	3,474.7
May	1.417	55.0	134.0	354.3	3,491.3
June	0.917	54.4	135.0	453.3	3,504.6
July	1.000	55.0	134.0	472.3	3,607.4
August	0.917	54.2	134.0	408.3	3,558.1
September	0.833	55.5	136.0	445.6	3,634.9

The Playa well was selected for the above table because the Playa well site is the closest producing well to the ocean, being located just to the east of Fremont Street in the extreme northern part of Seaside. The DWR's engineering witness, Richard W. Meffley, testified that the relatively low chloride ion concentration of water taken from the Del Monte observation well could be explained by water from the upper aquifer flowing down the gravel pack of the well to mix with water from the lower aquifer. For that reason he suggested also monitoring the production wells. Cal-Am is monitoring all of its Seaside wells and submitting monthly reports to the Commission.

As may be seen from the above table, the water level dropped 1.25 feet in the eight-month period studied, and is now approaching sea level. The chloride ion concentration, however, has held steady and is well below the United States Public Health Service's recommended maximum of 250 milligrams per liter for drinking water.5/

5/ Now administered by the Environmental Protection Agency (EPA).

Environmental Impact Report

In our second interim opinion in Decision No. 84527 we discussed the construction of facilities required to treat additional water pumped from the Carmel Valley aquifer and to deliver the water to the metropolitan areas of the Monterey Peninsula.[6] We stated that, in the past, we would have ordered forthwith the immediate construction of the necessary facilities, namely the Begonia iron removal plant and the Canada de la Segunda pipeline.[7] Because the record at that time did not, however, contain the environmental data required to comply with the California Environmental Quality Act of 1970 (CEQA),[8] and also lacked evidence necessary to give the consideration to community, recreational, and historical factors as specified by Section 762.5 of the Public Utilities Code, we deferred ordering construction of these facilities. We declared that we would, at the next hearing, consider the application of CEQA and Section 762.5 to the construction of the Begonia and Canada projects.

Subsequent to our Second Interim Decision No. 84527, without further order of the Commission, Cal-Am, pursuant to CEQA, the Guidelines for Implementation of the California Environmental Quality Act of 1970 (Guidelines)[9] and Rule 17.1 of the Commission's Rules of Practice and Procedure (Rule 17.1)[10] prepared, and on April 1, 1976, filed, an Environmental Data Statement (EDS) for the Canada pipeline

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6/ Decision No. 84527, mimeo. pages 45 and 46.
7/ Decision No. 84527, mimeo. page 58.
8/ 4 Cal. Pub. Res. Code § 21000 et seq.
9/ 14 Cal. Adm. Code Ch. 3, § 15000 et seq.
10/ 20 Cal. Adm. Code Ch. 1.

and the Begonia iron removal plant projects. (Previously the examiner had ruled that the Commission was the "lead agency", the projects were not "emergency projects" exempt from the requirements of CEQA, and that Cal-Am was the "proponent.")[11/]

The EDS was, as required by Rule 17.1, circulated to all state and local agencies involved in approving and carrying out the project, to the Resources Agency, and other agencies, organizations, and individuals with special expertise or concern. Copies of the EDS were also made available to public libraries serving the Monterey Peninsula and were available for inspection at Cal-Am's Monterey District office.

After considering comments received and Cal-Am's comments, the staff, on October 4, 1976 distributed its Draft Environmental Impact Report (Draft EIR). The Draft EIR, in addition to environmental aspects of the projects, also addressed the community, recreational, and historical factors specified by Section 762.5 of the Public Utilities Code.

Hearings on the Draft EIR commenced in Seaside on December 6, 1976.

11/ A summary of all environmental motions and their disposition is included in Appendix B.

Issues to be Decided Herein

The following topics will be considered in this decision:

1. Rate structure of the Monterey District. (Per Ordering Paragraph 9 of Decision No. 84527.)

2. An inquiry into Cal-Am's finances and its relationship to American Water Works Company, Inc. (American Water Works), insofar as these subjects affect the adequacy of the water supply of Cal-Am's Monterey District. (Conducted pursuant to Ordering Paragraph 8 of Decision No. 84527.)

3. A reexamination of the ban in new service connections imposed by Ordering Paragraph 4 of Decision No. 84527.

4. Recently developed information concerning the water supply available from the Carmel Valley aquifer.

5. A reexamination of the exemption granted municipally sponsored urban redevelopment or renewal projects in Ordering Paragraph 1 of Decision No. 81443 and Ordering Paragraph 4 of Decision No. 84527.

6. The consequences of the naming of Water West as a respondent.

7. A request by Del Monte Properties Company (Del Monte) that the Commission affirm that Del Monte is eligible to receive service for its Deer Flats and Old Capitol Tract properties.

8. Construction of the required facilities.

RATE STRUCTURE

Present Rate Structures and Levels

In Ordering Paragraph 10 of our Second Interim Decision No. 84527 we directed the Utilities Division of our staff to investigate Cal-Am's rate structure, insofar as that subject affects the Monterey Peninsula water situation. Similarly, in our recent Cal-AM rate increase Decision No. 86249, we made a finding that additional evidence should be adduced in this proceeding, Case No. 9530, concerning alternative rate schedules, including those employing a single block system of rates. In response to these directives, Associate Utilities Engineer Wallace F. Epolt, P.E., prepared a report on Cal-Am's rate structure which he presented at the September 22 and 23, 1976 hearings.

The present rates for the Monterey District were made effective September 11, 1976, under authority granted by Decision No. 86249. In that decision we reduced the number of blocks in the general metered service schedule from six to four and, as noted above, solicited additional evidence concerning alternative rate structures. The present rates retain the traditional declining rate block form, modified to provide for three different elevation zones to reflect the wide range of elevations encountered in the District. The tariffs provide that charges to golf courses for irrigation during the off-peak hours, 9:00 p.m. to 5:00 a.m., will be at a rate 15 percent lower than the general metered service rates. Cal-Am's employees are allowed a 25 percent discount.

General metered service rates are shown in the following tabulation:

Quantity Rates:	Per Meter Per Month Gravity Zone	1st Elevation Zone	2nd Elevation Zone
First 300 cu.ft. or less	$ 2.50	$ 2.65	$ 2.85
Next 1,700 cu.ft., per 100 cu.ft.	.470	.530	.570
Next 18,000 cu.ft., per 100 cu.ft.	.397	.471	.541
Over 20,000 cu.ft., per 100 cu.ft.	.369	.449	.519
Minimum Charge:			
For 5/8 x 3/4-inch meter	2.50	2.65	2.85
For 3/4-inch meter	3.20	3.40	3.60
For 1-inch meter	4.50	4.70	4.90
For 1-1/2-inch meter	8.00	8.50	9.00
For 2-inch meter	13.50	14.00	14.50
For 3-inch meter	24.00	25.00	26.00
For 4-inch meter	38.00	40.00	42.00
For 6-inch meter	75.00	80.00	85.00
For 8-inch meter	120.00	125.00	130.00

The Minimum Charge entitles the customer to the quantity of water which that minimum charge will purchase at the Quantity Rates.

Del Monte Contract

Records of the Commission show that, prior to 1930, the Monterey District was served by Monterey County Water Works (MCWW), a corporation whose stock was wholly owned by Del Monte and prior to 1919, by Del Monte's predecessor, the Pacific Improvement Company (Pacific Improvement). In 1916, Pacific Improvement segregated its water properties into MCWW and into a so-called "private water system". The private system, which was physically interconnected with MCWW's public utility system, supplied Pacific Improvement's, and later Del Monte's, hotels and other properties.[12/] In 1930, Chester H. Loveland acquired, from Del Monte, both the stock of MCWW and the facilities of the private water system.

12/ The segregation of the facilities into a public utility and a private water system was recognized in our Decision No. 3059 dated January 25, 1916 in Application No. 1657. (9 CRC 91, 94.)

As "an integral and substantial part of the consideration" of the sales agreement, Mr. Loveland agreed to sell, and Del Monte to buy, from the private water system, for a period of 50 years, all water required to meet Del Monte's reasonable then and future needs, up to a maximum of 35 percent of the amount of water available to MCWW and to the private system from the Carmel River.

Del Monte was to pay for the water thus delivered at rates ranging from $1.10 for the first 300 cubic feet down to $0.10 per 100 cubic feet for all water over 30,000 cubic feet. These rates were for gravity water only, and should pumping become necessary, Del Monte would pay the cost of such pumping.

Despite the provisions of Section 17(b) of the Public Utilities Act (reenacted in 1951 as Section 531 of the Public Utilities Code), which required public utilities either to charge their filed rates or to obtain exceptions from the Commission, the rate provisions of the Del Monte Contract were never submitted to the Commission for approval, presumably because the water system operators considered the sales to Del Monte to be a nonutility service.

In 1935, Mr. Loveland and his associates merged their various utility interests, including MCWW and the private water system, into the California Water & Telephone Company[13/] (Cal. Water & Tel.). The Del Monte contract obligated the "heirs, assigns, and transferees" of Mr. Loveland. Thus, when Cal. Water & Tel., and later Cal-Am acquired the Monterey District water properties, they assumed the obligations, and the benefits, of the Del Monte contract.

13/ Pursuant to Decision No. 28276 dated October 14, 1935 in Application No. 20127. (39 CRC 406.)

In Decision No. 30046 dated August 16, 1937 in Case No. 3825, we noted that, despite the evident intent of the Commission and Pacific Improvement, when, in 1916 they carved out a practically separate system to serve Del Monte, there had since been only a vague adherence to the 1916 agreement. Not only had there been gradual commingling of the use and operation of the so-called private system and the utility system, but new agreements had been made between the predecessor corporations which considerably altered the contractual relationship. The Commission observed that all of such agreements and conveyances were between corporations, one of which completely held the stock of the other. (40 CRC 683, 686.)

In the 1937 proceeding the Commission, in view of the interlacing of the two systems over the years, adopted a staff recommendation that the utility and "private water system" operations be considered together, and that the rates for the utility service be established at a level that would return to Cal Water & Tel. a proper estimated net income, assuming that the utility's rates were imputed to the Del Monte service. The Commission has consistently followed this practice in the nearly 40 years that have followed Decision No. 30046, reaffirming the imputation of Del Monte revenues most recently in Decision No. 86249 dated August 17, 1976 in Application No. 54942.

The history of the Del Monte contract and the Commission treatment thereof have been reviewed in detail because their effect on Cal-Am's actually realized revenues must be considered in any restructuring of the Monterey District rates. The history is also helpful in understanding the overall Cal-Am Monterey District situation and the constraints under which the utility operates.

Staff Report

As a starting point for the staff's study of rate structure alternatives, Mr. Epolt accepted the water usage that was developed by the staff in the recent rate proceeding, Application No. 54942, and adopted by the Commission in Decision No. 86249.

Mr. Epolt divided this usage into three separate customer classifications: residential, business, and golf course service. He then proceeded to design three different rate schedules for each of the three classifications. For these new rate designs, he abandoned the existing minimum charge form and substituted a service charge form, whereby there would be a service charge, depending on the size of the meter, and quantity rates, depending on water usage. To give recognition to a lifeline concept, he proposed no charge for the first 300 cubic feet per month of usage under the residential schedule. The residential rate schedule therefore became a hybrid type with characteristics of both the minimum charge and service charge forms.

The service charges specified were the same for each of the nine schedules he developed, but the quantity rates were different, depending on both the customer classification and on the rate type assumed, namely inverted quantity rates, modified inverted rates, and uniform rates.

Each of the three rate types would produce the $3,627,400 gross revenues adopted in Decision No. 86249, assuming that there would be no overall revenue change resulting from the application of the revised rates.

Mr. Epolt's three alternatives are shown in the following table:

	Service Charge Per Meter Per Month
For 5/8 x 3/4-inch meter	$ 2.50
For 3/4-inch meter	2.75
For 1-inch meter	3.75
For 1-1/2-inch meter	5.25
For 2-inch meter	6.75
For 3-inch meter	12.50
For 4-inch meter	17.00
For 6-inch meter	28.00
For 8-inch meter	42.00

	Usage			Quantity Rates Per Meter Per Month		
	Residential Classification	Business Classification	Golf Courses	Inverted Rates a/	Modified Inverted b/	Uniform Rates a/
	Cubic Feet			$ Per 100 Cubic Feet		
First	300	-	-	No Charge	No Charge	No Charge
First	-	5,000	50,000	0.374	0.392	0.395
Next	700	-	-	0.374	0.392	0.395
Next	1,000	20,000	350,000	0.394	0.392	0.395
Next	3,000	475,000	400,000	0.414	0.392	0.395
Over	5,000	500,000	800,000	0.464	0.452	0.395

a/ Add $0.060 per 100 cu.ft. for First Elevation Zone and $0.090 per 100 cu.ft. for Second Elevation Zone.

b/ Add $0.058 per 100 cu.ft. for First Elevation Zone and $0.088 per 100 cu.ft. for Second Elevation Zone.

Customer usage characteristics were found to be as follows:

	% of Bills	% of Water Sold	Av. Mo. Cu.Ft. Per Customer	% 5/8"x 3/4" Meters	% 1" Meters	% Larger Meters
Residential	87	51	1,000	90	9	1
Business	13	43	5,000	60	21	19
Golf	Less than 0.1	6	350,000	0	0	100

The following tabulation summarizes cumulative billings and water use for gravity zone customers. These customers receive about 66 percent of bills and use 70 percent of water. Golf courses are located only in the gravity zone.

Monthly Cubic Feet	Residential Cumulative		Business, etc. Cumulative		Golf Cumulative	
	% Bills	% Water	% Bills	% Water	% Bills	% Water
300	16.9	3.0	-	-	-	-
1,000	64.7	33.5	48.0	4.0	-	-
2,000	90.4	68.1	65.3	9.2	-	-
5,000	98.9	90.8	83.0	20.7	7.5	0.1
25,000	-	-	96.9	51.2	-	-
50,000	-	-	-	-	44.8	6.2
400,000	-	-	-	-	90.1	58.8
500,000	-	-	99.9	91.5	-	-
800,000	-	-	-	-	98.4	88.8

Charges computed under the existing schedules and according to Mr. Epolt's three alternatives are illustrated in the following table:

Monthly Water Use	Existing Rate Charge	Inverted Rate Charge	Inverted Rate % Change	Modified Inver. Charge	Modified Inver. % Change	Uniform Rate Charge	Uniform Rate % Change
		RESIDENTIAL - 5/8 x 3/4-inch meter					
300 cu.ft. or less	$ 2.50	$ 2.50	0.0	$ 2.50	0.0	$ 2.50	0.0
1,000 cu.ft.	5.79	5.12	11.6	5.24	9.5	5.27	9.0
2,000 cu.ft.	10.49	9.06	13.6	9.16	12.7	9.22	12.1
5,000 cu.ft.	22.40	21.48	4.1	20.92	6.6	21.07	5.9
		BUSINESS - 5/8 x 3/4-inch meter					
300 cu.ft.	2.50	3.62	44.8	3.68	47.2	3.69	47.6
1,000 cu.ft.	5.79	6.24	7.8	6.42	10.9	6.45	11.4
2,000 cu.ft.	10.49	9.98	4.9	10.34	1.4	10.40	0.9
5,000 cu.ft.	22.40	21.20	5.4	22.10	1.3	22.25	0.7
25,000 cu.ft.	100.40	100.00	0.4	100.50	0.1	101.25	0.8
		GOLF * - 4-inch meter					
50,000 cu.ft.	163.75	204.00	24.6	213.00	30.1	214.50	31.0
200,000 cu.ft.	634.23	795.00	25.3	801.00	26.3	807.00	27.2
400,000 cu.ft.	1,261.53	1,583.00	25.5	1,585.00	25.6	1,597.00	26.6
800,000 cu.ft.	2,516.13	3,239.00	28.7	3,153.00	25.3	3,177.00	26.3

* With 15 percent discount applied to existing rates only.

The alternate rate proposals do not provide any discount for employees or for service to golf courses.

Mr. Epolt explained that he proposed a service charge rate so that a customer requiring a large meter would pay for the maintenance and depreciation of the meter, and not have these costs absorbed in the normal use as in the present minimum charge schedule. Secondly, the service charge rate form has an advantage that the customer pays for all water used (except for the residential lifeline allowance as explained earlier). The feature of the customer's paying for all water used is particularly important under the limited water supply situation of the Monterey District.

Mr. Epolt pointed out that his inverted rate schedule would, because of the generally low level of usage of most customers compared to the system average use, result in lower bills for approximately 90 percent of billings. Because of the unusual usage characteristics of the Monterey District, whereby a few customers, such as the golf courses, use large amounts of water, and the typical residential customer uses less water than in most other California systems, Mr. Epolt designed his modified inverted schedules to have a uniform rate for each classification until 90 percent of the water sales had been reached, and then a higher tail block rate.

The cubic feet blocking varies for the three classifications to reflect the recorded use and the average needs of water for each customer group.

In designing his three alternatives, Mr. Epolt made no allowance for price elasticity. He was of the opinion that any lowering of rates for the residential users would not increase use because use by this type of customer depends on habit. He did think that the increasing of rates for larger uses would tend to encourage conservation, however, but he had no data or experience upon which to make an estimate of the amount of conservation that could be expected.

In evaluating the three alternatives, Mr. Epolt felt that an inverted rate schedule could penalize a large user, such as a housing development or mobile home park served through a single connection. Inverted rates also have a disadvantage in the kind of leverage that they exert on utility revenues. When water usage or demand, as the term is used in the economic sense, increases, revenues increase disproportionately. Should conservation cause usage to decrease significantly, revenues would drop faster than usage, and well intentioned conservation efforts could result in financial difficulties for the utility.

Mr. Epolt testified that, in his opinion, a service charge with a uniform commodity rate was the fairest because the customer paid the costs associated with his meter and the same rate regardless of the use to which the water was put, without any judgments as to what quantities were appropriate for each usage classification. He also felt that a uniform quantity rate would provide some incentive to large users to hold their consumption down.

Mr. Epolt made a study of actual revenues realized from service under the Del Monte contract and corresponding imputed revenues. Del Monte Properties takes approximately 3-1/2 percent of the Monterey District's water sales. Usage and revenues for a normal water year are as follows:

Usage	241,220 ccf
Revenues at:	
Contract Rates	$ 26,670
Filed Rates *	80,630
Inverted Rates	100,180
Mod. Inv. Rates	99,370
Uniform Rates	99,420

* Using a 15 percent discount for 225,510 ccf taken for golf course irrigation.

Mr. Epolt was questioned about the reasonableness of the present rates. He replied that, based on his review of the cost of service study made in connection with the last rate case, it appeared to him that the present rates ordered by Decision No. 86249, including the discounts for golf courses and employees, were justified on a cost basis.

At the completion of Mr. Epolt's testimony, the staff counsel, Lionel Wilson, stated that it was the position of the staff that imputation of phantom revenues from Del Monte properties was no longer a valid concept. He declared that Cal-Am's predecessor had received water rights through the contract which are not in the rate base, and on which Cal-Am and its predecessors have not been able to earn. He pointed out that, without the right to dam the Carmel River, the water situation on the Peninsula would be very bleak.

Cal-Am's Rate Recommendations

Cal-Am's rate recommendations were made by Chesly G. Ferguson, P.E., a retired vice president of California Water Service Company and former general division engineer of the Utilities Division of the Commission staff. Mr. Ferguson testified that he had made his own rate studies and also reviewed those of Mr. Epolt. His results came within $300 of those of Mr. Epolt so his own were not presented.

Mr. Ferguson strongly recommended placing a uniform quantity-surcharge rate form into effect, as being a more equitable rate.

Mr. Ferguson said that there was no possible way that a predetermination could be made of the conservation of water which would result from the combined effect of the various conservation programs presently in effect or proposed and from any change in rate structure. He said that such a determination could only be made in retrospect. Without such a quantitative determination, it was necessary for him, and Mr. Epolt, to design rate proposals excluding allowances for conservation.

He testified that, because the low water supply problem was a community-wide problem, it did not seem appropriate or equitable, at least in his opinion, that the utility should underwrite the advantages to the public, through losses in its earnings, of the water conservation program. The effect on earnings would be accentuated by a change in rate structure, either to an inverted rate or uniform rate structure because the reduction in sales would probably occur in the higher quantity blocks where the rates would be higher than the present low rate blocks.

To furnish some protection to the utility and avoid the problem of retroactive ratemaking, Cal-Am, through Mr. Ferguson, was requesting the Commission to allow a surcharge of $.02 per ccf which would be placed in an impound account. After one year of service under the new rates, the disposition of the surcharge and the impound account could be decided by an advice letter filing based on the then known facts.

Positions of Other Parties

Del Monte filed a brief in which it strenuously opposed the staff and utility recommendations. Del Monte submitted that the staff report shows the following:

1. 51 percent of all water sold in the district is for residential use.

2. Staff's recommendation would result in a rate reduction of approximately 10 percent for all residential users.

3. The most conspicuous large users, golf courses, use 6 percent of the water sold.

4. Staff's recommendation would increase rates to golf courses by at least 25 percent.

5. Staff's recommendations would not have an economic effect on the average commercial customer.

Del Monte argues that, if there is any validity to the concept of price elasticity, and the staff says there may be, it is totally preposterous to believe that conservation will be aided by giving a price reduction of 10 percent to a group using 51 percent of the total volume of water and a 25 percent increase to a group using 6 percent of the water. This becomes even more incredible when it is considered (as staff did not) that this latter group has already voluntarily effected a 20 percent reduction in usage and thus already minimized its use.

To Del Monte it is unreasonable to assume that further major reductions in consumption can be achieved even through such a major price increase as proposed by staff. The more probable result of the staff's proposal is that overall water consumption in the district would increase because of increased demand in the residential sector.

In arriving at any decision concerning rate structures in the Monterey District, extreme care should be taken to insure that a rate design generally appropriate during normal times is also appropriate under existing conditions, Del Monte asserts. It reminds the Commission that it has previously concluded that there is a severe water shortage in the area. The severity of the shortage is such that curtailment has been imposed as an emergency measure. In order to meet the existing emergency situation, and as a part of the existing curtailment orders, the District's largest consumers, the golf courses, have implemented programs designed to reduce their water consumption to 80 percent of what was used in the year 1972. Because the situation is primarily the result of Cal-Am's failure to expand system facilities to the extent necessary to meet the existing and future needs of the service territory, the problem will not be completely alleviated simply by the resumption of normal rainfall. Even after normal rainfall has replenished the existing sources, because of Cal-Am's capacity restraints, Del Monte

submits that it will remain imperative that excessive use not be encouraged by granting a rate decrease of approximately 10 percent to consumers using over 50 percent of the total water volumes consumed.

Del Monte further argues that because of provisions of Section 454 of the Public Utilities Code, relating to notice that must be given by public utilities filing applications for rate increases, due process requires that the ratepayers receive a similar notice of the staff rate restructuring proposal in this case.

David L. Hughes, chairman of a voluntary association known as Lot Owners Without Benefit of Land or Water (LOWBLOW) representing lot owners who, under the terms of our Second Interim Decision No. 84527, are unable to receive water service, questioned Mr. Ferguson as to the basis of his assertion that the low water supply problem is a community-wide problem, since it results from the failure of Cal-Am to augment its transmission facilities when it knew in 1968, from the Kennedy Engineers report, that such augmentation would be required in 1970.[14] Mr. Hughes contended that the inability of Cal-Am to deliver water, therefore necessitating conservation measures, should not be rewarded by a surcharge to make up for revenues that it would not realize because it could not transmit sufficient water through its constricted transmission facilities.

Rate Structure Consideration

After careful consideration of the staff and company showings and of the positions of the other parties, we conclude that it would not be prudent, under present circumstances, to make any changes in rate structure at this time. The primary factor behind this conclusion is our desire not to further widen the gap between the phantom revenues that we impute to Cal-Am and the real dollar revenues received.

14/ See Decision No. 84527, mimeo. pages 46 and 47.

In Decision No. 86249, our last rate decision for all of Cal-Am's operating districts, we adopted the staff's method of estimating revenues by pricing out water consumption according to type of customer and amount used. The presently effective rates, as authorized by Decision No. 86249, and the alternate rates designed by the staff were all designed to produce the revenues based on normal consumption for the year 1975.

As noted above, because of our water conservation and rationing orders, and voluntary restraint in water use, particularly by large water users such as the golf courses, water consumption by the larger users has declined. A shifting of the revenue requirement to the present tail block would have the effect of attributing revenues to water consumption that is no longer taking place. It would obviously also widen the gap between revenues imputed Del Monte service and the revenues actually received.

Although Cal-Am acquired the Monterey District properties with a full knowledge of the Del Monte contract and its regulatory implications, we do not, considering the tasks faced by the utility in augmenting its facilities, deem it appropriate to add an increase in imputed revenues to the other burdens that Cal-Am, and through it American Water Works, have assumed as a result of acquiring Cal. Water & Tel.'s water properties.

A secondary consideration supporting a conclusion not to restructure rates at this time is the point raised by Del Monte that the large users, especially the golf courses, have made significant reductions in their use of water in response to the water conservation and rationing programs instituted in response to our fourth and fifth interim decisions in this proceeding. Recognizing that these reductions were made by the large users in their own enlightened self-interest, it still does not seem fitting to reward these efforts with a significant rate increase, particularly when it

appears that the present rates are sufficient to recover the cost of service. There may also be some merit to Del Monte's contention that a 10 percent reduction for most residential customers could tend to promote consumption for that class.

In our two decisions dealing with water conservation we did not explain our solicitude for the golf course customers. Since the mysterious disappearance of the Monterey sardine in the early 1940's, the Peninsula has been without a basic industry to serve as a source of employment. The economy of the area now is very largely dependent on catering to personnel stationed at several military and naval installations and to visitors, many of whom are attracted by the world renowned golf courses. Should the courses become unusable or uneconomic, the employment of many people, most of them relatively unskilled persons employed by the many purveyors of food and lodging, would be severely affected, and the ripple effect would be felt by most of the local businesses.

Because of our action in maintaining the present rate structure, we need not consider the merits of Cal-Am's proposed surcharge or Del Monte's contention that we are precluded, at this time, from restructuring rates by Section 454 of the Public Utilities Code.

In closing this discussion of rate structure we should note our previous remarks in Second Interim Decision No. 84527 that our expansion of Case No. 9530 to include rate structure, was prompted by the need to consider how the cost of required new facilities can be supported through rates. The facilities that will ultimately be required to provide adequate water service may require substantial revisions in rate forms, possibly including acreage and connection charges.

INVESTIGATION OF AMERICAN WATER WORKS AND CAL-AM FINANCES

Background

In our Second Interim Decision No. 84527 we narrated the financial history of Cal-Am, and described its relationship to American Water Works, the Delaware holding company that owns all of Cal Am's capital stock, insofar as that information was available in Cal-Am's annual reports to the Commission and in the record in Cal-Am's Application No. 48170 to acquire the water properties of Cal. Water & Tel. We described the financial burden with which, in 1966, Cal-Am commenced operations, and we also described that of the $41,734,768 purchase price only $29,449,397 represented earning assets, the remaining $12,285,371 being carried as a non-earning plant acquisition adjustment. We related that Cal-Am had, as of December 31, 1974, expended over $4,000,000 for condemnation litigation involving its Sweetwater District properties in San Diego County.[15/] Further, we described how American Water Works had never, since the organization of Cal-Am, invested any additional funds in Cal-Am's capital stock. We noted that, until Cal-Am's Board of Directors (all of whom are officers or employees of American Water Works or its service subsidiary) decided that Cal-Am was receiving revenues from all of its operating districts sufficient to provide a return on equity attractive enough to serve as an incentive for further investments by American Water Works, the holding company did not, despite the assurance given by its president at the 1966 hearings, intend to invest any such funds.

In the order in Decision No. 84527 we expanded our investigation in Case No. 9530 to include Cal-Am's finances and its relationship to

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15/ Rate base value of the Sweetwater properties being condemned was $10,598,037.

American Water Works, insofar as these subjects affect the adequacy of the water supply of the Monterey District. We also directed the Finance and Accounts Division of the Commission staff to investigate these topics and prepare a report for our consideration.

In Decision No. 86249 dated August 17, 1976, which disposed of Cal-Am's rate increase Application No. 54942, we again considered Cal-Am's capital structure in connection with our determination of a reasonable rate of return. Because of the essential nature of the Monterey construction projects and to make certain that adequate funds would be available for construction projects in other districts, we granted Cal-Am a 9.2 percent rate of return, 0.3 percent above the staff recommendation. We noted that this rate of return will provide applicant with annual gross revenues of about $250,000 more than would have been derived under the staff recommended rate of return; more importantly it will increase Cal-Am's bondable capacity by more than $1 million. We ordered Cal-Am to maintain, until further order of the Commission, a recorded capital structure in which long-term borrowings from non-affiliates shall not represent more than 50 percent of its total capital structure.

We also found, in Decision No. 86249, that a 9.2 percent rate of return was reasonable only if substantial progress on the Monterey District's construction projects was indicated within 120 days after a final EIR for the Begonia and Canada projects had been issued. Should such progress not transpire, authorized rates based on a 9.2 percent rate of return were, for all districts except Monterey, to be lowered so as to yield 8.6 percent. For Monterey authorized rates would revert to the prior rates until such time as it is indicated that a water supply adequate for future needs would be available to customers in the Monterey service area.

Staff Report

At the August 25, 1976 hearing, Financial Examiner II Raymond Charvez presented two exhibits, the first, dated August 13, 1976, being the report that we had required by Decision No. 84527 and the second, a supplementary exhibit which was comprised of tables corresponding to tables on the August 13 staff report but revised to reflect the results that we adopted in our Cal-Am rate Decision No. 86249 dated August 17, 1976.

The staff report explored the following methods of financing that it considered to be available to Cal-Am:

1. Equity financing.
2. Debt financing.
3. Interim bank loan.
4. State debt financing pursuant to California Safe Drinking Water Bond Act of 1976.
5. Internally generated funds.

In addition the staff noted that construction funds could be obtained from Cal-Am's customers, either directly by means of a surcharge to water bills or indirectly through the inclusion of construction work in progress in the rate base.

The staff report concluded by recommending that:

1. Cal-Am be ordered to stop paying dividends and not transfer any funds to its parent, American Water Works, until the near-term phase facilities are put into service in its Monterey District.
2. Cal-Am be ordered to investigate all possible methods of financing including applying for a loan through Proposition No. 3, the California Safe Drinking Water Bond Act of 1976, as approved at the June primary election, and report to this Commission of their inquiry.

3. Upon receiving a general rate relief decision from this Commission, Cal-Am be ordered to immediately negotiate a line of credit for the purpose of interim financing the construction of the facilities without delay.

4. The customers in the Monterey District should not be required to contribute by means of a surcharge.

None of the parties had cross-examination questions for Mr. Charvez.

Cal-Am Showing

Robert W. Bruce, Cal-Am's vice president finance, treasurer, and secretary testified in rebuttal to Mr. Charvez. He presented two exhibits, one of which was designed to expand upon, and to clarify the staff report. The second was intended to clarify a cash flow table in the staff's supplementary report.

The material in Mr. Bruce's exhibits was of an accounting and statistical nature. His recommendations were confined to his oral testimony.

In his oral testimony Mr. Bruce commented on the staff alternatives and recommendations. He was in favor of including construction work in progress in the rate base but would not recommend a surcharge to rates. He reported that Cal-Am had contacted the DWR regarding availability of safe drinking water bond funds. He also said that Cal-Am had an appointment with the Bank of America to commence preliminary negotiations toward obtaining a line of credit.

Regarding the staff's recommendation that Cal-Am be ordered to cease the payment of dividends, Mr. Bruce referred to a statement made previously by O. L. Banz, Cal-Am's president,[16] in which

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16/ Mr. Hays having retired since issuance of Decision No. 84527.

Mr. Banz stated that, should such a dividend prohibition occur, there would be no real likelihood that anyone would ever consider investing in Cal-Am and the desperately needed pipeline and iron renewal plant will be delayed or perhaps never be accomplished.

Financial Requirements

Cal-Am's forecast of its needs for external financing, as summarized by Mr. Bruce from various exhibits in Cal-Am's recent rate application is shown in the following table:

CALIFORNIA-AMERICAN WATER COMPANY

Forecast Capital Budget

Estimated Cost of New Plant Required in Excess of Plant Installed by Use of Internally Generated Funds
(Dollars in Thousands)

District	A.54942 Exhibit Number	1975	1976	1977	1978	1979	Five Year Total
Coronado	66	$ 91.0	$110.0	$ 50.0	$ 50.0	$ 50.0	$ 351.0
Sweetwater	72	1,243.5	361.0	606.0	406.0	200.0	2,816.5
Baldwin Hills	38	3.6	-	-	-	-	3.6
Duarte	59	12.3	-	-	-	-	12.3
San Marino	53	45.0	-	-	-	-	45.0
Monterey Peninsula	23	820.1	299.0	2,536.0	-	-	3,655.1
Village	46	-	49.2	-	-	-	49.2
Total Company		$2,215.5	$819.2	$3,192.0	$456.0	$250.0	$6,932.7

Since no external financing has occurred since these estimates were made, the forecasted capital expenditures have been postponed.

The Sweetwater District is the only district, other than Monterey, requiring a large infusion of outside money, most of which is needed for a large diameter transmission main.

Cal-Am's latest estimate of the construction costs of the Canada and Begonia projects, together with a cost estimate of intermediate phase plant additions, as prepared by Albert I. Bennett, P.E., of American Water Works and presented by Mr. Bruce is as follows:

CALIFORNIA-AMERICAN WATER COMPANY

Estimated Cost of Proposed Monterey Peninsula District Plant Additions at 1973 Price Levels
(Dollars in Thousands)

Near-Term Phase		
Canada De La Segunda Transmission Pipeline	$3,000.0	
Begonia Iron Removal Plant	970.0	
Well Improvements	68.0	$4,038.0
Intermediate Phase		
Three New Wells	$ 380.0	
Treatment Plant	847.0	$1,227.0
Total		$5,265.0

Cal-Am's most recent estimate of 1976 total system wide construction expenditures is $2,077,000, (not including the Begonia and Canada projects) of which $1,520,000 for routine main extensions would be financed by advances and contributions, for a net requirement of $557,000.

From the above discussion it can be seen that Cal-Am must raise, over the next five years, approximately $7,000,000 in outside financing, including some money from advances and contributions. For 1976, it must finance $557,000 for normal construction, exclusive of capital expenditures for the Begonia and Canada projects, from internally generated funds and from outside financing.

Financial Prospects

Having developed, from the record, a picture of Cal-Am's financial requirements, we will proceed to examine its prospects of meeting these requirements, particularly insofar as they pertain to Cal-Am's ability to finance the needed Monterey facilities.

Financial Prospects - Equity

Although Cal-Am's recorded capitalization at December 31, 1975 shows a common equity ratio of 49.3 percent in actuality, when the nonearning components representing the unamortized acquisition adjustment ($9,100,000) and the deferred costs of the Sweetwater condemnation case ($4,100,000) are deducted from common equity, the common equity component of Cal-Am's capital structure is reduced to 33.8 percent. The staff believes that some improvement in the equity component of the capital structure is necessary if Cal-Am is to regain a viable credit position and be able to finance at a reasonable cost in the near future.

The following tabulation from the staff report shows Cal-Am's capital structure on three bases: as recorded at December 31, 1975, with the common equity reduced by the amount of the unamortized acquisition adjustment, and with the common equity reduced by the amount of the unamortized acquisition adjustment plus costs of the Sweetwater condemnation suit:

Item	Capitalization at December 31, 1975		
	Recorded	Adjusted[a]	Adjusted[b]
	(Dollars in Thousands)		
Debt	$28,600	$28,600	$28,600
Common Equity	27,800	18,700	14,600
Total Capitalization	$56,400	$47,300	$43,200
Percentage of Total			
Debt	50.7%	60.5%	66.2%
Common Equity	49.3	39.5	33.8
Total Capitalization	100.0%	100.0%	100.0%

a/ Adjusted to eliminate $9,100,000 acquisition adjustment from common equity.

b/ Adjusted to eliminate $9,100,000 acquisition adjustment and $4,100,000 cost of Sweetwater condemnation from common equity.

Mr. Bruce testified that Cal-Am has no plans to issue additional equity and that its position regarding issuance of equity securities remains unchanged from the positions described in our Second Interim Decision No. 84527.[17/]

Since the board of directors of Cal-Am is comprised exclusively of officers or employees of American Water Works it is not unreasonable to conclude that Cal-Am's refusal to issue equity is a result of the holding company's reluctance to invest any of its own funds in its wholly owned California subsidiary.

American Water Works' abhorrence of Cal-Am's equity does not extend to the holding company's other operating subsidiaries. In its 1975 Annual Report to Stockholders, American Water Works made the following statement:

> "An essential element in the sale of capital securities by System operating companies is an adequate common equity ratio. Although retention of earnings by the subsidiaries assists in the maintenance of minimum equity ratios, additional common equity is required when substantial amounts of other securities are being offered for sale. The Company proposes to add $20,000,000 to the common equity of subsidiaries through the purchase of common stock. In this respect, the Company has arranged to borrow up to $25,000,000 from two banks under agreements which provide for a maturity date of November 1, 1978 for the borrowings, and the payment of interest based on the prime rate, adjusted as it fluctuates, plus a maximum of 1/2%. Borrowings under these agreements amounted to $5,000,000 at the end of 1975.
>
> "Utilizing the proceeds from the bank borrowings and other available funds, the Company increased its investments in securities of subsidiaries by purchasing common stocks in the aggregate amount of $6,000,000 from four operating companies. . . ."

17/ D.84527, mimeo. pp. 49 through 57.

The record contains American Water Works Annual Report Forms 10-K as filed with the Securities and Exchange Commission for the years 1973, 1974, and 1975. These reports show that in the last four years the holding company invested $40,077,000 in the securities, (mostly common stock) of its subsidiaries, as follows:

Year	Amount
1972	$11,719,000
1973	8,028,000
1974	13,432,000
1975	6,898,000

Financial Prospects - Funded Debt

Under the terms of the First Mortgage Bond Indenture, Cal-Am's net earnings available for interest coverage must be equal to at least 1.75 times the aggregate annual interest charges on all long-term debt, including the proposed new issue. With respect to the future issuance of debentures, the debenture indenture requires that interest coverage must be at least 1.5 times the annual long-term interest expense including the proposed new issues. Both of the indenture interest coverages are based on pre-tax calculations.

Times interest coverage is calculated by adding net income, interest charges, and income taxes together and then dividing the resulting sum by the annualized interest costs of outstanding long-term debt.

According to a pro forma calculation by the staff, the 9.20 percent adopted rate of return from Decision No. 86249 would provide, 12 months after the decision's effective date, a mortgage bond interest coverage of 1.99 times. This rate of return of 9.20 percent should provide additional debt capacity of $3,397,000.

Mr. Bruce determined that using the 1975 normalized test year and 9.2 percent rate of return adopted in Decision No. 86249, interest coverage on long-term debt would be 1.96 times. On a recorded twelve months ended June 30, 1976, adjusted to reflect the

rate increase on a pro forma basis, the long-term debt interest coverage dropped to 1.65 times, or to a level below the 1.75 required by the mortgage bond indenture. This drop was caused by the necessity, because of a drier than normal year, to purchase water for the Sweetwater District at a cost of approximately $240,000.

According to Mr. Bruce the resulting 1.65 times coverage precluded the issuance of first mortgage bonds. The utility would, however, still be able to issue debentures. Mr. Bruce believed that, by paying an interest rate of 11 percent, Cal-Am could issue $2,300,000 of debentures before it would come against the required 1.5 times interest coverage.

Financial Prospects - Interim Bank Loan

Interim bank financing is a common method used by utilities to finance construction. The usual procedure is for the utility to arrange for a line of credit from a large bank, and then draw on the credit to meet construction expenditures. When the drawings are completed, the utility arranges for debt or equity financing, or both, and pays off the bank loan.

Cal-Am's policy is to employ interim bank financing and it is presently seeking a line of credit from the Bank of America. The amount of credit that will be extended will, of course, not be known until the arrangements are completed. In the past, however, Cal-Am has been able to obtain, from this bank, lines of credit ranging from $500,000 to $3,000,000. A line of credit would give Cal-Am interim financing and sufficient time to increase its earnings under its new rates to meet the requirements of its first mortgage and debenture indentures. The utility could, should Commission authorization be obtained, then retire its short-term debt with permanent funding obtained from long-term debt and common equity.

Financial Prospects - Internally Generated Funds

Broadly stated, internally generated funds are the money that is left over after cash payments are made. In the usual situation they are comprised of retained earnings and depreciation, and are analogous to the savings of a family unit. In Cal-Am's case there is also available the amortization of certain preliminary surveys and investigations. Since depreciation and amortization represent the write-off of previous expenditures that were carried in the asset side of the books, they represent no cash outlay, and the money they represent is available for investment on plant.

The following table shows a comparison of the cash flow estimates of the staff and Cal-Am. The differences arise from the staff's use of data from rate increase Decision No. 86249 whereas Cal-Am used recorded data. The recorded net operating revenues were lower than the normalized, principally because of the necessity of purchasing water for the Sweetwater District because of reduced runoff from the watershed of the Sweetwater River.

CALIFORNIA-AMERICAN WATER COMPANY

COMPARATIVE PRO FORMA CASH FLOW
ANALYSES @ 9.20% RATE OF RETURN
YEAR 1975

Line No.		Staff Normalized Basis (Dollars in	Cal-Am Recorded Basis Thousands)
1	Rate Base	$39,744.0	$ -
2	Rate of Return	9.20%	-
3	Net Operating Revenues	$ 3,656.4	$3,384.1
4	Add: Depreciation	1,334.7	1,285.5
5	Amortization	292.5	292.5
6	Total Funds	$ 5,283.6	$4,962.1
7	Less: Interest Expense	2,489.9	2,544.7
8	Sinking Funds	430.0	430.0
9	Advance Refunds	512.0	512.0
10	Total Deductions	$ 3,431.9	$3,486.7
11	Cash Flow Available for Construction	1,851.7	1,475.4
12	Estimated Construction Expenditures - 1976	$ 2,077.0	$2,077.0
13	Less: Advances and Contributions	1,520.0	1,520.0
14	Net Cost to Company	$ 557.0	$ 557.0
15	Cash Flow Available for Monterey (Line 11-Line 14)	$ 1,294.7	$ 918.4
16	Less: Pro forma Dividend Payments	874.9	629.6
17	Retained Earnings at 75% Payout Available for Monterey	$ 419.8	$ 288.8

Both the normalized and the pro forma recorded approaches have merit. The normalized results are indicative of what can be reasonably expected over the years. The most recent recorded results may be the ones that a bank will look at. A favorable water year both lessens the need for and greatly facilitates bank financing.

Without a dependable long-range weather forecast, we have no way of predicting what the actual results for the next few years will be. Accordingly, for our consideration of cash flow and internally generated funds we will accept the staff's normalized basis. Net income, obtained by deducting interest expense from net operating revenues would be $1,166,500 on the staff's normalized basis and dividends at a 75 percent payout ratio would be $874,900.

Cal-Am has maintained, since its inception, a policy of paying out 75 percent of its net income to the holding company, American Water Works. Originally it paid out 75 percent of the previous year's net but, in the third quarter of 1975, it commenced paying out 75 percent of the previous quarters' income.

Payment of $874,900 in dividends would leave $419,800 available, on a normalized basis, from internally generated funds.

Over the nine and three quarter years between its formation and December 31, 1975, Cal-Am earned $7,748,600 and paid out $5,890,000, or 76 percent, of its earnings in dividends to the holding company. In addition, Cal-Am invested $4,100,000 in its Sweetwater condemnation litigation. Over the last nine and three quarters years, book value of Cal-Am's stock, including the Sweetwater condemnation costs as an "asset", increased from $102 to $111, an increase of 8.8 percent or a compound annual rate of 0.87 percent. Book value of American Water Works common, over the 10 years ended December 31, 1975, increased from $11.64 to $17.11, a 47 percent increase, or a compound annual rate of 3.93 percent.

Over the last ten years Cal-Am has contributed $7,748,000 to the $140,462,000 consolidated net income of American Water Works and its subsidiaries, or 5.52 percent. Over the same period it contributed $5,890,000 of the $62,510,000 in common and preferred dividends paid by the holding company to its stockholders, or 9.42 percent of the dividends paid out.

The ratio of American Water Works preferred and common dividends to consolidated net income amounted to 44.50 percent, compared to the 76 percent ratio of Cal-Am for the same period.

If we apply the holding company's consolidated payout ratio of 44.50 percent to Cal-Am's $7,748,000 net income earned since 1966, we find that Cal-Am's share of the dividends paid by American Water Works was $3,447,860. It then follows that the $2,442,140 difference between the $5,890,000 in dividends paid out by Cal-Am to the holding company, and Cal-Am's $3,447,860 pro rata share of the holding company's dividends was invested in American Water Works' other subsidiaries or used to retire the holding company's preferred stock and debt.

Appraisal of Financial Prospects

The refusal of the holding company to contribute to Cal-Am's equity capital means that required construction funds must either be borrowed, saved, or obtained from customers through higher rates.

In our Decision No. 86281 dated August 24, 1976, in Pacific Gas and Electric Company's (PG&E) Applications Nos. 55509 and 55510 for higher rates for its Electric and Gas Departments, we discussed the inclusion of construction work in progress in the rate base. In that decision, while denying construction work in progress in rate base,

we recognized that timely inclusion in rate base of significant additions to plant is a subject that is not well suited to current ratemaking procedures, and we invited interested parties to comment on how we might devise a procedure appropriate for all utilities. We recognized that, with the unprecedented demands for new capital presently confronting utilities, they are obliged to seek new and different methods of financing, including customer participation in raising funds for plant construction. At the same time, we expressed a continuing concern that because of the impact of income taxes proposals such as inclusion of construction work in progress in rate base require more than two dollars of added revenues from customers for each dollar of additional cash flow finally made available to the utility. We urged applicant to explore carefully all methods of customer participation in meeting financing needs that would eliminate this "two-to-one" tax effect.

The inclusion of construction work in progress in the rate base would not be self-executing, but would require the imposition of higher rates. Before deciding on the subject of including construction work in progress in the rate base, or of imposing a surcharge, both of which involve the "two-to-one" tax effect, we would like to consider the responses that we may receive from the invitation made in Decision No. 86281.

Unless Cal-Am should sell more stock the only other method of external financing available is to borrow money. There is a significant gap between the 1.99 times interest coverage predicted by the staff on a normalized basis and the 1.65 pro forma recorded basis presented by Mr. Bruce. Whether the trustee under the bond indenture would decide that Cal-Am met the 1.75 times test and permit the issuance of additional bonds is a question that only time will answer. In the event that the staff proves to be correct, and should the Commission permit, Cal-Am would probably be able to issue approximately $3,400,000 in bonds or debentures.

Should Cal-Am be unable to issue bonds, it appears that it could, at a minimum, issue the $2,300,000 on debentures predicted by Mr. Bruce.

As explained above, Cal-Am's ability to obtain interim bank financing depends on its being eligible for permanent financing. Should the bank's loan officer conclude that Cal-Am would be unable to refinance its bank loan with permanent capital, the prospect of obtaining a loan from that bank would be remote.

As shown earlier in our discussion of Cal-Am's prospects of obtaining equity financing, Cal-Am's recorded percentage of debt to total capital as of December 31, 1975 amounted to 50.3. The utility is thus already slightly over the 50 percent ratio prescribed by our Decision No. 86249. At least half of the funds required for the Canada and Begonia projects must therefore be

obtained from retained earnings or new equity. We have seen that the near-term phase of these projects will require capital expenditures of $4,038,000 over a 24-month period. We have also seen that Cal-Am's 1976 systemwide financial requirements will be approximately $557,000, excluding the cost of the Begonia and Canada projects. Thus annual capital requirements over the next two years will be approximately $2,576,000.

Absent an infusion of equity from American Water Works, and assuming that Cal-Am's 75 percent dividend ratio is maintained, at least half, or $1,288,000, of these annual financial requirements must be met through retained earnings. The $418,800 available from this source will not be adequate, a shortfall of approximately $869,200. Should dividends be restricted, $1,294,700 on a normalized basis would be available. The remaining funds could be financed by debt securities, the 50 percent limitation maintained, and the project financed.

The Commission thus faces four choices:

1. Relax the 50 percent debt limitation.
2. Increase Cal-Am's rates to a point where it would finance from retained earnings, while maintaining the present 75 percent dividend payment policy.
3. Direct Cal-Am to issue equity securities.
4. Order Cal-Am to curtail dividends.

In view of the circumstance related in this order and in Decisions Nos. 84527 and 86249, we are of the firm opinion that it would be most unwise and imprudent to relax the 50 percent limitation.

A raising of rates, systemwide or in the Monterey District alone, to permit Cal-Am to maintain a 75 percent dividend payment and still meet its financial requirements would require rate increases to levels that would not meet the tests established for just and reasonable rates.[18/] Assuming that such a procedure were to be legal it does not meet our concept of fairness.

The question of requiring Cal-Am, by formal Commission order, to issue equity securities has not been raised at hearings nor argued in briefs in neither Case No. 9530 nor Application No. 54942. This alternative therefore will not be considered in this decision.

It thus appears that the only alternatives open to the Commission are to back off from the 50 percent debt limit or restrict the payment of dividends until such time as Cal-Am's finances indicate their restoration.

Arguments Concerning Authority of Commission to Restrict Payment of Dividends

Cal-Am, in a legal memorandum filed October 13, 1976, contends that:

> "[A]ccording to unambiguous rulings of the California Supreme Court, the staff's recommendation, if adopted, would be unlawful.
>
> "As a regulatory agency, the jurisdiction and police power of the Public Utilities Commission are limited to that authorized by legislation or judicial precedent. No enabling statute

18/ Public Utilities Code Sec. 451, Federal Power Commission et al. v Hope Natural Gas Co. (1944) 320 US 591, 605; 88 L ed 333, 346.

> empowers the Commission to determine the propriety of dividend payments by a public utility under the California Corporations Code; by statute that right is reserved exclusively to the corporation's board of directors. No statute authorizes the Commission to veto the reasonable business judgment of management regarding the conduct of such internal affairs of the corporation as the method of financing and paying for capital improvements and other services, nor is the Commission empowered to substitute its judgement for that of management in that regard. To the contrary, the California Supreme Court has unambiguously reaffirmed that the determination of such purely internal business matters is the exclusive and absolute right and responsibility of management, not the Commission. Finally, no statute satisfying the requirements of the federal constitution allows the Commission to confiscate the property of corporate shareholders without due process or just compensation."

As authority for those contentions Cal-Am cites Pacific Telephone & Telegraph Co. v Public Utilities Commission (1950) 34 Cal 2d 822, 828, 830; Pacific Telephone & Telegraph Co. v Public Utilities Commission (1965) 62 Cal 2d 634, 653; California Water & Telephone Co. v Public Utilities Commission (1959) 51 Cal 2d 478, 495; Corporation Code Sections 1500, et seq.; and Richards v Pacific Southwest Discount Corp. (1941) 44 CA 2d 551, 558.

Cal-Am also cites, as Commission precedents In the Matter of Pacific Gas & Electric Co. (1932) 38 CRC 252, 259 and In the Matter of Venice Consumers Water Co. (1924) 24 CRC 880, 883.

In response the staff admits that there is no specific statute or judicial precedent which would authorize the Commission to prohibit the payment of dividends. The staff reminds us, however, that the Commission has, under Section 701 of the Public Utilities Code, not only the powers and duties expressly specified, but also all powers necessary to enable it to carry out fully and effectively all purposes set forth in the Constitution and by statute.[19/]

The staff also argues that Sections 816, 817, and 851, which charge us with "supervision, regulation, restriction, and control" over issuance of securities and transfer or merger of utility property, give us the power to control the capital structure of utilities under our jurisdiction, both as to increases or decreases therein. The staff advises that the power to enter an order affecting capital structure, such as an order prohibiting the payment of dividends, is to be implied and is necessarily incidental to the right of the Commission to approve and supervise the issuance of stocks, bonds, and other evidences of indebtedness. When Section 701 is considered in conjunction with those sections dealing with the Commission's authority to regulate service and financing, it seems clear to staff that the Commission has the authority to order a utility not to pay out dividends until inferior and inadequate services are made reasonable.

The staff believes that the leading case upon which Cal-Am relies, Pacific Telephone & Telegraph Co. v Public Utilities Commission (1950) 34 Cal 2d 822, is not controlling.

19/ Public Utilities Code Section 701:

> "The Commission may supervise and regulate every public utility in the State and may do all things, whether specifically designated in this part or in addition thereto, which are necessary and convenient in the exercise of such power and jurisdiction."

Cal-Am quoted the following passage from the 1950 PT&T Supreme Court decision:

> "If the Commission is empowered to prescribe the terms of contracts and practices of utilities and thus substitute its judgement as to what is reasonable for that of management, it is empowered to undertake the management of all utilities subject to its jurisdiction. It has been repeatedly held, however, that the Commission does not have such power." (Pacific Telephone & Telegraph Co. v Public Utilities Commission (1950) 34 Cal 2d 822, 828.)

The staff believes, however, that the facts in the present case are distinguishable from that case. First of all, in Decision No. 86249 the Commission has ordered that Cal-Am shall maintain a capital structure in which long-term borrowings from non-affiliates shall not represent more than 50 percent of its capital structure. By so ordering, it seems to the staff that the Commission is attempting to protect Cal-Am's capital structure from impairment. The 1950 PT&T case specifically recognized the Commission's power to disregard the corporate entity and make managerial decisions where the capital of a utility could be impaired and thus its ability to serve the public might be weakened.

The staff reminds us that there is no doubt that Cal-Am has not met the required standards of service in its Monterey District, and as we noted in Decision No. 84527, "Monterey's water problem is not lack of water but lack of funds." (Page 48, mimeographed copy of Decision No. 84527.) According to the staff, during the hearings concerning the financing of the required facilities, no new facts were introduced that would alter that conclusion.

In addition, the staff says that in the 1950 PT&T case the Supreme Court recognized a certain broad class of regulatory powers that enables the Commission to regulate certain activities of a utility:

> "The Commission has been given broad powers to regulate the relationships of the utility to the consumer; thus it can determine the services that must be provided by the utility and the rates therefor. It has also been given certain specific powers to regulate the manner in which the utility provides the required services to safeguard the utility's ability to serve the public at reasonable rates; thus the Commission must approve the sale or encumbrance of operative property necessary or useful to the utility in the performance of its duties...and it must approve the issue of securities and may specify the manner in which funds so raised may be spent." (34 Cal 2d 827.)

The staff believes that the Commission's powers to prohibit the payment of dividends are derived from this class of regulatory powers, and that by ordering Cal-Am to make no cash dividend payments, the Commission would be exercising its constitutionally mandated powers to provide public utility customers with reasonable service at reasonable rates.

The staff submits that if the Commission should adopt Cal-Am's position that the Commission has no jurisdiction to prohibit dividend payouts, a utility would be free at any time after the Commission has approved the composition of its capital structure to declare a partial liquidating dividend which would change the capital structure from that which the Commission approved. If this contention were to be correct, the right granted to the Commission to determine the capital structure at the inception of operations or when additional capital is provided by issuance of

stocks or bonds, or when there should be a merger or a re-organization, would be meaningless because immediately thereafter the utility could nullify the direction of the Commission by making capital distributions to its stockholders without Commission approval.

The staff denies that the curtailment of dividends would constitute a "taking" without just compensation of property in which Cal-Am shareholders have a vested interest, or that such an order would violate both the Fifth Amendment and the "Due Process Clause" of the Fourteenth Amendment of the United States Constitution.

The staff believes that this argument misunderstands the nature of dividend payments to stockholders; a dividend payment is a situation where liquid assets of a company are transferred from the company to the stockholder. The staff notes that the stockholder is receiving nothing he did not already own. In other words, a utility's cash, whether retained in the business or paid out in the form of dividends, is the stockholder's assets. Therefore, according to the staff, an order prohibiting dividend payouts is not a "taking", inasmuch as the utility's cash still remains as the property of the stockholder.

Cal-Am responded, by a letter dated November 4, 1976, characterizing the staff's argument concerning the declaration of liquidating dividends as a "serious flaw". Cal-Am admits that the Commission does have broad authority expressly granted in Section 851, as an example, over liquidations of utility assets and, thus, by refusing to allow such liquidation, the Commission indirectly has authority to prevent "liquidating dividends".

According to Cal-Am, there is no such express statutory authority, however, regarding the distribution of cash dividends (i.e., profits) on common stock and, in fact, the California Supreme Court has ruled that no such authority, express or implied, exists.

Cal-Am then quotes Justice Traynor where, in the 1950 PT&T case, at 34 Cal 2d 387, he said:

> "(6) It might, for example, be wise business judgment to divert profits from the payment of dividends to finance expansion into fields that the utility has not theretofore entered. In the absence of an enabling statute meeting the requirements of due process, however, the commission cannot require management to make such choices. (Hollywood C. of C. v Railroad Com., 192 Cal 307 [219 P. 983, 30 A.L.R. 68].)"

Cal-Am states that the staff cannot deny that the PT&T case is the only authority on point and that it comes down on the side of management autonomy on this issue.

Consideration of Cited Authorities

In reviewing the cases cited by Cal-Am we fail to find any indication that, at the time of the 1950 PT&T case, the holder of 87.93 percent of PT&T's stock, American Telephone and Telegraph Company (AT&T), had failed to provide equity funds to its subsidiary, and as a result PT&T was required to curtail service. (We know the contrary to be true. Our files show that between 1946 and 1950 PT&T sold over a quarter of a billion dollars of common stock. Not only did AT&T purchase its full share but, PT&T by successfully opposing proposals that preemptive rights be abandoned in favor of competitive bidding, preserved AT&T's opportunity to maintain its proportional interest in PT&T.)

The issue in the 1950 PT&T case was whether the Commission could set the level of payments under the AT&T license payments. Four jurists concurred that the Commission could not, but two judges dissented. It is not at all clear that, had PT&T not been striving to meet the explosive post-war demand, and had not AT&T been willing to supply its share of the massive equity investment required, the judges would have interpreted the facts and law as they did. As the staff has reminded us, Justice Traynor, at 34 Cal 2d 833 and 834, said,

> "Under sections 60 and 75 [PU Code Sections 1702, 1703, 1704, 2102, and 2103] of the act the commission is empowered to stop illegal practices of utilities. If by the device of a contract for services, American were exacting excessive payments that impaired Pacific's capital and thus weakened its ability to serve the public, the Commission could disregard the separate corporate entities and treat the excessive payments as an illegal dividend. (Ohio Central Telephone Corp. v Public Utilities Com'n., 127 Ohio St. 556 [189 N.E. 650]; see, Ballantine on Corporations (Rev. ed.) § 142, p. 330; cf., Western Canal Co. v Railroad Commission, 216 Cal 639, 652 [15 P.2d 853].) We do not have such a case before us, however, for the payments under the license contract are not impairing Pacific's capital or affecting its ability to serve the public."

We have mentioned Cal-Am's Sweetwater condemnation litigation and how Cal-Am has expended $4,100,000 to defend plant that was included in rate base at a depreciated original cost of $10,428,066.[20/]

As of December 31, 1975, Cal-Am's earned surplus amounted to $2,119,591, only about half of the deferred debit representing the Sweetwater condemnation costs. Should the present 75 percent dividend policy continue, Cal-Am will have, as a practical matter, a negative earned surplus until such time as the just compensation is realized. Should, for some reason, Cal-Am fail to recover the costs of the just compensation litigation, it could have a recorded negative earned surplus.

A reading of the Hollywood C.C. case cited by Justice Traynor in the 1950 PT&T case reveals that that case concerned the question of whether the Commission had the authority, under former Section 36 of the Public Utilities Act (now P.U. Code Section 762), to order the Los Angeles Railway Corporation to extend certain of its streetcar lines into previously unserved territory in the Hollywood district of Los Angeles. The court concluded that Section 36 of the Public Utilities Act, insofar as it sought to confer jurisdiction upon the Commission to order a street railway company to extend its lines into a new territory in which it has no franchises, was ineffective for that purpose and to that extent void.

20/ As of the inventory date, April 1, 1969 the superior court awarded Cal-Am just compensation of $14,485,000 plus $17,296 costs. The court of appeal upheld the superior court in a unanimous decision issued September 15, 1976, as modified September 27, 1976. (South Bay Irrigation Dist. v Cal-Am Water Co., App., 133 Cal Rptr 166, 175-177. Cal-Am has informed our staff that it is appealing this decision to the Supreme Court.

In reaching this conclusion the court recognized that the authority of the Commission over a public utility which dedicated itself to render a vital service in a specific territory is another matter. At 192 Cal 311, Justice Kerrigan said:

> "Within the field of original dedication the regulative authority has ample freedom of action, as a public utility undertaking to supply a given public need submits itself to the regulation and control of public authority with respect to the service it has undertaken. Thus, improved train service may be required, as may switching connections between railroads. But all of these requirements represent a legal exercise of the police power, under which the state may regulate the service which the public utility has undertaken to give the public. It is obvious that an order compelling extensions and service in a field not embraced within the limits of its enterprise is of a totally different character.

(In reading the PT&T cases cited by Cal-Am we are reminded that we have also been chided by the Supreme Court for not being sufficiently zealous in our regulation of that utility. (City of Los Angeles v Public Utilities Commission (1972) 7 Cal 3d 331.)

A review of Cal-Am's citation to the 1965 PT&T case shows that the court said that Section 701 does not permit the Commission to disregard the provisions of Sections 728 and 729 of the Public Utilities Code regarding retroactive ratemaking. The citation concludes with a citation from an earlier case in the same volume. "[S]tatutes are to be interpreted to give a reasonable result consistent with legislative purpose."21/

21/ River Lines Inc. v Public Utilities Commission (1965) 62 Cal 2d 244, 247.

After a rereading of the 1959 Cal. Water & Tel. case, and particularly the page cited by Cal-Am (51 Cal 2d 495), we are puzzled as to its relevancy. The pertinent section seems to concern whether the Commission could compel the extension of Cal. Water & Tel's. mains into undedicated territory on conditions other than those specified by Cal. Water & Tel. in its agreements, and without which the utility, in the exercise of its managerial judgment, would not have signed the agreements in the first place.

The page cited in the Richards case (44 CA 2d 558) seems to invoke the question of whether the directors acted in good faith in reducing the rate of depreciation, based on the remaining life method of depreciation, and in distributing the resulting increased earnings in dividends. The trial court did not find that there was fraud or deceit or bad faith of any character, a conclusion with which the Court of Appeals apparently concurred. Again, we are unable to see where the Richards case has any relevancy to the problem at hand.

The Pacific Gas and Electric case ((1932) 38 CRC 252, 259) likewise does not appear to be in point. In that case the Commission stated that the payment of dividends was a matter which rests with the boards of directors of public utilities. In this instance, however, the Commission was being asked to authorize a public utility to issue stock to acquire control of properties whose earnings were inadequate to pay the dividends proposed on such stock.

The Commission declared:

"The logical thing to do would be to reduce the stock issue so as to be in line with the cost and/or the earnings of the properties to be acquired. But it is urged that the earnings of Pacific Public Service Company will improve with a change in economic conditions and that the situation can be worked out in a satisfactory manner. We are inclined to give applicant an opportunity to demonstrate this and if it is successful in its endeavor, consider a modification of the order herein. In the meantime, however, we believe that applicant should be permitted to issue the $6,841,200 of stock only upon condition that it transfer $5,000,000 from its earned surplus now invested in properties to Account No. 251, "Appropriations for additions and betterments," and file with the Commission a resolution of its board of directors agreeing that it will not capitalize such amount through the issue of stock or evidences of indebtedness until and unless the earnings of the Pacific Public Service Company properties are sufficient to pay the annual dividends on the $6,841,200 of stock and accumulate a surplus of $5,000,000 from earnings or the sale of properties at a price in excess of that being paid by the Pacific Gas and Electric Company for their control."

Such a transfer from Cal-Am's earned surplus to an appropriation for additions and betterments would not be a practical alternative, however, since Cal-Am's 1975 year-end earned surplus of $2,119,590.70 is far less than would be required for construction of the Begonia and Canada projects.

In Venice Consumers Water ((1924) 24 CRC 883) the Commission observed, in a case involving financing proposed by Venice Consumers to pay for water utility properties that it was acquiring, that it did not have the authority to require Venice Consumers to issue its stock directly to the stockholders of a company being acquired.

Consideration of Curtailment of Dividends

In deciding whether to order the curtailment of dividends, we are cognizant that the only directly stated statutory authority that we can find for such action is the general power contained in Section 701 of the Public Utilities Code. A careful reading of each and every one of the cases cited by Cal-Am fails to turn up any specific instance where the Supreme Court of this State has told us that we do not, should circumstances require, have the power to restrict the payment of dividends.

We realize that we must be discreet in applying Section 701, a broad and general statute, for such a statute, if frivolously employed, could easily lead to meddlesome interference into the day-to-day operations of a private enterprise, or worse, if injudiciously applied, to intrusion by a regulatory authority into situations where the Legislature did not intend. On the other hand, it was obviously with definite purpose that the Legislature, when in 1911 it drafted the Public Utilities Act, included Section 31 (later codified as Section 701). Section 701 was placed in the Code to be used when the situation indicated. In deciding whether, under Section 701, we have the power to curtail the payment of dividends, we will consider the question in the context of the entire record in this case as developed to this point.

Specifically we will consider that:

1. We permitted American Water Works, through its newly organized subsidiary, Cal-Am, to acquire the Cal. Water & Tel. water properties at a cost far in excess of their earning capacity. Such authorization was granted only after the president of American Water Works assured the Commission, under oath, that capital funds would be

provided as needed. He further assured the Commission that 99.9 percent of the decision to commit funds for capital improvements would be made in the necessity to maintain a proper standard of service.

2. American Water Works has not, despite the assurances of its president, made any cash investments in Cal-Am's securities since Cal-Am acquired Cal. Water & Tel's. water properties.

3. Cal-Am has, by maintaining a dividend payment ratio higher than the ratio of American Water Works' dividend to its consolidated net income, caused Cal-Am to send up-stream to the holding company, funds that were then invested in American Water Works' other operating subsidiaries or were used to retire the holding company's stock and debt.

4. By financing the Sweetwater condemnation exclusively through Cal-Am, American Water Works has, to protect the holding company's equity investment, depleted Cal-Am's treasury of an amount in excess of $4,100,000. Should this debit be written off, Cal-Am would have a negative earned surplus. By failing to fund the Sweetwater condemnation costs, American Water Works has placed Cal-Am in a very precarious financial condition.

5. Because of its failure to finance and construct the facilities necessary to produce and deliver the water directly or indirectly available to Cal-Am by virtue of its rights to water from the Carmel River, Cal-Am has persistently overdrafted the Seaside aquifers, thus risking salt water intrusion and loss of that water source to the community for an indefinite period in the future.

6. Because of inadequate production, storage, and transmission plant, Cal-Am has not been able to meet the ordinary demands and requirements of the water consumers of its Monterey District, resulting in the necessity of the Commission imposing a connection ban and water rationing.

7. The connection ban has caused financial hardship and emotional distress to those lot owners affected.

8. Water rationing has caused serious inconvenience to the customers of Cal-Am's Monterey District.

9. Cal-Am's board of directors has, by formal resolution, used the urgent necessity for additional capital investment in the Monterey District as a bargaining ploy in a unilateral attempt to negotiate with this Commission over Cal-Am's authorized rate of return.

10. Cal-Am has informed the Commission through its vice president finance, treasurer, and secretary that Cal-Am has no intention of issuing equity securities.

11. Should Cal-Am continue to pay dividends, it will not, absent an issue of equity securities, be able to finance its needed capital additions and still maintain the 50 percent debt limitation established by the Commission.

We find that Cal-Am, under the absolute domination and control of the American Water Works holding company complex, the largest investor-owned water operation in the United States, by not financing and constructing the necessary production and storage and transmission plant, has failed to meet its obligation to furnish and maintain the adequate, efficient, just, and reasonable

service required by Section 451 of the Public Utilities Code.[22] Cal-Am, and through it American Water Works, willingly accepted this obligation, despite our admonitions in Decision No. 70418.[23]

22/ "451. All charges demanded or received by any public utility, or by any two or more public utilities, for any product or commodity furnished or to be furnished or any service rendered or to be rendered shall be just and reasonable. Every unjust or unreasonable charge demanded or received for such product or commodity or service is unlawful.

"Every public utility shall furnish and maintain such adequate, efficient, just, and reasonable service, instrumentalities, equipment, and facilities as are necessary to promote the safety, health, comfort, and convenience of its patrons, employees, and the public.

"All rules made by a public utility affecting or pertaining to its charges or service to the public shall be just and reasonable."

23/ "It is essential, however, that there be no misunderstanding of this Commission's policy as regards the treatment of any excess purchase price in a rate proceeding, and for this reason it is herein stated that it is the policy of this Commission to fix rates on the basis of an original cost rate base and that the plant acquisition adjustment is not included as an element of such a rate base. The purchaser's president testified under cross-examination that he understood such rate-making treatment to represent Commission policy and that he would not urge a treatment inconsistent with such policy. Tr. 86-87. Moreover, the witness for the California-American Water Company stated that it was his understanding that the low return to common shareholders of California-American Water Company resulting from the purchase at a price substantially in excess of the original cost less depreciation of the properties being acquired would not be used or claimed as a basis for the filing of a rate increase application. Tr. 147." (Decision No. 70418 dated March 8, 1966 in Application No. 48170, 65 CPUC 281, 286.)

Considering the entire record in this case including, but not limited to, the circumstances summarized above, we can draw no other conclusion than that it would be foolhardy to allow Cal-Am to continue with payment of dividends. We also conclude that by persisting in payment of dividends, the directors of Cal-Am, all of whom are officers or employees of American Water Works or its wholly owned service subsidiary, are, unless and until the Sweetwater debit is converted into earning assets, in the process of liquidating this utility. We see no alternative but to order the curtailment of dividends until such time as Cal-Am's financial situation permits their resumption. Far from taking property, we will be, by taking this action, conserving it for the benefit of Cal-Am's creditors, customers, and rank and file employees. Mr. Banz's remarks to the contrary, we believe that our action will actually improve Cal-Am's status with money lenders. We are convinced that this is a type of situation that the Legislature had in mind when, 65 years ago, it made the present Section 701 a part of the original Public Utilities Act. Our holding that we are not constrained to merely stand by and fret as the Monterey

situation continues its inexorable deterioration and that our interpretation of Section 701 in this situation is a reasonable one, is further reinforced by the words of Justice Traynor in the 1950 PT&T case, 34 Cal 2d 822, 833, and 834, quoted above. This conclusion is reinforced by our finding that Cal-Am has, despite the commitments, made under oath, by American Water Works' president, failed in its public utility obligation to maintain the reasonable level of service required by Section 451 and such failure is the direct result of not financing and constructing adequate facilities.

Heeding the advice of the Supreme Court in River Lines, Inc., supra, we interpret Section 701, taken together with Sections 451, 816, 817, and 851 of the Public Utilities Code, as giving us the power and duty to order what we perceive to be the only reasonable result consistent with legislative purpose and direct Cal-Am to stop paying dividends or otherwise transferring any funds to American Water Works except for value received, until such time that the Commission shall find it prudent to permit their restoration.

REEXAMINATION OF CONNECTION BAN

Background

In our Second Interim Decision No. 84527 dated June 10, 1975, we found, among other things, that:

> "Cal-Am's Monterey District has reached the limit of its capacity to supply water and, except as provided in the order that follows, no further consumers can be supplied from the system of such utility without injuriously withdrawing the supply wholly or in part from those who have heretofore been supplied by the corporation."

and in Ordering Paragraph 4, pursuant to Section 2708 of the Public Utilities Code, we ordered:

> "Until otherwise permitted by further order of this Commission, California-American Water Company shall not provide water to new service connections within its Monterey Peninsula District, other than those in municipally sponsored redevelopment or renewal projects, unless, prior to the effective date of this order, a valid building permit has been issued."

The opinion in Decision No. 84527 contains a description of the events and conditions that caused us to impose the service restriction. In the opinion we declared:

> "In ordering this connection freeze we take full cognizance of the fact that the effects of this action will fall most heavily on the working people of the building trades. We also recognize that it will distort the normal pattern of real estate values. It is our intention that the freeze be lifted at the earliest prudent moment."

In the year and a half since Decision No. 84527 became effective the connection ban has indeed caused hardship to the working people of the Peninsula and has drastically distorted real estate values. Persons owning developed lots have been unable to carry out their plans to build and have not been able to recover their investment, since, without water, their land has no economic utility, only speculative value. Properties with water service have, on the other

hand, appreciated at an abnormal rate and the higher market values, soon recognized by the assessor, have been reflected in higher real estate taxes, causing hardship indirectly to those not affected directly by the ban.

One group of people particularly vexed by the connection ban is comprised of retirees and prospective retirees, who, having paid taxes on parcels for many years while living elsewhere or serving in the armed forces, returned to the Peninsula area and found, to their distress, that they were unable to complete long cherished intentions to build their retirement homes. This distress has, for many, been aggravated by their not being able to complete construction within the time specified by the Internal Revenue Code and their being faced with paying a substantial capital gain tax on funds derived from sale of their former homes. A further hardship is the necessity to pay high rents while construction costs rise faster than can be offset by interest on the funds set aside for investment in their new homes.

The Commission has been informally apprised of a number of such hardship cases and seven, shown on Appendix B, have resulted in formal proceedings being instituted before this Commission. One of those requests has been denied; action on the others has been deferred, by direction of the Commission, in the hope that developments in the most recent phase of this proceeding might permit the Commission to make the finding required by Section 2708 of the Public Utilities Code that the extension of water service to the complainant's property would not injuriously withdraw the water supply in part from those who had theretofore been supplied by Cal-Am.

Lot Owners' Association

A number of owners of lots of record have organized into an association they call Lot Owners Without Benefit of Land or Water (LOWBLOW) and have, since the May 24, 1976 hearings, participated actively in the proceeding. On June 17, 1976, the counsel for LOWBLOW filed a brief in which he contended that allowing connection

of service to an existing lot of record on the day that construction commences, or if required as a condition for a building permit, at the time the permit is applied for, would only add a minimal quantity to the present consumption of water. LOWBLOW's counsel also cited Supreme Court cases from which he concluded that Section 2708 of the Public Utilities Code does not envision an absolute quantification of the last drop of water, but rather an application of common sense and a balancing of equities.[24]

The counsel for the lot owners further argued that all owners of legal lots of record as of the date of the connection ban purchased their lots with a reasonable belief that Cal-Am could and would furnish their lots with water. This belief was reinforced on these cases where a public subdivision report from the Real Estate Commissioner is required. Since 1957, these reports have contained, either expressly or implicitly a statement by the Real Estate Commissioner, based on an evaluation by the staff of the Public Utilities Commission, that Cal-Am would furnish water service. Counsel argues that, by basing their decision to buy their lots on this assurance, the buyers came within the definition of consumers as contemplated by Section 2708. He also argued that buyers of other lots located within the dedicated service area of Cal-Am relied on the representation of Cal-Am to supply water within its service area and thus should be considered as existing consumers.

Following the initiation of the emergency water conservation and rationing orders described earlier, the president of LOWBLOW, David L. Hughes, a retired career naval officer, pointed out to the Commission that the amounts of water being saved were many times greater than the requirement that would be necessary to serve the number of additional water consumers that could be expected should the connection ban be lifted for legal lots of record.

24/ Butte Co. W.U. Assoc. v R.R. Com. (1921) 185 Cal 218; Kern County Land Co. v R.R. Com. (1934) 2 Cal 2d 29.

Following Mr. Hughes' presentation the examiner directed the staff to prepare an independent appraisal of the water requirements associated with an accommodation of the lot owners' predicament.

In response to the examiner's direction, Associate Utilities Engineer Francis S. Ferraro, P.E., prepared a report, which he presented at the September 22, 1976 hearing. Mr. Ferraro estimated that there were approximately 1,500 vacant residential lots in Cal-Am's service area. Should the Commission permit water service to these lots, construction on approximately 150 would start within one year. Each single family residence would normally require about 0.34 of an acre-foot per year. Should low water use appliances and landscaping requiring minimal water be used, the annual requirement would drop to 0.20 of an acre-foot. The initial annual incremental Monterey District water requirements under these estimates would thus be 51 acre-feet under normal water use conditions and 29 acre-feet using water conserving appliances and landscaping.

Mr. Ferraro recommended that all lots zoned R-1, single family residential, be allowed to receive water service from Cal-Am under the following conditions:

1. That applicant for service obtain a building permit prior to requesting service;
2. That applicant submit an affidavit that he would:
   a. Commence construction within 30 days.
   b. Not have any outside landscaping requiring water use.

Applicants could only submit such an affidavit once, and no member of his immediate family could submit a similar affidavit. No applications for service would be granted until Los Padres Reservoir was filled, an event that would require at least three inches of concentrated rainfall.

Nancy Strathmeyer, president of the Carmel Board of Realtors testified that the 30-day limitation for the commencement of construction would not be sufficient to arrange financing and suggested 60 days. Walter G. Miller, a lot owner with a proceeding pending before the Commission, testified that anticipating that he might get water service, he had approached a bank and had been informed that the bank would not begin negotiations for a loan until water service had been established.

Examiner's Request for Water Management Agency Position

Any easing of the connection ban would obviously have an impact on the amount of water available for service to existing customers and to new customers that would be served in the presently exempted urban renewal projects. The examiner, therefore, seeking guidance from the local agency formed for the purpose of planning and dealing with the water supply problem on the Monterey Peninsula, addressed a letter, dated September 2, 1976, to the Monterey Peninsula Water Management Agency in which he informed the Agency that the Commission was entertaining proposals for an easing of the connection ban for lots of record, and that, in considering proposals for easing the connection ban, the Commission would appreciate an expression of opinion from the Water Management Agency as to whether the ban should be eased and, if so, under what conditions.

At the September 22 hearing, Leo W. McIntyre, director of public works of the city of Monterey and pro tempore representative of the agency, reported that the examiner's letter had been placed on the agenda of the regular meeting of the board of directors of the agency on September 20, 1976. Although the board discussed the examiner's request extensively, no motions were made concerning the examiner's request and no action was taken by the board.

In the absence of authoritative local guidance from the Water Management Agency, the Commission will proceed to consider the problem and to dispose of it according to the Commission's best concepts of the practicalities and equities of the situation.

Discussion

In our second Interim Decision No. 84527 we described in detail our understanding of the Monterey Peninsula water supply situation and our concern that the continued overdrafting of the Seaside aquifers might result in salt water intrusion which would render some, or all, of these aquifers unusable. Since that time, as described earlier, the Del Monte Observation well has been completed and Cal-Am is in a position to monitor the static water level of the main Seaside aquifer.

During the extremely dry period since the completion of the well Cal-Am has continued to extract water from the aquifer of an annual rate of approximately 3,500 acre-feet and the water table has dropped 1.25 feet and, in September, was only 0.83 feet above sea level. (It should be noted that there was, except for a rare summer storm, virtually no rain during the reported period.)

As mentioned in Decision No. 84527,[25/] the completion of the Canada and Begonia projects would make available an additional 1,500 acre-feet and enable Cal-Am to cut back pumping from the Seaside aquifers to 2,000 acre-feet and thus permit the recharge of the aquifer. In the meantime the test well and monitoring program are available to give advance warning of any salt water intrusion.

Although the water level of the Seaside aquifer is still dropping, encouraging progress has been made in completing plans and compiling environmental data necessary to initiate the Begonia and Canada projects. As expressed elsewhere in this opinion, we are determined, should the environmental considerations permit, that the Begonia and Canada projects be initiated and completed.

25/ Mimeo. page 46.

The 29 acre-feet that would be required to serve the initial year's estimated construction, should the staff's recommendation be accepted, would have increased the water deliveries for the 12-month period ended September 1976 of 15,891.7 acre-feet by only 0.2 percent. Should the requirements increase at this rate for the 3-year period before water would become available from the Begonia and Canada projects, the incremental requirements would still be less than 1 percent of total.

After careful consideration of all the factors of the current Monterey Peninsula water situation as described in this opinion, specifically including the existence of a functioning and effective rationing program whose operating phases depend on the water levels in the two terminal reservoirs, and, also considering our expressed intentions concerning the construction of the Begonia and Canada projects, we conclude that by applying, as urged by lot owners' counsel, a common sense interpretation of Section 2708, one that is practical rather than technical, and one that will lead to a wise policy rather than mischief or absurdity,[26] the extension of service to lot owners of record, substantially in accordance with the staff's recommendations, will not injuriously withdraw the water supply wholly or in part from those who heretofore have been supplied by Cal-Am's Monterey District.

We have underlined the key word "injuriously". We recognize that sharing of the water supply so as to accommodate the distressed lot owners may cause a very slight additional inconvenience to present consumers but, the additional requirements are so negligible compared to the available supply that, under the rationing program, we do not believe that present consumers will suffer any detectable injury. Should events not turn out as envisaged in this decision, we will, at the appropriate time, determine what action should be taken.

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[26] 45 Cal Jur 2d, Statutes, Sec. 116.

In reaching this conclusion, we must reject the contention of counsel for the lot owners that, by virtue of owning property within the boundaries of the dedicated service area of a public utility water corporation, property owners become "consumers". Webster defines "consumer" as "one who uses (economic) goods, and so diminishes or destroys their utilities".[27] We accept this definition to be the usual, ordinary, and commonly understood meaning of the word consumer as used in the context of Section 2708.[28] It seems reasonable to conclude that, had the Legislature intended that it meant "consumers" to include others than those actually using water the Legislature would have written the statute differently.

We believe that it would not be prudent, however, to ease the connection freeze until there is some indication that the present drought has been broken. Accordingly we will accept the staff's recommendation that the easing of the freeze become effective when Los Padres Reservoir is filled. We will allow a 90-day grace period before construction must commence, as being a more realistic allowance for completing preliminary arrangements.

Neither the Commission nor Cal-Am would have any practical method of determining whether low water use devices will actually be installed in the interiors of new residences. Fortunately, as previously mentioned, most of the local agencies have adopted effective enforceable water conservation ordinances applicable to new construction. Our lifting of the connection ban will therefore apply to the aforementioned cities and the county. Should the remaining two cities adopt similar acceptable ordinances, we will extend the easing of the ban to those municipalities.

27/ Webster's Collegiate Dictionary, Fifth Edition.

28/ 45 Cal Jur 2d, Sec. 139.

Irrigation of landscaping in violation of a service applicant's assurances should be readily detectable. Cal-Am will be directed to minimize service to such a customer by inserting a flow restrictor at the meter. We shall provide a mechanism for appeal of such service minimization to the Commission and also provide that no other legal or equitable action shall accrue against Cal-Am because of such service minimization.

RECENTLY DEVELOPED INFORMATION CONCERNING WATER SUPPLY AVAILABLE FROM CARMEL VALLEY AQUIFER

In response to questions posed by the City of Carmel-by-the-Sea, Cal-Am, at the August 23 and 24, 1976 hearings, presented James Russell Mount, a licensed professional geologist associated with the firm of Dames and Moore, who reported on the results of his most recent studies of the Carmel Valley aquifer. Since this testimony is closely associated with the environmental questions pertaining to the Begonia and Canada projects, it will be considered in connection with our evaluation of these projects in a subsequent opinion. There has been additional testimony from Mr. Mount on this subject at the current hearings on the staff's Draft EIR.

REEXAMINATION OF URBAN RENEWAL EXEMPTION

Background

In our Second Interim Decision No. 84527, when ordering Cal-Am not to provide water to any new service connections, we exempted urban renewal projects. We stated, however, that should growth in usage continue at an undue rate, we would reexamine this exemption.

With the advent of water rationing, the examiner placed a reexamination of the exemption on the hearing agenda.

The staff prepared a report on the subject of urban renewal which was presented by Associate Utilities Engineer Francis S. Ferraro, P.E., on September 20 and 21, 1976.

The cities of Monterey and Seaside are involved in urban renewal projects.

Monterey Project

The single Monterey project, known as the Custom House Project, encompasses approximately 39 acres in an area north of Franklin Street between Washington and Pacific Streets. Substantial progress has been made in completing the project. A convention center is under construction, and bids have been let for a 380-unit hotel adjacent and integral to the convention center. Final financing of a parking garage is awaiting the completion of arrangements for the hotel. There also are proposals for commercial developments and parking facilities to be constructed on some of the remaining parcels. Substantial amounts of money have been invested in the Custom House Project, $8 million in the convention center alone.

Seaside Projects

Seaside has four redevelopment projects, Del Monte Heights Hannon, Gateway, and Laguna Grande.

Del Monte Heights is a residential development located just west of the Fort Ord fence. It is served entirely by the city's municipal water system. Nineteen lots and a church site are undeveloped.

Hannon is located in the center of Seaside above Fremont Boulevard. All lots are sold and homes have either been completed or are under construction upon all the sites.

Gateway is located between Fremont and Del Monte Boulevards and La Salle and Olympia Avenues. It features automobile agencies and related businesses and has been successful in attracting a number of such enterprises. There are only 20 vacant lots left, 15 of which have been sold. The 5 remaining lots will be retained by the city for use as a corporation yard. Of the 15 lots that have been sold, a 34-unit motel is planned for three and the remaining 12 will be used for boat sales, auto parts and repair shops, an auto painting shop, and a bar.

Laguna Grande is located along Canyon Del Rey Boulevard and is divided into three study areas.

The first study area is located at the Canyon Del Rey Boulevard Exit of the Highway 1 freeway, near the Holiday Inn. It is presently under development; a K-Mart has been completed and a Security Savings and Loan office is expected to be finished in approximately 18 months. A supermarket is contemplated, but no definite plans have been made.

The second study area is located on the north and east shores of Laguna Grande, along Del Monte and Canyon Del Rey Boulevards, south to Harcourt Avenue. Seaside intends to use the shore of Laguna Grande as a natural parksite requiring no water except for toilet facilities. The city owns 7 other parcels and has borrowed $465,000 for their development. The city anticipates that an existing building supply store at the intersection of Del Monte and Canyon Del Rey Boulevards will be torn down and a new building will be constructed. There also will be a restaurant and a city corporation yard. This project will require two to three years to complete.

The third Laguna Grande project study area is, for the most part, comprised of a triangle of land between Fremont and Canyon Del Rey Boulevards and Trinity Avenue. The city has no money invested in this area and has zoned it C-C, civic center district. All improvements are intended to be made by private investment. It appears that this area will gradually be changed from single family residences to multiple residential units.

Staff Recommendations

The staff recommended that certain parcels in the Monterey Custom House Project, for which no proposed use had been formulated, and that a lot that was surplus from the development of the first Laguna Grande study area in Seaside, should not be provided water service. The staff also recommended that, since the third Laguna Grande study area had not progressed beyond a zoning change, and since there is no city financing involved, this study area should not be exempted from the provisions of Decision No. 84527.

The staff further recommended that Cal-Am should be prohibited, until the water rationing plan is lifted, from supplying water for irrigation of any new outside landscaping for urban renewal structures that have not been completed. The staff also recommended that once the water rationing plan is terminated, these projects should meet the following requirements as a condition for receiving water service for outside irrigation:

a. Where possible, plants should be native, naturalized, 29/ or low water requiring.

b. If automatic sprinkler systems are installed, they should include moisture sensors (tensiometers) programmed to override the sprinkler controls.

In addition, the staff recommended certain building code modifications intended to promote water conservation. These recommendations have been met by the water conservation ordinances enacted by the two cities and will not be discussed further herein.

29/ Naturalized plants are those that can survive without care in an area to which they are not native.

The staff has estimated water use of the remaining developments in the projects as follows:

Monterey Custom House Project:

No restriction on connections	80 acre-feet/yr.
With building code revisions and no landscaping requiring irrigation	42 acre-feet/yr.
With all of the staff recommendations (including elimination of certain parcels)	34 acre-feet/yr.

For Seaside Projects Excluding Laguna Grande Study Area III and Municipally Supplied Del Monte Heights:

No restrictions on connections	22 acre-feet/yr.
With building code revisions and no landscaping requiring irrigation	12 acre-feet/yr.
With all of the staff recommendations (including elimination of certain parcels)	11 acre-feet/yr.

Cities' Position

The community development director for the city of Seaside, Finnly F. Sutton, and the redevelopment director for the Monterey Redevelopment Agency, Gary Chalupsky, both commented on the staff's proposals.

Mr. Sutton had no objection to the staff's recommendations. He said that the city of Seaside had issued a change order for the K-Mart project by which the city will not install landscaping unless it is successful in bringing in a well adjacent to the old Monte well.30/

30/ Abandonment of the Monte well was authorized by Decision No. 82394 dated January 29, 1974 in Application No. 54250. The record in that case indicated that the water produced by the Monte well exceeded the EPA's limits for chloride content and total dissolved solids.

Should the test well be unsuccessful the city will use redwood bark in the planting areas. Mr. Sutton said that the state Coastal Commission, which has jurisdiction over the project, has required extensive landscaping. The city has advised the Coastal Commission of its decision.

Mr. Chalupsky also said that the staff recommendations were acceptable, under the circumstances, to the Monterey Redevelopment Agency. He was concerned, however, that a temporary outright prohibition of extension of water service for new landscaping would be too stringent and would strike at the viability of projects that are very far along. He suggested that a project-by-project review would be preferable. He was also concerned that the agency might not be able to install conduit for sensors in projects where concrete has already been placed. Changes in previously approved landscaping would require concurrence of the Coastal Commission. Mr. Chalupsky suggested that provision be made for a case-by-case review, where the city and the developers could work out reasonable alternatives for outside water uses that would be exorbitant and not rational in terms of the present water situation.

The staff's recommendations appear to be most reasonable and will be accepted. Because of the difficulty of applying the staff's proposals to the many situations that can be expected to arise during the completion of the urban renewal projects, we will provide that our Executive Director with advice of our chief hydraulic engineer may allow variances on a case-by-case basis where circumstances warrant.

EXPANSION OF ORDER OF INVESTIGATION TO INCLUDE RANCHO DEL MONTE DIVISION OF WATER WEST CORPORATION

By Decision No. 86267 dated August 17, 1976, we expanded Case No. 9530 to include the Rancho Del Monte Division of Water West Corporation (Water West). Water West serves in an area on both sides of the Carmel Valley Road located between the Los Laureles Grade Road and the community of Carmel Valley Village. Water West thus separates the Carmel Valley portion of Cal-Am's service area into two noncontiguous parts. Water for Water West is obtained from three wells drawing from the Carmel Valley aquifer.

At the August 24, 1976 hearing, Francis F. Ferraro, P.E., an associate utilities engineer, presented a report of his investigation of the water supply of Water West. According to Mr. Ferraro's report, Water West's production and customer growth over the last four and a half years was as follows:

Year	Water Pumped (Acre-Feet)	Number of Customers
1972	215	318
1973	209	324
1974	222	333
1975	234	346
1976 (7 months)	169	362

Water West's production and storage capabilities are:

Yearly Pumping Capacity	800 acre-feet
Water Pumped Maximum Month	35 acre-feet
Pumping Capacity Maximum Month	70 acre-feet
Total Storage	200,000 gallons
Peak Day Usage	400,000 gallons

Water West's facilities are not interconnected with those of Cal-Am.

It was Mr. Ferraro's opinion that there was, for the present, adequate water available to the Water West system from the Carmel Valley aquifer. He concluded that there was presently no need for restriction or rationing in the Water West area.

Water West's manager, Robert Arenz, testified that he concurred with the staff's recommendation. He felt that it would be grossly unfair to his customers to penalize them by imposing water restrictions because of sins of either omission or commission by another utility.

The staff report shows that Water West's pumping and storage capacity are more than adequate and we will not order a connection ban. Should the Carmel Valley aquifer drop, however, because of lack of recharge resulting from the current drought, it may be necessary to set hearings pursuant to Sections 350 through 358 of the Water Code, and reexamine this conclusion.

DEL MONTE PROPERTIES' REQUEST FOR SERVICE TO OLD CAPITOL TRACT AND DEER FLATS PROPERTIES

Background

In our Second Interim Decision No. 84527 we discussed, and denied, motions by Del Monte for authorization of extension of water service to its Old Capitol Tract and Deer Flats properties. Service to these lands was precluded by our first interim Decision No. 81443. The circumstances by which service to these properties became an issue in Case No. 9530 were set out in Decision No. 84527[31/] and will not be repeated here. Subsequent to Decision No. 84527, Del Monte has taken back the Deer Flats property and returned the consideration paid by the purchaser, Monterey Savings and Loan Association.

By a written motion filed October 12, 1976 Del Monte requested an order of the Commission declaring the Old Capitol Tract and Deer Flats properties eligible for water service.

Del Monte's Contentions

Del Monte submits that Decisions Nos. 84527 and 84683 denying its initial motions were in error. Del Monte claims that, by virtue of contracts with Cal-Am, and Commission approval of such contracts, Cal-Am is committed to serve both Deer Flats and the Old Capitol Tract. According to Del Monte, such a commitment, especially where, as here, it is coupled with significant expenditures made by Del Monte in reliance on such commitments and Commission approval, qualifies these properties as customers of Cal-Am.

Del Monte argues that the fact that water has not yet been delivered to the properties does not affect its status as a customer, and for authority cites Butte County Water Users' Association v Railroad Commission, (1921) 185 Cal 218. Del Monte further holds that water need not be delivered to a property to entitle it to the rights of a customer and cites Sutter Butte Canal Co. v California Railroad Commission (1927) 202 Cal 179 wherein the Commission set rates for "contract consumers" which were treated as customers regardless of whether they physically received water.

31/ Mimeo. pages 8 and 9.

Del Monte claims that, according to Section 2711 of the Public Utilities Code[32] a customer cannot be deprived of his pro rata share of the available water supply, and also that the Commission is without discretion as to who may or may not participate in an available supply of water. According to Del Monte, where, as in the present case, the water company has voluntarily contracted to provide a portion of its water supply, and where that commitment has been specifically approved by Commission order, the consumer falls squarely within the protection of the statute. Del Monte submits that, by statute, its properties at Deer Flats and the Old Capitol Tract must be provided water service on the same basis as any other Cal-Am customer.

Del Monte contends that neither the individual lot owners nor the urban renewal projects have any greater right to water than does Del Monte under its Commission approved contracts. It further claims that the granting of water service to either group, coupled with a denial of water to Del Monte, would constitute an unreasonable discrimination against Del Monte, in violation of its rights to equal protection. Del Monte states that preference to either the lots of record or to the urban renewal projects, without the granting of service to Del Monte, would give rise to a separate enforceable cause of action in favor of Del Monte without regard to its status as a Cal-Am customer.

Del Monte closed its brief with a statement that continuation of either the urban renewal exemption or relief to individual lots of record, or both, without allowing service to the Old Capitol Tract and Deer Flats would constitute unlawful discrimination against Del Monte in violation of its rights to equal protection and would constitute an unlawful taking of Del Monte's property without due process of law.

32/ "2711. Section 2710 does not apply to territory or consumers which have once been served by the corporation. As between consumers who have been voluntarily admitted to participate by the corporation in its supply of water or required to be supplied by an order of the commission, in times of water shortage the corporation shall give no priority or preference but shall apportion its supply ratably among its consumers."

Discussion of Del Monte's Arguments

Del Monte's arguments contend that Del Monte, by virtue of arranging for the future extension of water service to the properties it was contemplating developing, or which it ultimately sold to another party for the purpose of developing, had become a consumer. To support this contention, Del Monte relies on two cases to which the Sutter Butte Canal Company (Sutter Butte), an irrigation company, was a party.

According to the Water Users case, Sutter Butte was, in 1919, supplying water to some 55,000, or slightly more, acres of land, mostly in Butte County. In September of that year the company contracted with the owners of fourteen thousand four hundred acres of land in Sutter County to extend its system to supply their lands, and pursuant to the contract Sutter Butte made the necessary enlargements and extensions of its system.

The irrigation company's rules required that applications for water for the ensuing year be filed by the first of January, and by that date in 1920 the owners of the fourteen thousand four hundred acres had filed their applications and paid the company's regular charge. The three preceding winters had been winters of light rainfall, and the winter of 1919-1920 was exceptionally dry, so that by spring it became evident that there was a serious danger of a water shortage. The company's old consumers, through the instrumentality of an association known as the Butte County Water Users' Association, filed a complaint with the Commission against the company, alleging that the company would not have water enough to irrigate both their lands and the fourteen thousand four hundred acres of additional lands, and asking for an order of the Commission directing the company not to supply the latter.

The matter was promptly heard and decided by the Commission, our order being handed down on April 21, 1920.[33/] At that time, of course, it was not possible to know with exactness just what water

33/ Decision No. 7453 dated April 21, 1920 in Case No. 1431 (18 CRC 105).

conditions during the summer to come would be. We found, among other things, that the fourteen thousand four hundred acres were within the area which the water company was organized to serve and for serving which it had made its water appropriations; that in a normal year the company's supply of water was adequate for the needs of the fourteen thousand four hundred acres as well as for those of the lands theretofore served; that at the time the contract between the company and the owners of the fourteen thousand four hundred acres for the supply of those lands was made, and at the time the applications of those owners for service were presented and accepted, it was reasonable to expect that the company would have a sufficient supply for all during the ensuing year, and the company was justified in accepting the applications. Upon the facts so found, we held, in effect, that the owners of the fourteen thousand four hundred acres had the status of consumers of the company and were entitled to be served, and ordered that they be served on an equal basis with the company's other consumers.

The Commission's order was upheld by the Supreme Court in a unanimous decision.

It is implied in Del Monte's arguments that, by contracting with Cal-Am for construction of water facilities, Del Monte itself became a consumer. In discussing the lot owners' petition we rejected the contention that, by mere virtue of owning property within the dedicated service area of a water utility, the lot owners became consumers. The distinction between Del Monte's status and that of the new customers of Sutter Butte is obvious. The irrigation company made the necessary enlargements and extensions of its system. By paying the company's regular charge by the first of January, applicants for service became consumers, even though irrigation water deliveries would not commence until later in the year. Thus the provisions of present Section 2711 applied to them. People, directly or indirectly, are the consumers of water, not the lands to which the water is applied.

Only when lands held by Del Monte are subdivided and sold, and flesh and blood human beings consume water for the usual life sustaining and irrigation purposes, can the occupants of the lands be said to be consumers.

The Sutter Butte v CRC decision cited by Del Monte pertains to charges made under "continuous" contracts appurtenant to the land, and provided that rates for service and charges under the contracts became a lien on the land. The company was levying a perpetual standby charge under the continuous contracts which it was not levying under "three-year" contracts. The Commission found this practice discriminatory and ordered that the continuous contract customers be eligible for the same rates as three-year contract customers. We fail to see how this case is relevant to the present situation.[34/]

According to the estimates of Del Monte's attorney, as reported in Decision No. 84527,[35/] the Deer Flats property would normally require from 50 to 80 acre-feet and the Old Capitol Tract 400 to 500 acre-feet. We recognize that this incremental burden would not be placed on the system at once, and that, with appropriate conservation measures, it could be reduced. Until the necessary production and transmission facilities are provided by Cal-Am, this incremental water requirement could only be met by substantially reducing the water available to present customers under the rationing plan. Under present circumstances, a withdrawal of several hundred acre-feet of water from the supply available to the present consumers, could only be an injurious withdrawal of supply and not permissible according to Section 2708 of the Public Utilities Code.

We do not agree that, by authorizing, under stringent conditions, the continuation of water service sufficient to permit the completion of ongoing urban renewal projects, and by allowing, under even more stringent conditions, the extension of service to individual

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34/ Decision No. 16289 dated March 20, 1926 in Case No. 2126 (27 CRC 765, 768 & 787).

35/ Mimeo. page 21.

lots of record, we are, by not providing sufficient water to Del Monte to permit the subdivision and sale of two large tracts of land, discriminating against Del Monte or depriving it of its property without due process of law.

It is trite but true that land speculation and development is a risky business. Del Monte is probably the best informed land operator in the area. Del Monte was, at one time, an owner of the water utility itself. The plain fact is, that by assuming that water service would be available, Del Monte miscalculated, and the marketability of its properties has been impaired. The properties, highly desirable ones, are still in Del Monte's possession; they have not been taken. Their ultimate development is by no means precluded. We have not been persuaded that, by not, at the expense of Cal-Am's Monterey District water consumers, insuring that Del Monte can, in the near future, dispose of its properties at a suitable profit, we are unlawfully taking Del Monte's property without due process of law.

Del Monte's motion will be denied.

CONSTRUCTION OF REQUIRED FACILITIES

Under the side heading of "Environmental Impact Report" we referred to our declaration in Decision No. 84527 concerning the construction of the Begonia Iron Removal Plant and the Canada de la Segunda Pipeline. Apparently that declaration has been misunderstood by Cal-Am. To a brief in its rate increase Application No. 54942 filed on January 22, 1976, Cal-Am attached the following document:

"CALIFORNIA-AMERICAN WATER COMPANY

I, ROBERT W. BRUCE, Secretary of CALIFORNIA-AMERICAN WATER COMPANY, a California corporation, DO HEREBY CERTIFY that the following is a true and complete copy of a certain resolution duly adopted by the Board of Directors of said Company at a meeting thereof duly convened and held on October 24, 1975, at which meeting a quorum was present and acting throughout, and that said resolution has not been modified or rescinded and remains in full force and effect on the date hereof:

> RESOLVED, that California-American Water Company hereby assures the California Public Utilities Commission that the Company will proceed with the financing and construction of both the Canada de la Segunda transmission facilities and the Begonia Iron Removal Plant project to accomplish improvement of service in its Monterey District if it is granted the rates or rate of return it has proposed for its system-wide operations in the rate increase proceedings now pending before the Commission identified as Application No. 54942.

IN WITNESS WHEREOF, I have hereunto affixed my signature and the corporate seal of said Company this 2nd day of December, 1975.

/s/ ROBERT W. BRUCE
Secretary

EXHIBIT A"

In Application No. 54942, Cal-Am requested a system rate of return of 10.09 percent. In Decision No. 86249 dated August 17, 1976, we found that:

> "11. A maximum rate of return of 9.2 percent related to the estimated 1975 mid-year rate base adopted herein is reasonable for the purposes of this proceeding. The maximum level of 9.2 percent is reasonable only if substantial progress on the Monterey district's construction projects is indicated within 120 days after a final order concerning the environmental impact of those projects. In the event that such construction has not progressed to that extent, the lower level of 8.6 percent is reasonable for all districts except Monterey Peninsula district and the present rate levels for the Monterey Peninsula district will be reasonable until it is indicated that a water supply adequate for future needs will be available to customers in the Monterey service area."

The demands of Cal-Am, with the Begonia and Canada projects held as hostages, were thus not met by the Commission. At the September 20 hearing Mr. Bruce testified that Cal-Am was evaluating whether the rate relief granted in Decision No. 86249 was sufficient to permit it to proceed with financing of the facilities.[36/]

36/ On December 13, 1976, Cal-Am filed Application No. 56936 for authorization to issue a promissory note in the amount of $4,000,000. We are pleased to see that Cal-Am is finally taking the step needed to put its system on a financially sound basis. We do not, however, feel that this belated filing rectifies Cal-Am's foot-dragging over the years and we feel that the discussion of financing, or the lack thereof, in this decision is still appropriate. After all, the money is not yet in Cal-Am's account and the uses to which the money may be put have not yet occurred.

The construction of the Begonia and Canada projects is imperative, especially since Cal-Am, in the time following our Second Interim Decision No. 84527, has demonstrated its inability to render adequate service in its Monterey District, and has requested the Commission to institute water rationing.

The Commission recognizes that Cal-Am has, without a direct order on our part, proceeded in a diligent manner to obtain the production of an environmental data statement. Somehow, however, the management of American Water Works seems to have gained an impression that this Commission is amenable to bargaining with the public utilities under its jurisdiction.

In Decision No. 86249 we provided Cal-Am with a rate of return 0.3 percent higher than the rate recommended by our staff as being adequate for the financing of the projects. The financial evidence in this case clearly demonstrates that these projects can be financed. Further, when we permitted American Water Works, through Cal-Am, to acquire the water properties in question, it was upon the personal assurance, given in sworn testimony at a public hearing, of American Water Work's president that the parent company was in the position to provide capital funds and would provide such funds as needed.

Let us make one thing clear. This Commission has no intention whatsoever in engaging in any haggling with the management of Cal-Am, and of American Water Works, over the construction of the Begonia and Canada projects. So that there are no doubts on that score on the part of the management of those companies, we will herein, without prejudging the outcome of the environmental impact hearings, order initiation of construction of these facilities within 120 days after the effective date of a favorable final order concerning the environmental impact of these projects, and order their completion within 850 days after such effective date.

To make our position even more clear about the seriousness with which we take the construction of these facilities, Cal-Am is placed on notice of the provisions of Section 2107 of the Public

Utilities Code. Failure to comply with this order may result in a penalty of $2,000 for each day that either the initiation or completion of the construction of the Begonia and Canada projects is delayed.

FINDINGS AND CONCLUSIONS

1. It would not be approporiate under present circumstances to make any changes in Cal-Am's Monterey District rate structure at this time.

2. Cal-Am, by not financing and constructing the necessary production, storage, and transmission plant, has failed to furnish and maintain such adequate, efficient, just, and reasonable service, instrumentalities, equipment, and facilities as are necessary to promote the safety, health, comfort, and convenience of its patrons and the public, as required by Section 451 of the Public Utilities Code.

3. The Commission has, acting under the authority contained in Section 701 of the Public Utilities Code, taken together with its responsibility under Sections 451, 816, 817, and 851, the power, and in this instance the duty, to direct Cal-Am to cease the payment of dividends or other transmission of funds to American Water Works, its employees or subsidiaries, except in payment for value received. Under the circumstances as developed in the record of this case, this power should be exercised and such payments be prohibited until such time as the Commission shall find it prudent to permit their restoration.

4. Cal-Am should be authorized and directed, commencing at such time as any water rationing plans prescribed by this Commission are no longer in effect, to provide water service for use in irrigation of outside landscaping in the urban renewal projects of the cities of Monterey and Seaside, in accordance with the following conditions only:

1. Plants are native, naturalized, or low water requiring.
2. Automatic sprinkler systems include moisture sensors, programmed to override the sprinkler controls.

The Executive Director of the Commission should be authorized to grant case-by-case variances from the above provision.

5. Ordering Paragraph 4 of Decision No. 84527 in Case No. 9530 should be modified to prohibit new water service to connections for the lots in Monterey's Custom House Project labeled F-16, D-1, E-1, E-2, E-3, H-2, H-4, and I-1 on Exhibit 84 and to the surplus parcel of approximately 10,000 square feet located in Seaside's Laguna Grande Project study Area I near the K-Mart. Cal-Am shall not provide water to new service connections in the Seaside Laguna Grande study Area III project, other than those that could be served without the urban renewal exemption.

6. Water West has not, at this time, reached the limit of its capacity to supply water. A connection ban is therefore not appropriate.

7. The limited extension of water service to the property of individual lot owners of record in accordance with the terms and conditions set out in the order that follows will not injuriously withdraw the water supply, wholly or in part, from those who heretofore have been supplied by Cal-Am's Monterey District.

8. Cal-Am should be authorized and directed, commencing at such time as Los Padres Reservoir shall be filled to overflow, to accept applications for water service from individual lot owners of record according to the terms and conditions set out in the order that follows.

9. The motion of Del Monte for an order declaring the Old Capitol Tract and Deer Flats properties to be eligible for water service should be denied.

10. The Begonia Iron Removal Plant and Canada de la Segunda projects are, should environmental considerations permit their construction, urgently needed to alleviate the present critical water supply situation in Cal-Am's Monterey District.

11. Cal-Am should initiate the construction of the Begonia and Canada projects within 120 days after the effective date of a favorable final order concerning the environmental impact of these projects, and should complete the projects within 850 days after such effective date.

12. Cal-Am is admonished that should it fail to comply with our directives herein concerning the initiation or completion of the Begonia and Canada projects, it may be subject to a penalty of $2,000 for each day that either the initiation or completion of either the Begonia or Canada project has been delayed.

13. Case No. 9530 should be continued.

SEVENTH INTERIM ORDER

IT IS ORDERED that:

1. Until further order of this Commission, California-American Water Company shall pay no dividends, nor otherwise transmit any funds to American Water Works Company, Inc., or to any subsidiary, officer, or employee of American Water Works Company, Inc., except in payment for value received.

2. California-American Water Company is authorized and directed, commencing at such time as any water rationing plans prescribed by this Commission are no longer in effect, to provide water service for use in irrigation of outside landscaping in the urban renewal projects of the cities of Monterey and Seaside, in accordance with the following conditions only:

   1. Plants are native, naturalized, or low water requiring.
   2. Automatic sprinkler systems include moisture sensors, programmed to override the sprinkler controls.

The Executive Director of the Commission is authorized to grant case-by-case variances from the provision of this ordering paragraph.

3. Ordering Paragraph 4 of Decision No. 84527 in Case No. 9530 is modified to prohibit new water service to connections for the lots in Monterey's Custom House Project labeled F-16, D-1, E-1, E-2, E-3, H-2, H-4, and I-1 on Exhibit 84 and to the surplus parcel of approximately 10,000 square feet located in Seaside's Laguna Grande Project study Area I near the K-Mart. California-American Water Company shall not provide water to new service connections in the Seaside Laguna Grande study Area III project, other than those that could be served without the urban renewal exemption.

4. California-American Water Company is authorized and directed, commencing at such time as Los Padres Reservoir shall be filled to overflow, to accept applications for water service from individual owners of record of lots which are, at the date of this decision, zoned for single residential use. Service to the lots of such owners of record shall be subject to the conditions attached as Appendix C.

5. The motion of Del Monte Properties Company entitled "Motion for Order Declaring the Old Capitol Tract and Deer Flats Property Eligible for Water Service" is denied.

6. California-American Water Company shall, within one hundred twenty days after the effective date of a favorable final order of this Commission concerning the environmental impact of the Begonia

C.9530 kd

Iron Removal Plant and the Canada de la Segunda Pipeline projects, initiate the construction of said projects, and shall complete said projects within eight hundred fifty days after the effective date of such final order.

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

Dated at San Francisco, California, this 5th day of JANUARY, 1977.

Robert Batinovich
President

Vernon L. Sturgeon

Leonard Ross

Commissioners

I will file a dissent.
William Symons, Jr.
Commissioner

I concur in part and dissent in part
Vernon L. Sturgeon
Commissioner

C.9530 kw

APPENDIX A

LIST OF APPEARANCES

Respondent: Dinkelspiel, Pelavin, Steefel & Levitt, by Lenard Weiss, and Harvey Schochet, Attorneys at Law, and Charles de Young Elkus, Jr., for California-American Water Company.

Interested Parties: Graham & James, by Boris H. Lakusta and David J. Marchant, Attorneys at Law, Donald G. Hubbard, Attorney at Law, John M. Lotz, and James Saunders, for Standex International Corporation; Hebard R. Olsen, for Ord Terrace Water Quality Committee; Chickering & Gregory, by James E. Burns, Jr., Thomas J. Mellon, Jr., and David R. Pigott, Attorneys at Law, for Del Monte Properties Company; L. W. Mc Intyre, for the City of Monterey; Allan D. LeFevre, for Gallaway and Sons; John M. Moore, Attorney at Law, for Carmel Valley Limited; Dave Stewart, for Monterey Pacific, Inc.; John Kramer, Attorney at Law, for Richard Meffley, Department of Water Resources; John Crivello, for the City of Seaside; Hal C. Green and Nancy Strathmeyer, for Monterey Board of Realtors and Carmel Board of Realtors; Ralph Games, Leo E. Thiltgen, Philip Nelson, and Tom Scardina, for Monterey County Building Trades Council and Monterey County Labor Council; Donald G. Hubbard and A. David Parnie, Jr., Attorneys at Law, for Lot Owners Without Benefit of Land or Water; William C. Marsh, Attorney at Law, for Urban Renewal Agency of the City of Monterey; Frank W. Langham, Jr., for Monterey Peninsula Water Management Agency; David M. Hollingsworth, Attorney at Law, for Henry Yamanishi and the Monterey Bay Landscaping Association; Finnly F. Sutton, for Redevelopment Agency of City of Seaside; Boris H. Lakusta and David J. Marchant, Attorneys at Law, for Lot Owners Without Benefit of Land or Water; and Loren E. Smith, Edwin B. Leo, Melvin J. Vercoe, and Thomas Collins, for themselves.

Commission Staff: Cyril M. Saroyan and Lionel B. Wilson, Attorneys at Law, and Melvin Mezek, for the Commission staff.

Tabulation of Decisions in Case No. 9530

C.9530 - Order Instituting Investigation of Cal-Am's Monterey District. Filed April 3, 1973.

D.81443, 5/30/73 - Interim Order. Prohibits extending or accepting distribution mains within or from Monterey Peninsula District system to serve new developments. Denied motion for interim order granting certificate to serve Hidden Hills area. Denied motion for 6 months' continuance.

D.81987, 10/10/73 - Cal-Am authorized to extend service to subdivisions Carmel Views #4 in Carmel Valley and William in Seaside.

D.84527, 6/10/75 - Second Interim Order, A.53653, for certificate to serve Hidden Hills development denied without prejudice. New water connections in Monterey Peninsula District prohibited except in municipally sponsored redevelopment or renewal projects or unless a valid building permit has been issued prior to effective date of order. Investigation expanded and continued.

D.84683, 7/15/75 - Denied rehearing. Modified D.84527 by exempting property granted variance from D.81443 by D.81987. Effective date of D.84527 is 7/15/75.

D.84858, 9/3/75 - Order Extending Time. Time for compliance with Ordering Paragraph 6 of D.84527, complete test well, extended to 1/31/76, and commencement of monthly monitoring reports, extended to 2/29/76.

Examiner's Ruling, 10/8/75 - Examiner rules that Begonia Iron Removal Plant and Canada de la Segunda Pipeline projects are not emergency projects, that Cal-Am is proponent of the projects and shall pay deposit required at or before filing EDS.

Examiner's Ruling, 12/1/75 - Denies supplemental motion filed 10/2/75 by Cal-Am asking Commission determination that Begonia Iron Removal Plant and Begonia well are not subject to provisions of CEQA.

D.85409, 2/3/76 - Third Interim Order. Petition of Mayors of Peninsula cities that ban on new water service connections to lots of record be lifted subject to city's control of connections. Denied.

Examiner's Ruling, 5/6/76 - Denies motion filed 4/1/76 by Cal-Am that Commission make a finding and decision that Cal-Am's Canada pipeline and Begonia plant projects will not have a significant effect on the environment and that there be prepared a "Negative Declaration" rather than an Environmental Impact Report.

D.86042, 6/29/76 - Order Extending Time. Time for compliance by Commission staff with Ordering Paragraph 10 of D.84527 re reports extended to 8/13/76.

D.86051, 7/2/76 - Fourth Interim Order. Initiates water rationing by Cal-Am in Monterey District, in 3 restrictive phases, triggered by available supply in distribution reservoirs, Phase 1, effective 7/2/76.

D.86267, 8/17/76 - Amendment to Order Instituting Investigation naming Water West Corporation as additional respondent.

D.86270, 8/17/76 - Fifth Interim Order. Established water rationing Phase 1/2 to become effective immediately and be effective until further order of the Commission.

D.86747, 12/14/76 - Sixth Interim Order. Changed authorized evening watering hours of 5:00 p.m. to 7:00 p.m. to 4:00 p.m. to 6:00 p.m. Made these hours effective during period of standard time and original hours of 5:00 p.m. to 7:00 p.m. effective during period of daylight saving time.

Status of Related Proceedings
Initiated Since April 3, 1973

D.82394, 1/29/74 - Authorized sale of Monte well and site of approximately 1/6th acre. Well water of poor quality and well not in use except as observation well.

D.85620, 12/30/75 - C.9962. Request by Peter H. Klaussen for water service connection. Denied.

D.86249, 8/17/76 - Authorizes filing of revised rate schedules. Higher rate schedules (except Schedules Nos. BH-1, MO-7, V-9FL, and V-9MC) expire 5/30/77 with extension permitted up to 120 days after effective date of final order concerning EIR. Lower rate schedules to then become effective. Directs rehiring equivalent number of men dismissed for economy reasons in Sweetwater and Coronado Districts. Orders that capital structure shall not have more than 50 percent borrowings from nonaffiliates.

C.10006, filed 11/17/75 - Benn v Cal-Am for water service connection. Submitted 9/3/76.

A.56334, filed 3/18/76 - Miller for order of exemption from provisions of D.84527. Submitted 5/3/76.

C.10083, filed 4/19/76 - Enterprise Cannery Partnership v Cal-Am for water service connection. Off calendar on request of complainants.

C.10088, filed 4/21/76 - Prentice v Cal-Am for water service connection. Pending.

C.10156, filed 8/5/76 - Hughes v Cal-Am for water service connection. Pending.

C.10173, filed 9/15/76 - Urcis v Cal-Am for water service connection. Pending.

Conditions for Service to Lot Owners
of Record Under Ordering Paragraph 4

1. Applications for service under Ordering Paragraph 4 will be accepted only in the following areas: Del Rey Oaks, Seaside, Monterey, Pacific Grove, and the Zone 11 area of the Monterey County Flood Control and Water Conservation District.

2. Applications for other areas in the Monterey District of California-American Water Company will be accepted only after the local governmental agency has enacted a water conservation ordinance acceptable to the Commission. Approval of such ordinances will be by means of a letter from our chief hydraulic engineer.

3. Applicants for water service must sign a declaration with California-American Water Company stating:

   a. Outside landscaping will not be irrigated.

   b. Within 90 days, construction will start on a home in which applicant intends to live.

4. An applicant (including any member of his or her immediate family living under the same premises as the applicant) may receive water service under these provisions only once.

5. Violations of the conditions specified by subparagraph 3.a above shall result in the following penalties:

   a. First violation: Written warning by California-American Water Company that a further violation will result in water restrictions.

   b. Second violation: California-American Water Company shall restrict the customer's water service by inserting a device to reduce the customer's water flow at his meter to that which will flow through a one-eighth inch orifice, and such restriction shall be removed only after a one-week period has elapsed, and upon payment by the customer to California-American Water Company of a $25 reconnection fee.

   c. Subsequent violations: California-American Water Company shall restrict the customer's water service by inserting a device to reduce the customer's water flow at his meter to that which will flow through a one-eighth inch orifice, and such restriction shall be removed only when a thirty-day period has elapsed and the customer pays to California-American Water Company a $25 reconnection fee.

6. Customers receiving service under the conditions set forth in this ordering paragraph who consider themselves to be aggrieved by any action taken or threatened to be taken pursuant to these conditions shall have the right to first petition the Commission staff, and such petition may include a request for interim relief. Any person not satisfied with the decision of the staff, which shall be by a letter from the Executive Director of the Commission, shall then have the right to file a formal complaint with the Commission and may include a request for interim relief. No other action at law or in equity shall accrue against California-American Water Company because of, or as a result of, any matter of thing done or threatened to be done pursuant to the provisions of these conditions.

7. These conditions shall remain in effect until further order of the Commission.

C. 9530 - D. 86807
California-American Water Company

COMMISSIONER WILLIAM SYMONS, JR., Dissenting

The Commission majority presumes to arrogate to itself today the power to interdict payment of dividends by companies under its jurisdiction. This unprecedented step is an illegal and unnecessary act of coercion.

It is unnecessary because facts to date show that California-American Water Company is moving rapidly ahead with plans to construct the needed Canada de la Segunda pipeline and Begonia iron removal plant in conformance with our rate-fixing order of August 13, 1976 (D. 86249). The engineering plans were drawn and submitted. Hearings on the Environmental Impact Report started December 6, 1976 and are currently in progress.

An "argument from necessity" supposedly underlies today's Order. It is based on an appraisal that financing for these projects is not likely, except by diversion of the company profits. No portion of these earnings are to be available for dividends; the idea is to convert them instead to internally generated funds for plant expenditure. This appraisal refuses to take into account further facts known to us -- that the utility has secured a proposed $4,000,000 project construction loan from the Bank of America. (See A. 56936, "Application to Execute Loan Agreement" filed by California-American Water Company with this Commission on December 13, 1976.) The proposed decision approving this loan is before us on the public Agenda for the Commission Conference of January 11, 1977.

Why then, if the scenario of necessity can no longer be maintained, the stubborn push to go forward with this precedent-setting order to prohibit payment of dividends? I believe the answer is precisely this: to set a precedent -- to expand significantly the power of the Commission. Understand that our August 13, 1976 Order was drawn up in a traditional rate-making mode. In order to prod the company, we authorized a 9.2% rate of return systemwide, but if needed progress in construction did not occur, the rate of return would

fall back to 8.6% for all districts (and lower for the Monterey Peninsula District) (D.86249). The facts show California-American Water Company has responded to this order and has made the progress required therein. But having to work in the rate-making mode, even if it proves effective, is chaffing to some at the Commission who believe that they could use further power. However, as the California Supreme Court has reminded us in Pacific Telephone and Telegraph Company vs. Public Utilities Commission, 34 C 2d 822, our regulatory authority is not broad in all areas: it is broad in some areas and specific in others. Referring to the Public Utilities Act, the Court stated, page 827:

> "The act grants to the commission broad regulatory powers, which may conveniently be divided into two classes. The commission has been given broad powers to regulate the relationship of the utility to the consumer; thus it can determine the services that must be provided by the utility and the rates therefor. It has also been given certain specific powers to regulate the manner in which the utility provides the required services to safeguard the utility's ability to serve the public efficiently at reasonable rates; . . ." (Emphasis added)

Thus with regard to rates and services we have broad powers, but as to the manner of provision we have certain specific powers as laid down in statute. Following the Court's analysis, the fact that we are specifically empowered to authorize new stock issues, does not mean the Legislature was giving us total power over stocks and dividends related thereto, nor that we were empowered to divert profits, which we had previously authorized and the utility has earned, from dividends into plant expenditures. While some commissioners may feel, that by virtue of the appointive office they hold, they are on the board of directors of every public utility in the state, this is not the law. Nor will be so until these companies are made state corporations.

Equally repugnant is the improper confiscation of property inherent in this act, but it is not necessary to rely on this point, given that the ban on dividends is defective as unjustified by necessity and unauthorized by statute.

San Francisco, California
January 5, 1977

William Symons, Jr.
WILLIAM SYMONS, JR.
Commissioner

C. 9530 - D. 86807
California-American Water Company

COMMISSIONER VERNON L. STURGEON, Concurring in Part and Dissenting in Part

I concur with the rationale, purposes and objectives of this decision. I dissent, however, to the "modus operandi." Precluding the payment of dividends, I feel, is unlawful, unnecessary and counterproductive.

San Francisco, California
January 5, 1977

Vernon L. Sturgeon
VERNON L. STURGEON
Commissioner