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ORIGINAL

Decision No. 88127 NOV 22 1977

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of NORTH LOS ALTOS
WATER COMPANY to increase its
rates and charges for its water
system serving portions of the
Cities of Los Altos and Mountain
View in Santa Clara County.

Application No. 55471
(Filed January 30, 1975)

John H. Engel, Attorney at Law, for applicant.
M. E. Densmore, for C.R.E.W., protestant.
Mary Carlos, Attorney at Law, for the Commission
staff.

OPINION

North Los Altos Water Company requests an increase in rates for water service designed to increase annual revenues in the test year by approximately \$99,000 over the rates now in effect.

Public hearings were held before Examiner Daly at Los Altos with the matter being submitted on December 17, 1976. Copies of the application were served upon interested parties and notice of hearing was published, posted, and mailed in accordance with Commission Rules of Procedure.

On March 26, 1976, applicant filed a petition requesting an interim rate increase pending final determination of the application. The proposed preliminary rates are based upon staff's estimates and recommended rate of return. Applicant contends that it is being deprived of urgently needed rate relief and requires an increase pending final order of the Commission.

The petition fails to state facts of an emergency nature justifying an interim increase. The petition for an interim increase is denied.

Applicant is a wholly owned subsidiary of Citizens Utilities Company (Citizens-Delaware), which operates and/or has subsidiary utility companies providing gas, electric, telephone, water, and wastewater services in more than 500 communities in the United States. The headquarters of Citizens-Delaware is located at High Ridge Park, Stamford, Connecticut. Services, including general management and supervision, engineering, accounting, financial, legal, and others, are performed in Stamford, Connecticut, by Citizens-Delaware for its subsidiaries. Certain management and supervising, accounting, billing, and other reporting services for Citizens Utilities Company of California (Citizens-California), and its California affiliates, including applicant, are performed at an administrative office in Redding, California. In addition, certain plants in the Sacramento office of Citizens-California are used for the common benefit of all water operations of affiliated water companies in California.

Applicant is presently engaged in providing public utility water service for approximately 1,354 active meter service connections, 16 private fire connections, and 145 public fire hydrant connections within the adjacent cities of Los Altos and Mountain View in Santa Clara County.

The water facilities include 15 deep wells that range in production from 37 to 400 gallons per minute, with a combined output of 2,529 gallons per minute. Storage is provided in nine tanks with a combined capability of approximately 1,525,000 gallons. As of December 1974, there were about 109,892 feet of distribution main ranging from 1 to 8 inches in diameter. Local operations are conducted from its office in Los Altos, where applicant employs one clerk, one serviceman, and a local representative in addition to the district manager.

Rates

Applicant proposes to increase rates as indicated by the following comparisons of present and proposed rates:

ANNUAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

Portions of Los Altos and vicinity, Santa Clara County.

RATES

	<u>Per Meter Per Month Present*</u>	<u>Per Meter Per Month Proposed</u>
Quantity Rates:		
First 600 cu.ft. or less	\$ 6.46	\$ 8.72
Next 2,400 cu.ft., per 100 cu.ft.66	.891
Over 3,000 cu.ft., per 100 cu.ft.47	.645
Minimum Charge:		
For 5/8 x 3/4-inch meter	\$ 6.46	\$ 8.72
For 3/4-inch meter	8.70	11.75
For 1-inch meter	13.50	18.25
For 1-1/2-inch meter	23.00	31.00
For 2-inch meter	35.00	47.25
For 3-inch meter	75.00	101.25

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

*When application was filed.

PUBLIC FIRE HYDRANT SERVICEAPPLICABILITY

Applicable to all fire hydrant service furnished to duly organized or incorporated fire districts or other political subdivisions of the State.

TERRITORY

A portion of the city of Los Altos, and adjacent unincorporated territory, Santa Clara County.

RATES

Present Rates
Per Hydrant Per Month
Diameter of Main Supplying Hydrant

<u>Type of Hydrant</u>	<u>Size of Connection</u>	<u>Smaller Than 4-Inch</u>	<u>4-Inch and Less Than 6-Inch</u>	<u>6-Inch And Larger</u>
Wharfhead	2½-inch	\$1.50	\$1.75	\$2.00
Wharfhead	3-inch	1.75	2.00	2.25
Standard	4-inch	-	2.50	3.00
Standard	6-inch	-	3.00	3.50

Proposed Rates
Per Hydrant Per Month
Diameter of Main Supplying Hydrant

<u>Type of Hydrant</u>	<u>Size of Connection</u>	<u>Smaller Than 4-Inch</u>	<u>4-Inch and Less Than 6-Inch</u>	<u>6-Inch And Larger</u>
Wharfhead	2½-inch	\$2.05	\$2.35	\$2.70
Wharfhead	3-inch	2.35	2.70	3.05
Standard	4-inch	-	3.40	4.05
Standard	6-inch	-	4.05	4.75

PRIVATE FIRE PROTECTION

APPLICABILITY

Applicable to all water service rendered for private fire protection purposes.

TERRITORY

Portions of the city of Los Altos and adjacent unincorporated territory, Santa Clara County.

RATES

	<u>Per Month</u>	
	<u>Present</u>	<u>Proposed</u>
For each 4-inch connection or smaller	\$ 6.00	\$ 8.10
For each 6-inch connection	9.00	12.15
For each 8-inch connection	12.00	16.20
For each 10-inch connection	25.00	33.75
For each 12-inch connection	35.00	47.25

Service and Quality of Water

Thirty-two public witnesses testified in the proceeding. With the exception of one, all witnesses expressed complaints including hard water, poor quality of water, service problems, and excessive rates.

The major problem relates to the hardness of the water, which requires most of the consumers to bear the additional expense of installing and maintaining water softeners. Various witnesses complained that the water when boiled produced a buildup of a white, sandy substance that coated pots and kettles. One witness, who is affiliated with a large restaurant and motor inn, testified that a

wheelbarrow of the material had recently been removed from one of the industrial water heaters. He not only displayed a small jar of the substance, but he also produced receipts for plumbing costs expended for removal of the substance and damage to facilities resulting therefrom.

Several witnesses testified on their own behalf and also on behalf of an association formed by other water consumers within the service area. The association, known as Citizens For Reasonable Water (CREW), introduced several exhibits and filed a brief in the proceeding.

A study of the North Los Altos system was made and a report thereof was introduced, Exhibit 26, by a civil engineer, representing the California State Department of Health. According to the report applicant has fully met the State Department of Health bacteriological drinking water standards during the past eight years; however, the report indicates that many of the wells do not meet consumer acceptance limits for iron and manganese or the recommended limits of total dissolved solids. According to the report, eight of the wells located in Mountain View produce water with chemical concentrations of iron and manganese in excess of the drinking water standard of .3 milligrams per liter for iron and .05 milligrams per liter for manganese. Analysis of six wells indicated total dissolved solid levels exceeding the recommended consumer acceptance limits of 500 milligrams per liter. The report further indicates that all of the wells, except Van Buren No. 2, Knapp, and Suzanne, are rated low or fair in electrical efficiency as determined by a recent efficiency rating test conducted by Pacific Gas and Electric Company.

The report recommends that:

1. Applicant should discontinue supplying water which contains more than .05 mg/l manganese.
2. Applicant should discontinue supplying water which contains more than .30 mg/l iron.

3. Applicant should institute planning, design, and construction of water treatment facilities needed to provide iron and manganese removal for all well sources producing water containing more than .3 mg/l iron or .05 mg/l manganese.
4. In the absence of providing adequate iron or manganese removal equipment, applicant should discontinue the use of those sources producing water containing iron in excess of .3 mg/l or manganese in excess of .05 mg/l and obtain water from other sources which meet all of the standards of the California Department of Health.
5. Applicant should mix or blend its well supplies containing levels of dissolved solids exceeding the recommended consumer acceptance limit for total dissolved solids with other supplies lower in dissolved solids. The blended water should contain less than 500 mg/l as total dissolved solids.
6. Applicant should arrange for interconnection with nearby water supplies.
7. Applicant should abandon or place on standby service the following wells because they either fail to meet state drinking water standards or are low in water yield as rated by the Pacific Gas and Electric Company: (1) Ramona #2, (2) Portola, (3) Cutter, and (4) Stevens.

The staff concurs in the recommendation of the Department of Health.

A summary of earnings for test year 1976 by applicant and staff is as follows:

SUMMARY OF EARNINGS 1976

<u>Item</u>	<u>Applicant</u>		<u>Staff^{1/}</u>	
	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Present Rates</u>	<u>Proposed Rates</u>
	(Dollars in Thousands)			
Operating Revenues	\$ 301.9	\$ 408.7	\$309.7	\$408.7
<u>Operating Expenses</u>				
Operation & Main.	\$ 114.2	\$ 116.9	\$111.2	\$111.5
Admin. & Gen.	36.5	41.2	25.0	25.0
Taxes Other Than Income	32.0	33.6	29.7	29.7
Depreciation	36.0	34.7	29.8	29.8
Income Tax	18.8	76.5	39.1	91.1
Total Expenses	\$ 237.5	\$ 302.9	\$234.8	\$287.1*
Net Operating Revenues	\$ 64.4	\$ 105.8	\$ 74.9	\$121.6*
Depreciated Rate Base	\$1,075.6	\$1,037.4	\$968.0	\$968.0
Rate of Return	5.99%	10.20%	7.74%	12.56%

^{1/} The staff's estimates for present and proposed rates reflect the amended figures set forth in Exhibit 29, which eliminates the Ramona, Portola, Cutter, and Stevens wells from rate base and reduces power costs for pumping.

* Corrected.

Rate Base

Applicant estimated rate base at \$1,037,400 and staff estimated it at \$968,800.

The following is a summary of applicant's and staff's estimates of average rate base for the test year 1976:

<u>Item</u>	<u>Applicant</u>	<u>Applicant Exceeds Staff</u>	
	(Dollars in Thousands)		
Utility Plant in Service	\$1,389.5	\$1,350.3	\$ 39.2
Reserve for Depreciation	(362.4)	(348.4)	(14.0)
Net Plant in Service	<u>1,027.1</u>	<u>1,001.9</u>	<u>25.2</u>
Common Plant	6.2	6.2	-
Materials and Supplies	8.5	3.4	5.1
Working Cash	47.0	23.3	23.7
Minimum Bank Balances	13.8	-	13.8
Non-Interest Bearing CWIP	1.9	.6	1.3
Advances for Construction	(50.9)	(50.9)	-
Contributions in Aid of Construction	(5.8)	(5.8)	-
Reserve for Deferred Income Taxes	<u>(10.4)</u>	<u>(9.9)</u>	<u>(.5)</u>
Average Rate Base	1,037.4	968.8	68.6

(Red Figure)

Utility Plant

On considering utility plant, the staff excluded the Wilkie pump station because it has not been used since 1972. Applicant contends that the Wilkie well is in operable condition and is in a standby status in the event of an emergency. As of December 1975, the station was valued at \$20,631.

Applicant estimated its 1976 construction program at \$50,000, but the staff excluded \$24,500 for replacement of the Alvarado tank because the item was not listed by applicant on its 4-2M Sheet filed with the Commission in March 1976. Applicant claims that individual projects are not normally entered on the 4-2M Sheet until some expenditures are made with respect to them. It contends that the existing tank at Alvarado is a wood structure which has

deteriorated to the point where it must be replaced and replacement is scheduled after the summer peak demand. According to applicant, a low bid of \$11,300 has been received and such amount should be included in the rate base.

The Wilkie pump station will be excluded and the amount of \$11,300 for replacement of the Alvarado storage tank will be included in rate base.

In concurring with the recommendations of the California State Department of Health, the staff amended its estimate of rate base by late-filed Exhibit 29. The amendment reflects the elimination of the Ramona #2, Portola, Cutter, and Stevens wells which had a book value of \$36,300 as of December 31, 1975. Applicant argues against the elimination of these wells from rate base claiming that while there is some indication that the water produced from these wells may in some respects, and on some occasions, exceed aesthetic water standards, the effect upon water delivered by the distribution system is nonexistent or minimal. Applicant contends that the wells are needed on a standby or peaking basis and their use on that basis complies with the recommendations of the State Department of Health, and that since these wells are used and useful in rendering public utility service, they should be included in the rate base.

Until applicant can demonstrate to the satisfaction of this Commission, an improvement in the quality of water produced and the operational efficiency of these wells, they will be excluded from rate base.

Material and Supplies

Applicant estimates materials and supplies at \$8,500 and the staff at \$3,400. Applicant claims that its estimate reflects 50 percent of the three-year average of the actual materials and supplies inventory. Applicant originally estimated

materials and supplies for 1976 at \$10,800, but apparently this included supplies held for the Felton and Montara affiliates.

The staff's estimate was based on \$2.47 per customer, which the staff and this Commission believe is a reasonable amount for a water system of 1,354 customers.

Working Cash

Applicant's estimate for working cash of \$47,000 exceeds that of the staff by \$23,700.

Originally applicant and staff computed working cash by using the simplified basis prescribed by Standard Practice U-16. Thereafter, applicant revised its estimate from \$28,100 to \$47,000 by use of a lead-lag days study, which applicant claims is more accurate.

The staff method following Standard Practice U-16 was adopted as reasonable in Decision No. 83610 dated October 16, 1974 in Application No. 54323 (Washington Water and Light Co.). The staff's estimate will be accepted.

Minimum Bank Balances

Applicant included \$13,800 for compensating minimum bank balances in test year 1976 rate base.

Applicant argues that the effect of maintaining such compensatory bank balances is that the borrower pays interest on the total amount of a particular loan, but actually has the use of a lesser amount, the balance being maintained in its account with the bank. According to applicant, its compensatory bank balances carry a legitimate cost; and since they are not included in the working computations, nor in the cost of capital, it is necessary to make allowances for them in rate base.

Applicant does not itself make any short-term borrowings. The balances are not directly related to the day-to-day activities of the applicant. The same disallowances were applied in Decision No. 76996 dated March 24, 1970 in Application No. 48905 (Guerneville

District), Decision No. 79915 dated April 4, 1972 in Application No. 52161 (Larkfield Water Company), and Decision No. 83610 dated October 16, 1974 in Application No. 54323 (Washington Water and Light Co.). The Commission's prior position will be followed and no minimum bank balance will be included.

Noninterest Bearing CWIP

The difference of \$1,300 between applicant's and staff's estimates results from the staff's use of a lower level of construction. Similarly the \$500 difference between the staff and applicant in the reserve for deferred taxes primarily results from the difference in the level of construction. We will adopt the staff's estimate.

Rate base in the amount of \$979,300 is reasonable and will be adopted.

Operating Revenues

Both applicant and staff estimate operating revenues of \$408,700 at proposed rates for test year 1976.

Applicant's estimate of 259.0 Ccf per average customer was accepted by the staff as reasonable. The staff's gross revenues at present rates are greater than applicant's because the staff used the rates placed in effect by Decision No. 84589, effective July 19, 1975, whereas applicant used the rates placed in effect by Advice Letter No. 27, effective July 7, 1974.

Operating Expenses

The summary of earnings indicates a difference of \$5,400 in operating and maintenance expense estimates for 1976. The following tabulation sets forth the detailed estimates of applicant and staff:

<u>O & M Expenses</u>	<u>Applicant</u>	<u>Staff</u>	<u>Applicant Exceeds Staff</u>
Salaries	\$ 30.1	\$ 30.1	\$ -
Purchased Power	26.4	22.4	4.0
Ground Water Charges	34.8	34.8	-
Materials, Serv., & Misc.	9.7	8.3	1.4
Customers Acctg. & Misc.	6.9	6.9	-
Transportation	5.2	5.2	-
Telephone & Telegraph	1.3	1.3	-
Uncollectible Accounts	1.2	1.2	-
Rental of Well Sites	1.3	1.3	-
Total	116.9	111.5	5.4

When the staff first made its presentation, its estimate of O & M expenses, as set forth in Exhibit 19, was exactly the same as applicant's, i.e., \$116,900. As the result of the findings and recommendations of the State Department of Health, the staff filed Exhibit 29, which reduced those expenses by \$5,400. Reductions in the purchased power and materials, service, and miscellaneous accounts reflect savings that would result from the elimination of the four-well sites and expected improvements in plant efficiencies.

Staff's estimate of O & M expenses, with reduced adjustment for purchased power, will be accepted and increased by \$3,700 for electric rate increases to August 27, 1976 by PG&E and the city of Palo Alto.

Administrative and General Expenses
(Dollars in Thousands)

<u>Item</u>	<u>Applicant</u>	<u>Staff</u>	<u>Applicant Exceeds Staff</u>
Administrative Office	\$17.5	\$ 9.9	\$ 7.6
Common Plant Expense	3.2	2.0	1.2
Legal and Regulatory Expense	7.3	2.3	5.0
Insurance	.3	.3	-
Injuries and Damages	2.4	2.4	-
Welfare and Pensions	10.0	7.6	2.4
Miscellaneous and Per Diem	.5	.5	-
Total	41.2	25.0	16.2

The first two items relate to the previously described allocated costs and expenses that were allocated by the parent company to its California subsidiaries. The allocation of these expenses was considered at length and determined in Decision No. 87609 dated July 19, 1977 in Application No. 55430 (Jackson Water Works, Inc.).

Per Decision No. 87609 the total allocation to all California operations of the Redding and Stamford mutual service accounts was \$465,000 of which 2.13 percent or \$9,904 was allocated to applicant. The total allocation to all California operations of Sacramento common utility plant was \$33,400 of which 5.95 percent or \$1,987 was allocated to applicant.

All of the exhibits pertaining to the allocation of these expenses were introduced in the Jackson Water Works, Inc. proceeding and were also introduced and received in this proceeding. By stipulation, all testimony introduced in the Jackson Water Works, Inc. proceeding relating to these exhibits was incorporated by reference in this proceeding. We, therefore, adopt the estimate of \$9,904 for Administrative Office Expense and the estimate of \$1,987 for Common Plant Expense.

Staff's estimate of \$2,300 for legal and regulatory expenses is \$5,000 less than applicant's estimate of \$7,300. Because applicant used house counsel, the staff excluded all attorneys' fees and salaries of Stamford, Redding, and Sacramento personnel who participated in its preparation of this proceeding. Staff considered those costs as part of the allocated expenses. Applicant's estimate included direct costs for such personnel, claiming it was in conformity with recommendations made by the Commission's Finance Division as set forth in Exhibit 21. The recommendations, which relate to the allocation of Stamford, Redding,

and Sacramento expenses; are intended for future proceedings. The purpose of these recommendations is to establish accounting procedures whereby accurate records will be available which will facilitate the future direct assignment of as many mutual service expenses as possible. These procedures are not presently in effect nor are accurate records for making direct assignments of cost presently available.

With regard to these accounting procedures recommended by the Commission's Finance Division it should be noted that Ordering Paragraphs 3 and 4 of Decision No. 87609 dated July 19, 1977 in Application No. 55430 (Jackson Water Works, Inc.) read as follows:

- "3. All cost accounting procedures of the administrative and office costs and expenses that are allocated by Citizens Utilities Company (Citizens-Delaware) to its California subsidiaries, including applicant herein, shall conform to the staff recommendations set forth in Exhibit 17.
- "4. Failure to conform to the staff recommendations set forth in Exhibit 17 will result in disallowance of all administrative and office expenses that are allocated to the California subsidiaries of Citizens-Delaware effective one year from the date of this order."

Applicant herein is clearly one of the California subsidiaries referred to and as such is put on notice that the above order is still operative and will be applied to this district by this order.

Applicant also included an amount of \$5,400 per year for three years to amortize the cost of a prior rate case. In Decision No. 82376 dated January 22, 1974, applicant was allowed legal and regulatory expense of \$6,300 to be amortized over a three-year period. The year 1976 would be the last year in which this amount would be

included. Staff therefore amortized this \$2,100 over a four-year period at a rate of \$525 per year along with the four-year amortization at the rate of \$1,000 per year for the estimated reasonable costs of the present rate case.

Staff also excluded applicant's claim of \$960 for outside counsel for the purpose of preparation and review of the applications, exhibits, and other petitions filed in this proceeding. This proceeding presented no extraordinary legal issues justifying the use of outside counsel for which the ratepayer should bear the burden. Staff's estimate is reasonable and will be accepted.

Management Study Expense (Regulatory Expense)

Pursuant to an order issued by Commissioner Robert Batinovich, Citizens Utilities Company contracted for a management study, the results of which were the subject of Decision No. 87608 dated July 19, 1977. Decision No. 87608, as amended by Decision No. 87776, authorized \$23,900 for the cost of the study to be allocated among the ten California subsidiaries of Citizens-Delaware over five years. Of the total cost 6.23 percent or \$298 was allocated to applicant.

We, therefore, adopt the estimate of \$298 for Management Study Expense. No adjustment has been made in the previous tables on the required revenues in this proceeding since the amount is small and the time involved in making such adjustments would delay this matter further. However, the amount will be offset against a recalculated deferred tax account as discussed, supra, under income taxes.

Applicant's estimate of \$10,000 for welfare and pension expenses is \$2,400 more than the staff's estimate. This is primarily attributable to the lower salary estimates for Stamford, Redding, and Sacramento. It is also attributable to the fact that the staff excluded expenses related to the Employee Efficiency Incentive Fund in accordance

with Decision No. 76996 dated March 24, 1970 in Application No. 48908 (Guerneville District). We consider the incentive fund more in the nature of a bonus, the cost of which should be paid for by the stockholders rather than the consumers. Staff's estimate will be accepted.

Taxes Other Than Income

Applicant's estimate of \$33,600 for 1976 is \$3,900 more than the staff's estimate of \$29,700.

Applicant determined the 1976 test year ad valorem taxes to be \$26,700 by the method used by the County Assessor, based upon 1976 present and proposed rates, and added one-third of the difference between them to ad valorem taxes at present rates.

The Santa Clara County Assessor uses a method of determining ad valorem taxes which is based upon capitalization of earnings and historical cost. Applicant contends, therefore, that the increase in earnings due to the proposed rate increase, and the amount of 1976 construction, will result in higher ad valorem taxes in the future. Applicant argues that since rates are set for the future, the impact of the increased rates and construction on ad valorem taxes should be reflected in the test year in order to match expenses and revenues for the period the rates will be in effect.

Staff used present rates to compute capitalized income valuation. Staff contends that since the ad valorem taxes for the 1976 test year will be computed using 1975 revenues and since the Commission has held that tax expense should reflect as nearly as possible the actual taxes paid during the test year, applicant's use of proposed rates is without merit and should be rejected (Decision No. 79915 dated April 4, 1972 in Application No. 52161, Larkfield Water Company).

We agree that ad valorem taxes should be determined on the basis of taxes actually paid during the test year and for this purpose present rates should be used. We will adopt the amount of \$30,800 as reasonable for total taxes other than income.

Depreciation

The difference between applicant and the staff in depreciation is primarily due to the staff's lower estimate of construction and its removal of the Wilkie, Ramona #2, Portola, Cutter, and Stevens wells. The amount of \$31,500 will be adopted as reasonable for this proceeding.

Income Taxes

The difference between applicant and the staff in income taxes is primarily due to different estimates of expenses.

Both applicant and staff followed the same procedures for determining tax depreciation; straight-line for federal taxes, and liberalized on a flow-through basis for state taxes.

The staff recommended that, pending the outcome of the rehearing of Applications Nos. 51774 (The Pacific Telephone and Telegraph Company) and 51904 (General Telephone Company of California) relating to the ratemaking treatment of federal income tax depreciation and investment tax credit, applicant be ordered to maintain its customer records as may be appropriate to implement customer refunds if the method of determining tax depreciation prescribed by the Commission in those proceedings differs from the method used by staff and applicant in this proceeding.

The Commission has now issued its decision in those matters (Decision No. 87838 dated September 13, 1977). Among other things, the Commission found:

"Under the normalization method we are adopting for ratemaking purposes, tax depreciation expense for ratemaking purposes will be computed on a straight-line basis while federal taxes will be computed on an accelerated depreciation basis. The difference between the two tax computations will be accounted for in a deferred tax reserve. The average sum of the test year deferred tax reserve and the deferred tax reserve for the three next subsequent years shall be deducted from rate base in the test year. As a result of each of the deductions from rate base federal tax expense will be recomputed on the same basis in the test year for the test year and the three corresponding subsequent years, thus matching the estimated tax deferral amount for each period with the estimated federal tax expense for the same period. This method complies with Treasury Regulation 1.167(l) - (l) (h) (6) and is normalization accounting." (Mimeo. page 48.)

No adjustment has been made in the deferred tax reserve or in the required revenues in this proceeding since the amount involved would be small and the time involved in making such adjustments would delay this matter further. The amount by which revenues would be decreased due to a recalculation is made even smaller by an offset of \$298 for the management study expense discussed, infra.

Applicant is placed on notice, however, that the treatment of tax depreciation and investment tax credit found reasonable in Decision No. 87838 will be applied in all future rate proceedings for all subsidiaries and affiliates of Citizens-Delaware.

Rate of Return

The applicant contends that a reasonable rate of return would be no less than 12 percent. The staff recommends a 9.00 percent to 9.30 percent rate of return, which would result in a 9.70 percent to 10.18 percent return on equity.^{2/}

^{2/} The rate of return exhibits received in the Jackson Water Works, Inc. proceeding (Application No. 55430) were also received in this proceeding. By stipulation all testimony relating to those exhibits was incorporated by reference in this proceeding.

The staff's recommended rate of return of 9.0 percent on the adopted rate base and a return on common equity of 9.3 percent might be reasonable for applicant if applicant was providing an adequate level of water quality and service. The record in this proceeding, however, clearly demonstrates that applicant's water quality and service are below minimum standards and inadequate.

The last authorized rate of return for applicant was 7.7 percent as determined by Decision No. 82376 dated January 23, 1974. Applicant is presently earning about 7.7 percent, which is reasonable under the circumstances.

In addition, the Commission takes notice of the following recent developments. First, a condemnation suit for applicant's system was filed on September 12, 1977, in the Santa Clara County Superior Court (Case No. P33021) by the Los Altos Community Facilities District No. 1. Second, AB 1881, which essentially prohibits applicant from engaging in any construction, prior to July 1, 1979, was recently signed into law and became effective immediately. (Ch. 801, 1977 Stats.) Under the circumstances the Commission will require applicant to obtain approval from the Executive Director prior to engaging in any construction work which may be exempted by Sec. 2, Ch. 801, 1977 Stats. (AB 1881).^{3/} This condition shall remain in effect until further order of the Commission.

^{3/} Sec. 2 of Ch. 801, 1977 Stats. (AB 1881) provides for an exception where construction work is necessary (1) to extend service to customers, (2) to maintain the existing water system, (3) to meet an emergency, or (4) to protect the health and safety of the public or any portion thereof.

Findings

1. The staff estimates of operating revenues, operating expenses, and rate base for test year 1976 are reasonable.
2. A rate of return of 9.0 percent on the adopted rate base would be reasonable if applicant was providing an adequate level of water service and quality.
3. Applicant's level of water service and quality is inadequate because of high levels of iron, manganese, and dissolved solids content, which have exceeded the limits of consumer acceptance.
4. Applicant's present rates are reasonable under the circumstances.
5. A condemnation proceeding for applicant's system was filed on September 12, 1977, in Santa Clara County Superior Court (Case No. P33021) by the Los Altos Community Facilities District No. 1.
6. AB 1881 (Ch. 801, 1977 Stats.) recently signed into law with an immediate effective date, essentially prohibits applicant from engaging in any construction prior to July 1, 1979.
7. Because of AB 1881 and the pending condemnation suit, applicant will be required to obtain prior approval from the Executive Director before engaging in any construction work which may be exempted by Sec. 2 of Ch. 801, 1977 Stats. (AB 1881) until further order of this Commission.
8. All cost accounting procedures of administrative and office expenses that are allocated by Citizens-Delaware to its California subsidiaries, including applicant herein, shall conform to the staff recommendations set forth as Exhibit 17 in the proceedings in Application No. 55430 of Jackson Water Works, Inc. and previously adopted in Decision No. 87609. Failure to do so will result in disallowance of all administrative and office expenses that are allocated to the California subsidiaries of Citizens-Delaware, effective July 19, 1978.

Conclusion

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

O R D E R

IT IS ORDERED that:

1. Until further order of the Executive Director, North Los Altos Water Company shall obtain Commission approval before engaging in any construction work which may be exempted under Section 2 Chapter 801, 1977 Statutes (AB 1881).

2. Applicant's petition for interim rate relief is denied.

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

Dated at San Francisco, California, this 27th day of NOVEMBER, 1977.

*I will file dissent
William Snows Jr*

I dissent

Vernon L. Sturgeon

Robert Batmang
President

Richard D. ...
... ..
Commissioners